

## THE JAPANESE RATE OF PROFIT IN Q4 2024. HAS THE JAPANESE ECONOMY REVERTED BACK TO NORMAL?

The Japanese Ministry of Finance recently released data for the fourth quarter of 2023 allowing this article to present the rate of turnover, surplus value, and profit amongst other ratios.

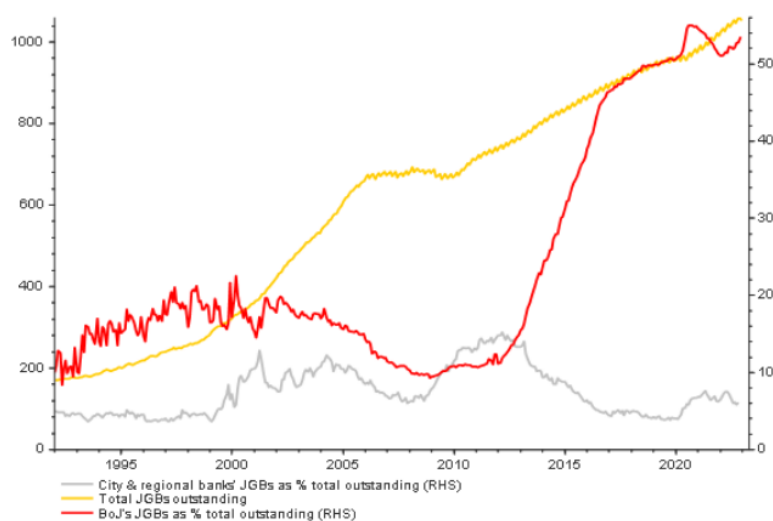
This article is divided into two. The first part deals with two interesting issues. Firstly, for the first time in 16 years the Bank of Japan has raised its interest rate, making it the last major Central Bank to abandon negative interest rates. Secondly, the current Shunto or wage-round will see Japanese wages, at least in the larger corporations, achieve real rises, something the Japanese Finance Ministry has been pushing for.

Japan is special, in that The Bank of Japan owns more government bonds than any other central bank. By the end of 2022, the [BOJ owned over 50%](#) of all outstanding Japanese government bonds, and by the end of 2023 this rose to 54%, at which time it started to taper its bond buying which began in 2013.

### Graph 1.

Figure 1. BoJ holds more than half of Japan's government bonds

JGBs outstanding in ¥tn on left-hand axis, BoJ & domestic banks' % shares on right



Source: Refinitiv Datastream, based on BoJ data

(Source: [OMFIF](#))

*"The Japanese government currently holds the world's largest public debt load at 1,286.45 trillion yen at the end of 2023, nearly twice the size of its economy. There is also the question of the roughly 300 trillion yen that is currently parked overseas by Japanese investors. These investors previously looked abroad to avoid the negative interest rates back home."* (In bold, my correction to the original quote.) However we should note that half the public debt is held by the BOJ. The balance in private hands amounts to 108% of GDP, which is no higher than that found in other countries, and given zero interest rates, is more bearable.

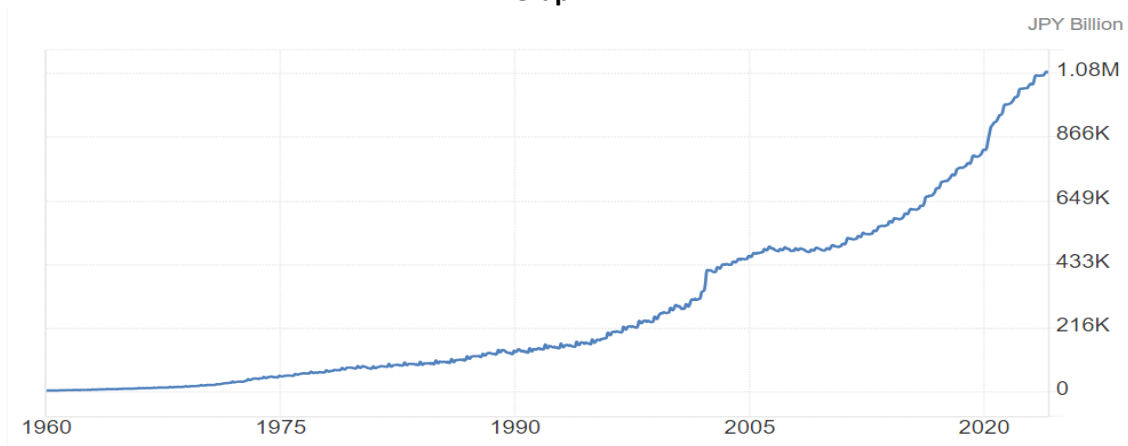
The purpose of buying debt was to counter the deflationary tendencies in the economy. It has been a complete failure, one which could have been anticipated. Throwing money at the rich capitalists who

already are hoarding money makes no sense. It simply does not enter into circulation, that is, it is not used for the purposes of productive or unproductive consumption, it is hoarded either at home or abroad.

All it does is add to the supply of money. It is important to note, that fiscal money in this case differs from credit money as provided by commercial banks. The former is permanent while the latter is temporary as credit always has a term and at term has to be repaid. That is why it is nonsense to claim the banks are the source of money. This claim only holds up if one looks to the creation of loans without including the extinguishing of loans through repayment. On the other hand, fiscal money is only destroyed when the BOJ sell bonds back to private investors taking back their money through what is called Quantitative Tightening, which is the opposite of Quantitative Easing, or QE vs QT.

As we can see this buying of bonds and shares (QE) has elevated the supply of money, in this case M1, and were we to examine M2, even more so, especially since 1995.

