Share Buybacks by Japanese Companies Hit a Record High.

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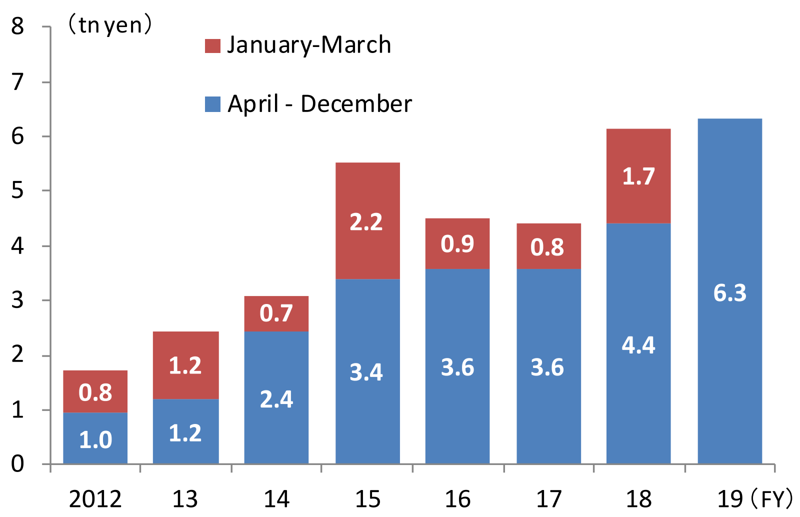
Buybacks in Japan Reached a Record High

Share buybacks by Japanese companies hit a record high. There are two main reasons behind this, uncertainty over the global economy and strengthening of corporate governance.

Share buybacks by Japanese companies are increasing. In the first nine months of this fiscal year, they have already reached to 6.3 trillion yen, exceeding the previous year's total（Figure1）.

The two main reasons for the increase in share buybacks are uncertainty over the global economy and strengthening of corporate governance. As US-China trade friction and geopolitical risks make the economic outlook uncertain, companies have to be cautious about making decisions on capital investment or mergers and acquisitions.

[Figure 1] Share Buybacks in Japan Hit Record High



(Note) The first section of the Tokyo Stock Exchange, Announced Buybacks
(Source) QUICK

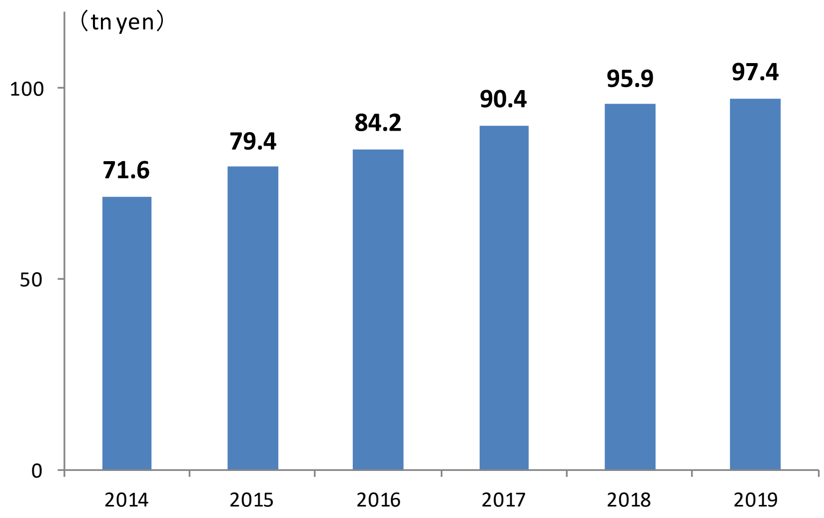
Meanwhile, the Japan's Corporate Governance Code, which was revised in June 2018, strongly urges listed companies to consider the cost of capital in their corporate management. However, cash held by Japanese companies continue rising (Figure 2), there seems to be plenty of room left for Japanese companies to continue the high level of share buybacks.

The amount of cash held by Japanese companies has been increasing, and there is still plenty of room for them to repurchase their own shares.

A number of institutional investors, including asset management companies and insurance companies, have accepted the Japan's Stewardship Code, increasing shareholder pressure on listed companies to make better use of their cash reserves. Under these circumstances, many listed companies believe that using the excess cash effectively for shareholders' needs is inevitable.

This is probably the reason that more companies are repurchasing their own shares. Some companies have even announced their share buybacks that exceed their annual capital expenditures.

[Figure 2] Cash held by Japan-listed companies continue increasing.



(Note) As of January of each year. Approximately 1600 companies in TSE1 that can be obtained data continuously (excluding those belonging to the Financial sector.)

(Source) QUICK

Share Buybacks will likely to increase in order to improve the ROE.

In fiscal year 2019, ROE is expected to deteriorate for two consecutive years due to US-China trade friction and other reasons. That could also boost share buybacks.