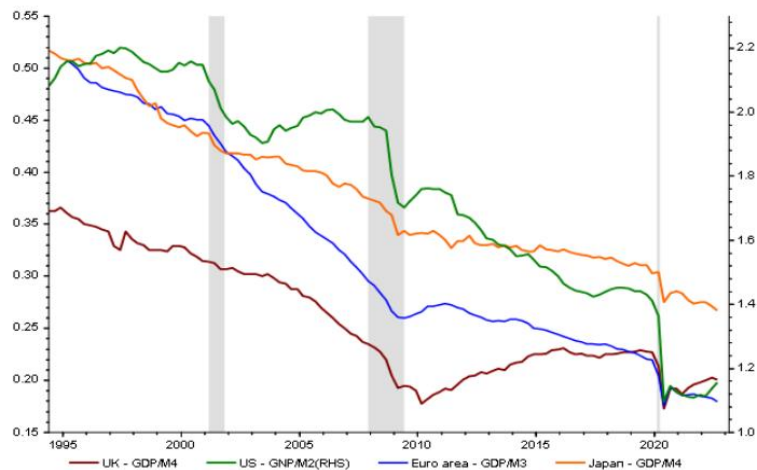
**Graph 2.**



And of course the amount of idle money is best expressed by the velocity of circulation which measures the stock of money against GDP. Graph 3 shows the collapse in the velocity of circulation.

**Graph 3.**

Estimated money velocity: ratios of nominal GDP to broad money supply. Grey is US recession



Source: Refinitiv Datastream

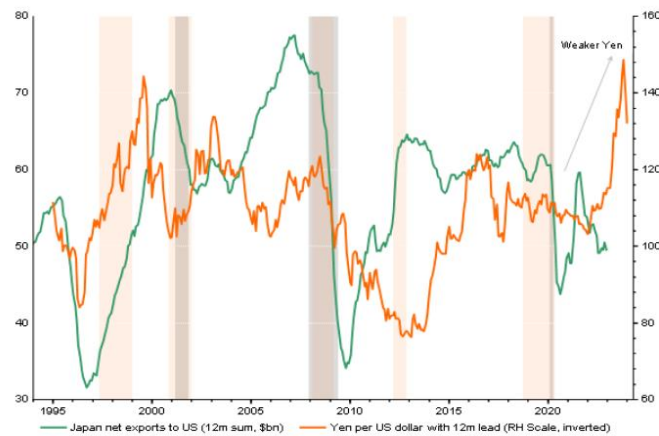
Japan's velocity of circulation was already half that of its major competitors and like its competitors the velocity of circulation has decelerated due to Quantitative Easing and latterly due to the infusion of Covid related support funds. This was particularly true of the US whose provision of Covid funds was the highest.

As most of these additional funds leaked abroad (the famous Japanese carry trade) it necessarily reduced the exchange rate of the Yen as it was used to purchase foreign currency with which to invest, particularly the Dollar and the Euro. At first the fall in the Yen benefited exports in Yen as they were relatively cheaper on world markets. In the graph below we see two peaks, the first prior to the dotcom crash and the second before the financial crash in 2008. Latterly however, thanks to China, the weak currency has not encouraged Japanese exports.

### Graph 4.

Figure 2. Yen weakness, if sustained, offers future trade benefits

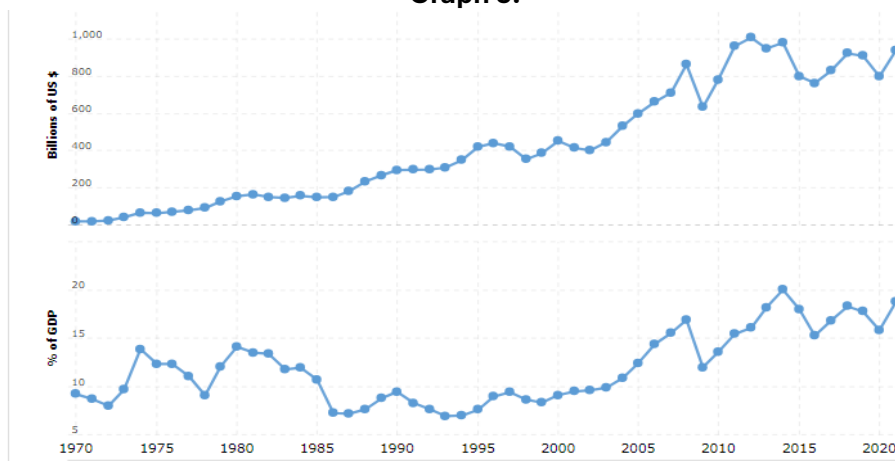
Japan trade surplus with US (rolling 12-month total, \$bn), lagged 1 year, versus \$/¥ on inverted axis. Blocks denote US (grey) and Japan (orange) recessions



Source: Refinitiv Datastream

Imports fared better, but that picture is confounded by the relocation of Japanese industry abroad and consequently the importation of goods previously produced within Japan, both final goods and especially intermediate goods.

### Graph 5.



Thus the net effect of all the BOJ’s quantitative easing was to drive down the value of the Yen and interest rates. But the fall in the Yen did little to raise prices through rising import prices, because import prices were moderated by goods being imported from cheaper producers. The problem remained, lackluster demand. This is the context for the change in emphasis by the BOJ and the Finance Ministry towards pay rises for workers, putting more money into the pockets of the only class that can and must spend it, workers. This is one of the big lessons of the Covid injection of funds, which for the first time was not monopolised by the rich, after all dear, I only have two wrists which means there are only so many Rolexes I can wear, but if I was an octopus....

For the first time it appears they have succeeded. This year’s Shunto or wage negotiations appear to be delivering the desired result. [“With a slew of major firms offering robust pay hikes, “I think it’s almost certain that this year’s \(shuntō wage hike figure\) will be much higher than last year’s,” Kobayashi said. Still, the pace of wage hikes has not kept up with inflation, with Japan’s real wages falling for the 22nd straight month in January. Consumption has also remained weak.”](#) However the article also goes on to add that smaller corporations will not be able to match these wage rises. [“The Japanese Trade Union Confederation, otherwise known as Rengo, announced a huge preliminary wage hike figure of 5.28 per cent, which would actually be a 33-year high, and a huge jump up from the wage raise of 3.58 per cent the previous year.”](#) [The current estimate for the 2024](#) round is 5.28 per cent at a time when inflation is now fallen to low levels again.

**Graph 6.**



We can now proceed to examine Japanese industrial corporations. There we will find a number of graphs examining real employment and compensation trends in greater detail. This data, though confined to industrial and service corporations, gives a better picture of the heart of the Japanese economy.

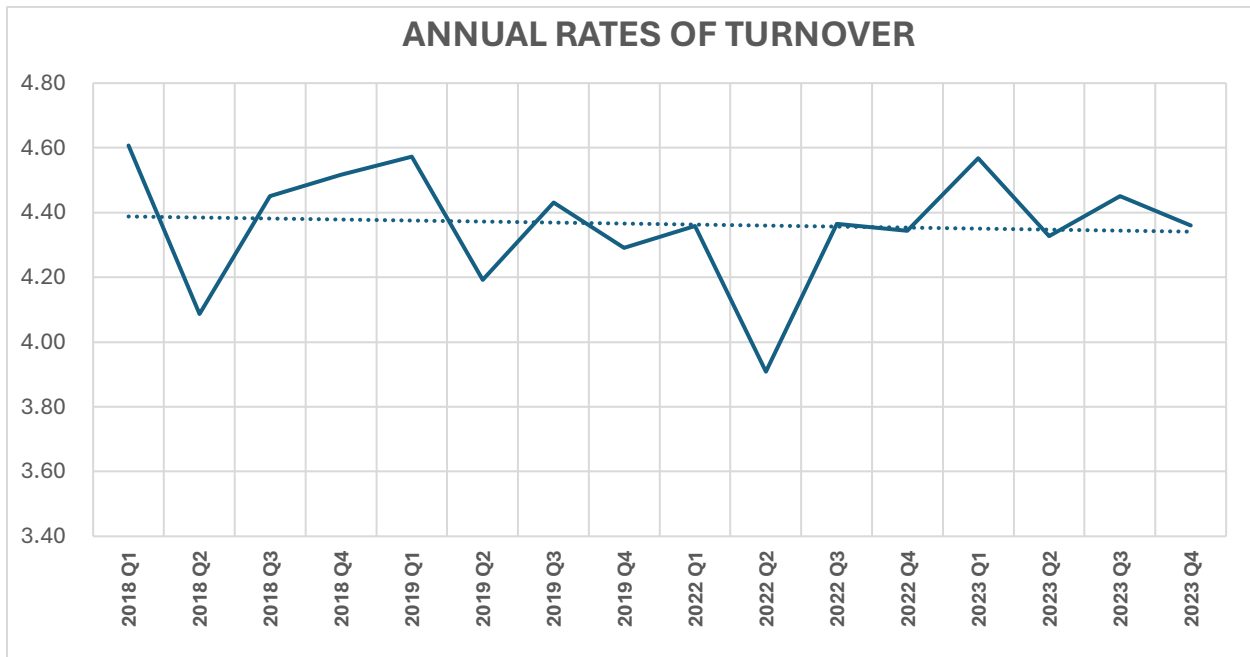
## Industrial corporations.

All data used to compile the graphs below is taken from the [Japanese Ministry of Finance, Policy Research Institute](#). The table providing the main data is Table M1. I have attached a copy of the M1 Table with my calculations in red for information purposes. In addition I have attached a worksheet showing all the transferred data as well as the calculations on which the graphs are based.

The graphs below compare the two years before the pandemic to the two years after the pandemic, in other words the calendar years 2018 & 2019 and 2022 & 2023. I am assuming these 48 months of analysis will be sufficient to establish a trend uncluttered by the peculiar circumstances surrounding the pandemic during 2020 & 2021. Of course there were still be after-effects resulting from the pandemic in 2022 but by 2023 these had cleared up.