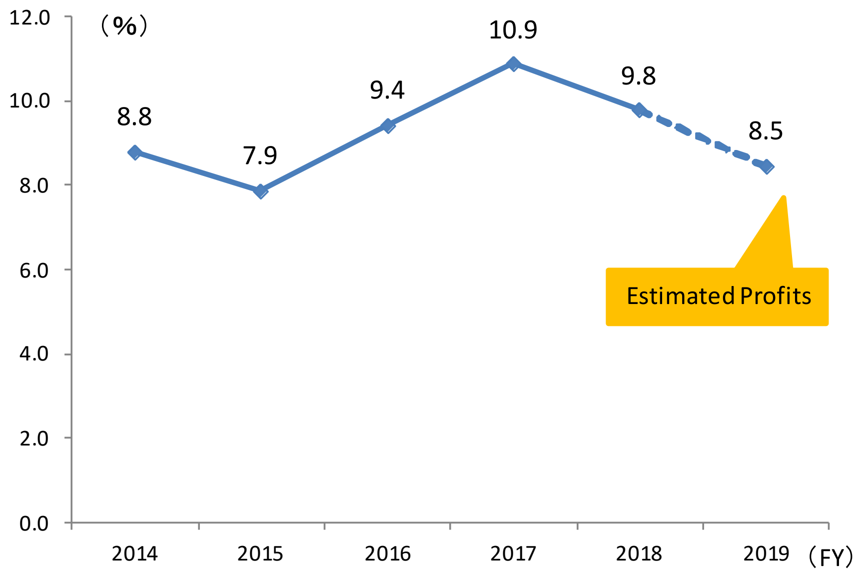
Buybacks may also be aimed at avoiding a deterioration of ROE due to an excessive increase in equity capital. In fiscal year 2019, the ROE of the entire market is expected to deteriorate for two consecutive years due to low profits caused by U.S.-China trade friction and other reasons. (Figure 3).

Out of the 1598 companies surveyed, 885 companies (about 55%) hold more cash compared to a year ago, and 565 of 885 companies (64%) expect a deterioration of their ROE in current financial year.

In recent years, an increasing number of shareholders vote against the election of presidents at general shareholders meeting if the company have low ROE. It appears that not only foreign investors but also domestic investors are urging companies to pay more attention to shareholders' wishes. It is highly likely that this trend will continue.

Especially, cash-rich companies with low ROE and those with high foreign stock ownership ratio are likely to plan the repurchases of their own shares.

[Figure 3] ROE is expected to deteriorate for two consecutive years



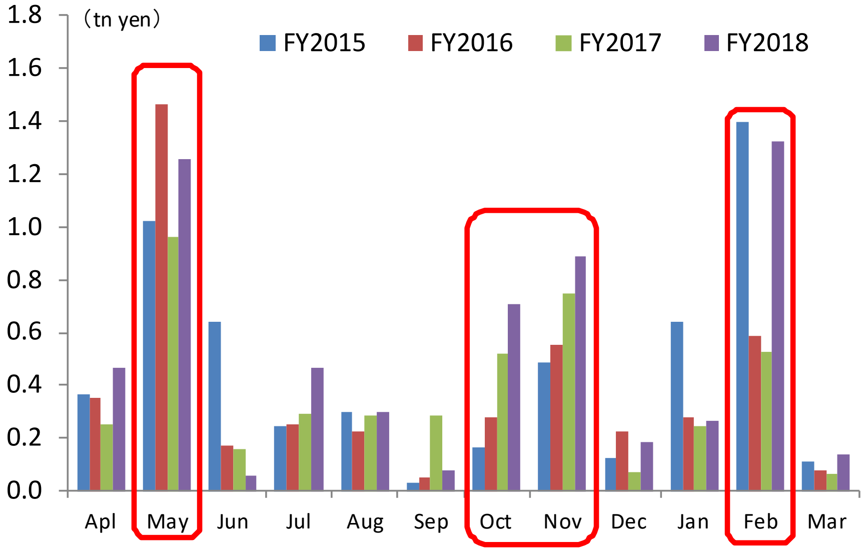
(Note) The estimated net profits are announced by the company (Using QUICK Consensus if not disclosed by the company). Approximately 1600 companies in TSE1 that can be obtained data continuously (excluding those belonging to the financial sector.)
(Source) QUICK

In fact, share buybacks by Japanese companies have seasonality. It tends to increase in May and October to November when full year and interim results are released. Buybacks also increase in February. As the end of the fiscal year is approaching, companies which can have prospects for full year results may announce share buybacks as soon as they release their third quarter earnings (Figure4).

Share buybacks by Japanese companies have seasonality and are expected to support stock prices throughout the year.

As mentioned above, Japanese companies are trying to strengthen the corporate governance and use the excess cash effectively under the pressure by the shareholders. The high levels of share buybacks will continue to support stock prices throughout the year. Improvement of the ROE and capital efficiency are also expected to raise corporate value and boost stock prices.

[Figure 4] Share Buybacks peak three times a year



(Note) The first section of the Tokyo Stock Exchange, Announced Buybacks
(Source) QUICK

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Shingo Ide heads the Japanese equity research team at NLI Research Institute.
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