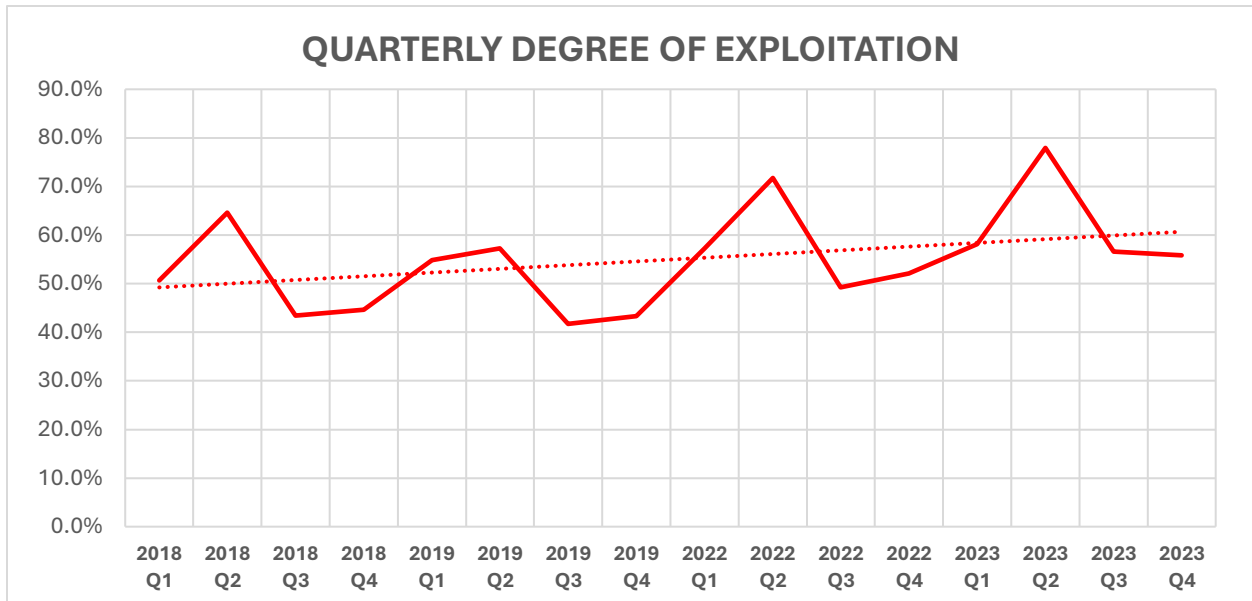
The first graph plots the movement in the rate of turnover which is key to understanding market conditions. Any acceleration tends to denote improving demand therefore improving market conditions, and any deceleration tends to denote deteriorating market conditions. The rate of turnover, despite slowdowns in the second quarter of each year, was more or less stable. The marginally down trend was heavily influenced by Q2 2022.

Graph 7.



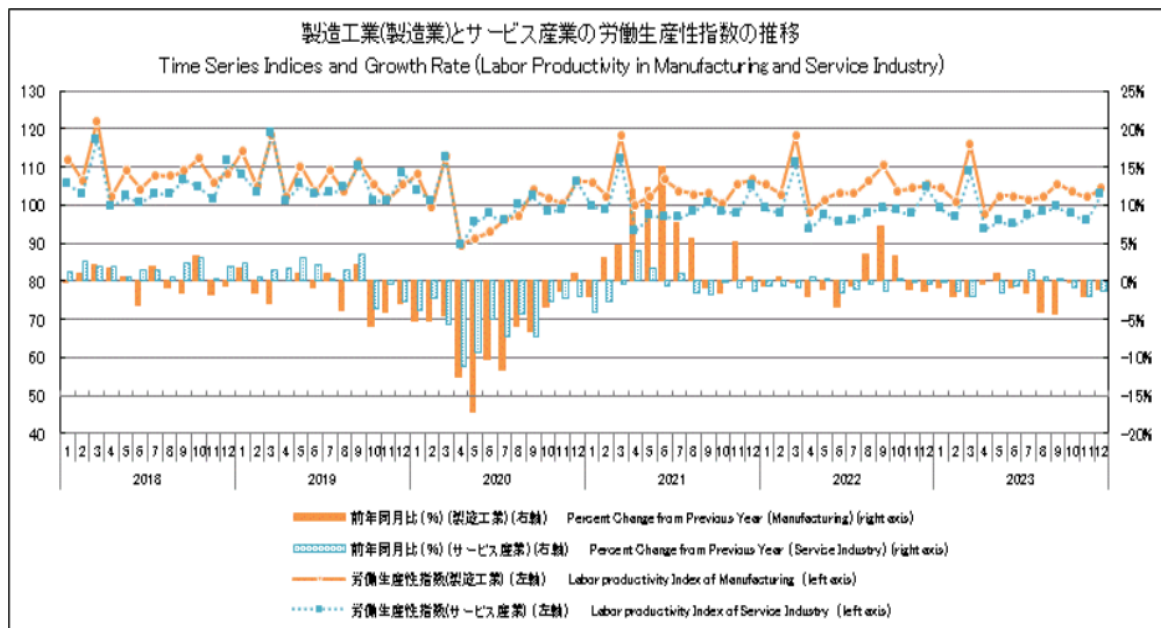
The quarterly degree of exploitation in the graph below is derived through dividing gross profits by worker compensation. The rate of exploitation rose between the two periods, with the results shown in Graph 8 below. (I use the word *degree* rather than the *rate* of exploitation, because this is the term Marx used, and it helps distinguish it from the rate of surplus value which is different, because r.o.s. includes turnover which in turn converts worker compensation into actual variable capital.)

Graph 8.

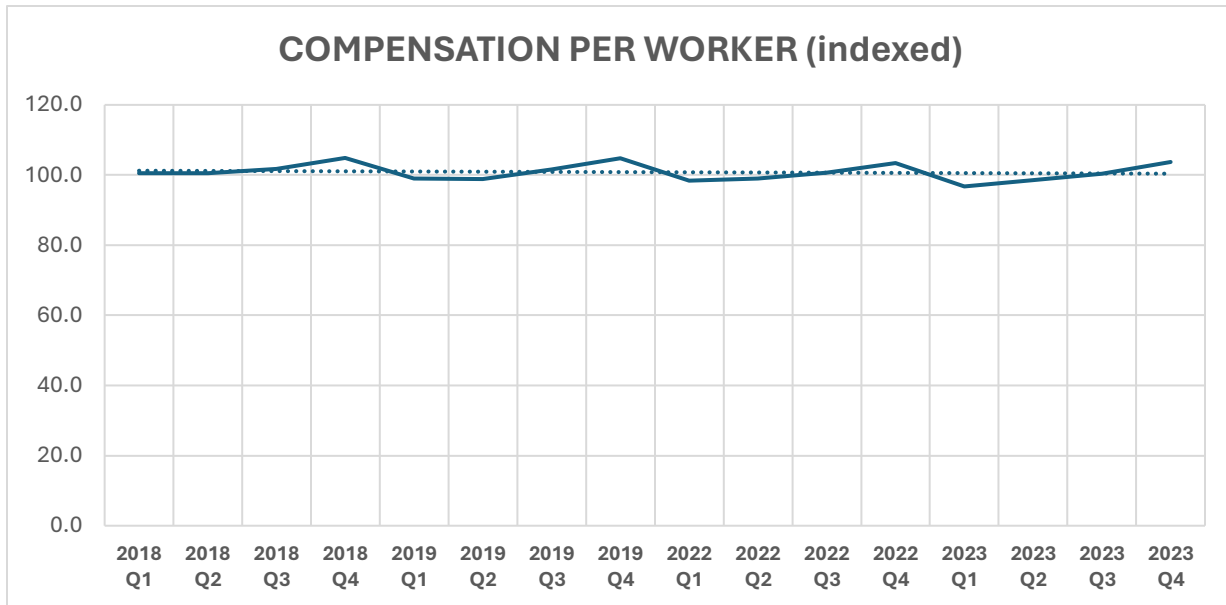


This rise in exploitation was due to real compensation per worker flatlining until the final quarter of 2023. This meant that whatever productivity gains there were, benefitted profits. Stagnant wages was the main driver for the rise in the rate of exploitation at this time. The recent fall from a high of 77.9% down to 55.8% due to rising wages, shows how sensitive the rate of exploitation is to prevailing compensation in the absence of rapid rises in productivity. Changes in productivity can be seen in the graph below taken from the [Japan Productivity Centre](#). Like everything else in Japan, productivity itself has been flatlining.

Graph 9.

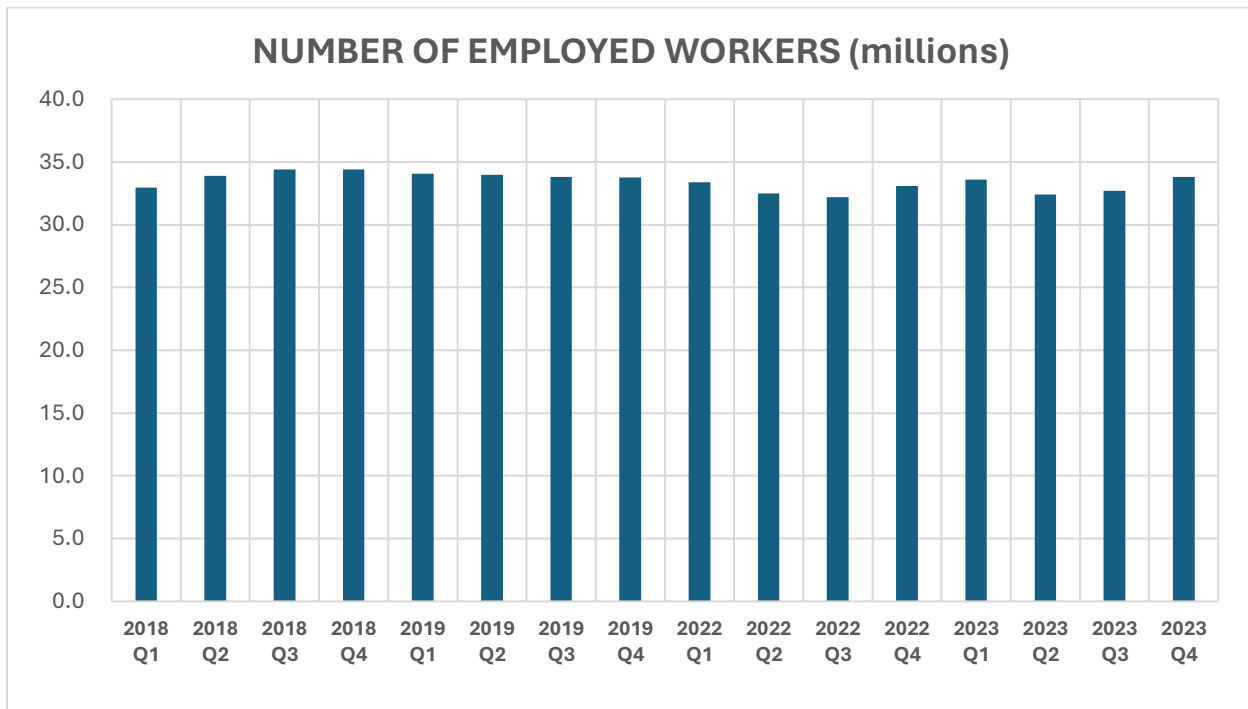


**Graph 10.**



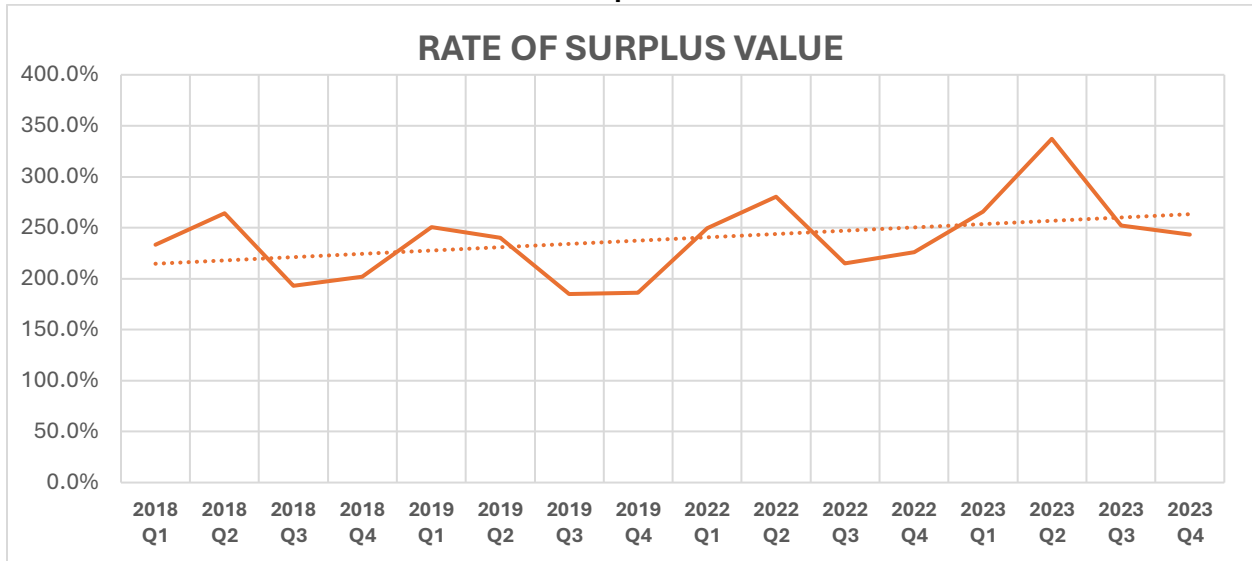
In addition, while compensation flatlined, the total number of workers for the period 2022-2023 was down 0.9 million. This meant that the total compensation bill was reduced except for the final quarter of 2023, and presumably 2024.

**Graph 11.**



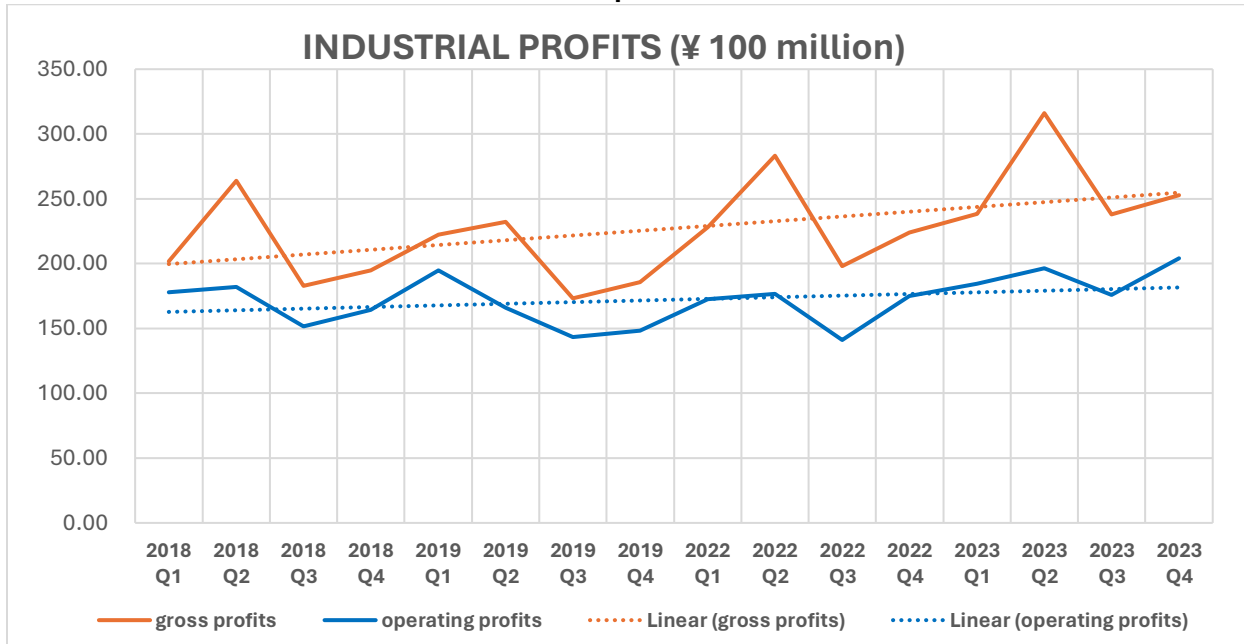
Due to the rate of turnover holding steady, both the trend in the rate of surplus value and the degree of exploitation increased similarly by about 24% from the beginning of 2018 to the end of 2023.

Graph 12.



Due to the rising rate of surplus value, profits increased. There are two graphs below, one denoting gross profits and the other operating profits. Gross profits include interest earned on the cash reserves and liquid assets held by Japanese corporations. These are vast, they amounted to about ¥510 trillion in 2023 or in dollars \$3.63 trillion at an [average exchange rate for 2023 of 140.5](#) Put another way they amounted to 50% of the value of fixed assets. So even if the BOJ did not repress interest rates, these vast hoards, due to a lack of investment in production would have depressed the rate of interest in any case. In the two years pre- the pandemic, nominal quarterly growth in net investment averaged 1% whereas in the post-pandemic period it rose to 1.3%. In real terms however, the post pandemic rise when adjusted for higher inflation meant that real investment was flat. (The [GDP deflator](#) rose by 8.3% over this latter period.)

Graph 13.

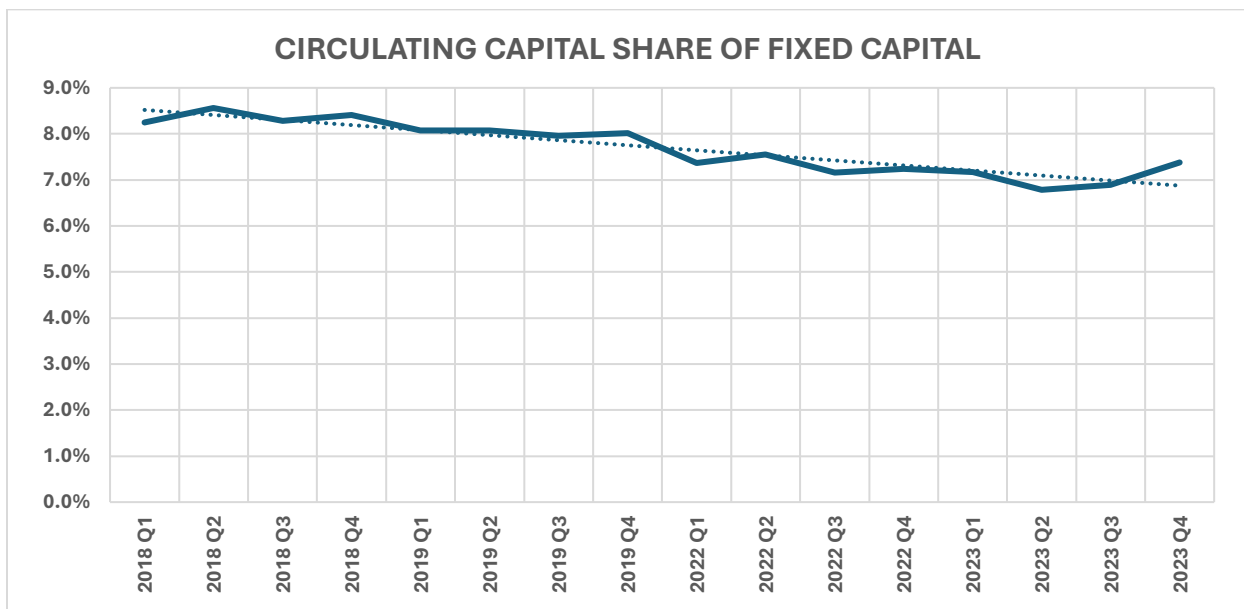




Similarly, the hunt for higher yields meant that Japanese corporations banked their hoards abroad, particularly in US government bonds where Japan is the biggest foreign investor, and in US money market funds. This contributes to our understanding why the Japanese Yen is so undervalued on world markets. Until this outflow of capital is reversed, and this will not happen until interest rates become competitive, the Yen will continue to weaken. This week's marginal rise in BOJ interest rates into positive territory failed to strengthen the Yen, showing how much higher interest rates must go to influence exchange rates.

Having looked at profits on the one side we can now turn to examine the capital side. The graph below measures circulating capital compared to fixed capital. The ratio is much lower than in the USA and closer to that of Germany. This shows that Japan is a more industrialized economy with a higher composition of capital. It is far less dependent on the so called service sector with its lower composition. That said, unlike the USA where employment rose after 2014, reducing the composition of capital, the reverse happened in Japan where the composition rose because of the fall in employment.

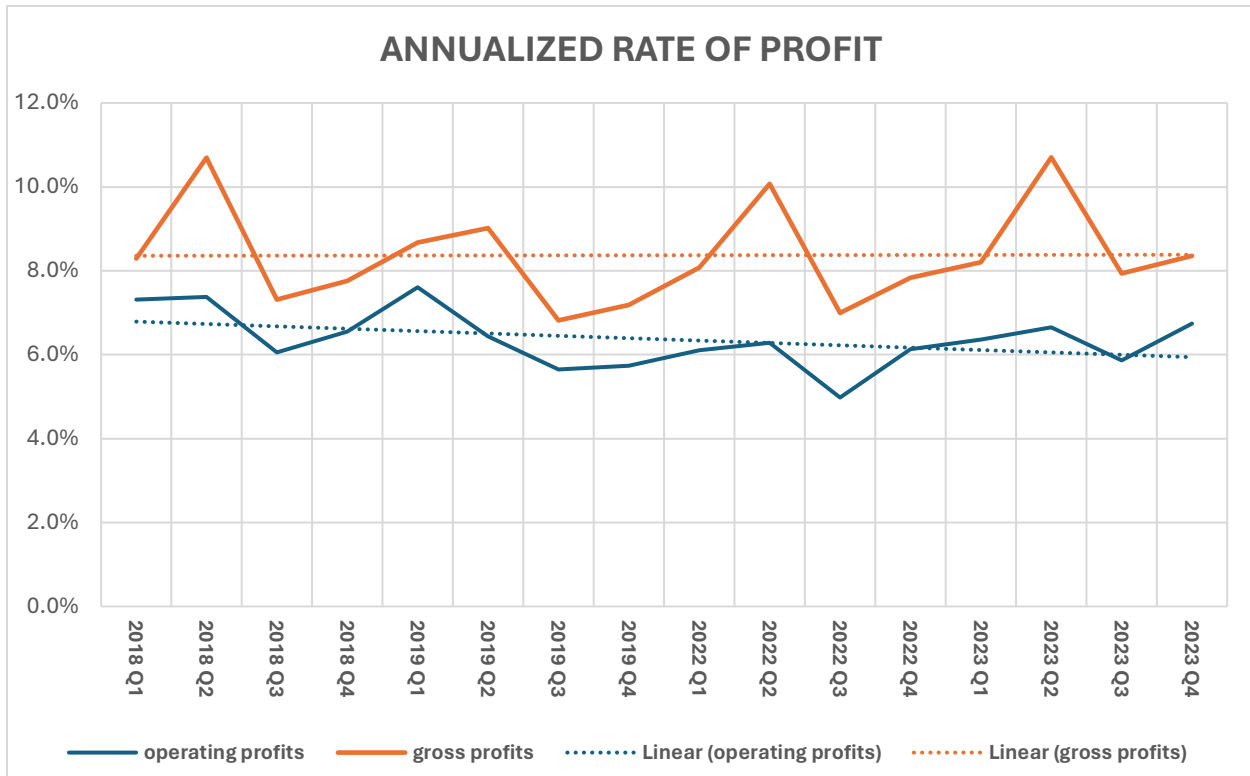
**Graph 14.**



The fall in the relative weight of circulating capital as well as anemic investment has helped to support the rate of profit which can be viewed in the graph below. As expected, the longer term trend is down. The exception being the last quarter, which despite higher compensation, was above trend. When accounting for the income from cash hoards, likely due to them being invested abroad, the gross rate of profit stabilized. (Japanese investors hold \$3 trillion abroad.) Nonetheless the operating profit rate is the more important as it shows how profitable Japanese industry is, not how profitable its financial investments are. No doubt those Marxists who like to overegg the importance of financial capital will be delighted by what they find in Japan.

The rate of profit here is based on both fixed and circulating capital, the best and only denominator yielding an accurate rate of profit. (Given that circulating capital as a share of fixed capital is three times higher in the USA compared to Japan, were we to exclude it, we would diminish the amount of capital more in the USA than in Japan. Accordingly a higher rate of profit would emerge artificially in the USA. For this reason it would be impossible to compare profitability between the two countries.)

Graph 15.



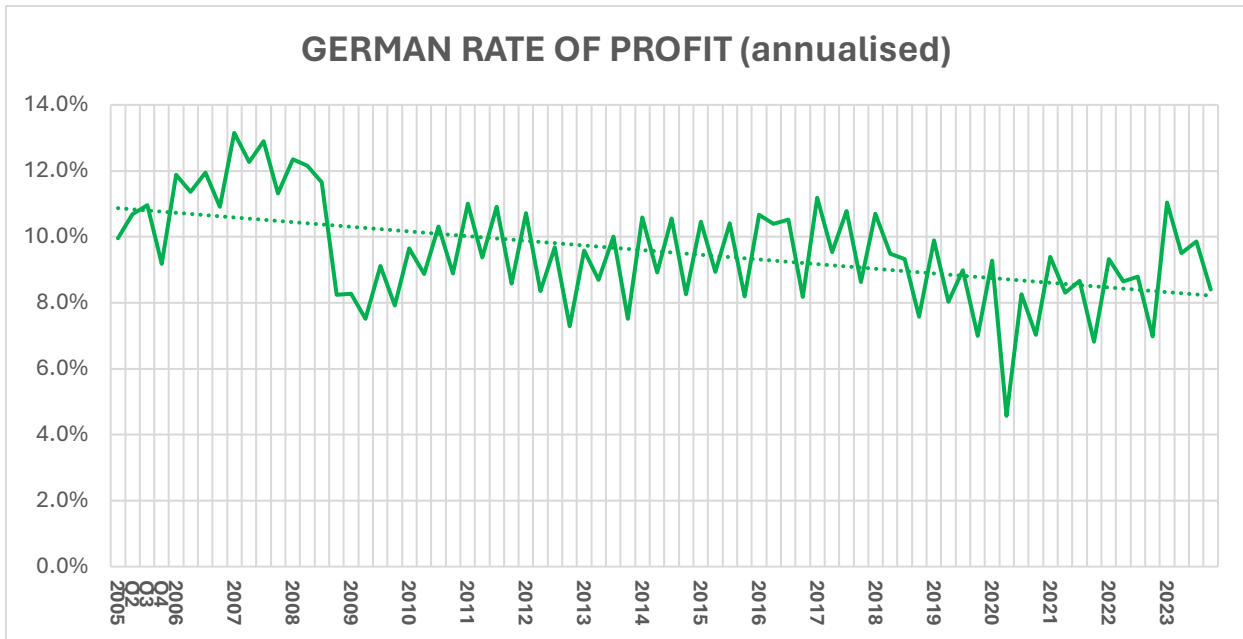
The rate of profit here is calculated on the basis of fixed and circulating capital, which is the Marxist method of calculating the rate of profit when not adopting constant and variable capital. Thus the rate of profit calculated this way aligns it with my calculations covering both the US and Germany. The standard for measuring and equating rates of profit is of course annual. By annualizing the original data which is normally presented quarterly, these three countries can be compared by using a common standard - annual. (Previously I measured the rate of profit for Germany quarterly as found [in my last article](#).)

The exception is China due to the difficulty in isolating fixed assets. Which is why I refer to it's rate as the *Complex Rate of Return* as capital there is based on fixed capital + inventory capital + financial assets. However, were we able to strip out financial assets, I am convinced that the average rate of profit in China would not be dissimilar to that found in the major economies.

Compared to the annual German rate of profit which averaged 9.1% over the period 2022-2023 the Japanese gross rate of profit was 8.5%, more or less in the same ballpark, while the pre-tax rate of profit for US corporations (excluding Q4 to be released next week) averaged 8.1% or 8.9% with interest included. This confirms the operation of one of the most dynamic laws governing capitalist production, one which Marx drew attention to repeatedly, and that is the equalization of the rate of profit. It holds true within nations, and it holds true between *developed* nations but only when measured accurately.

For comparison purposes I have added the German rate of profit below, and next week, when I have prepared the US rate of profit, I will provide all three rates of profit alongside each other - the US, Japanese and German.

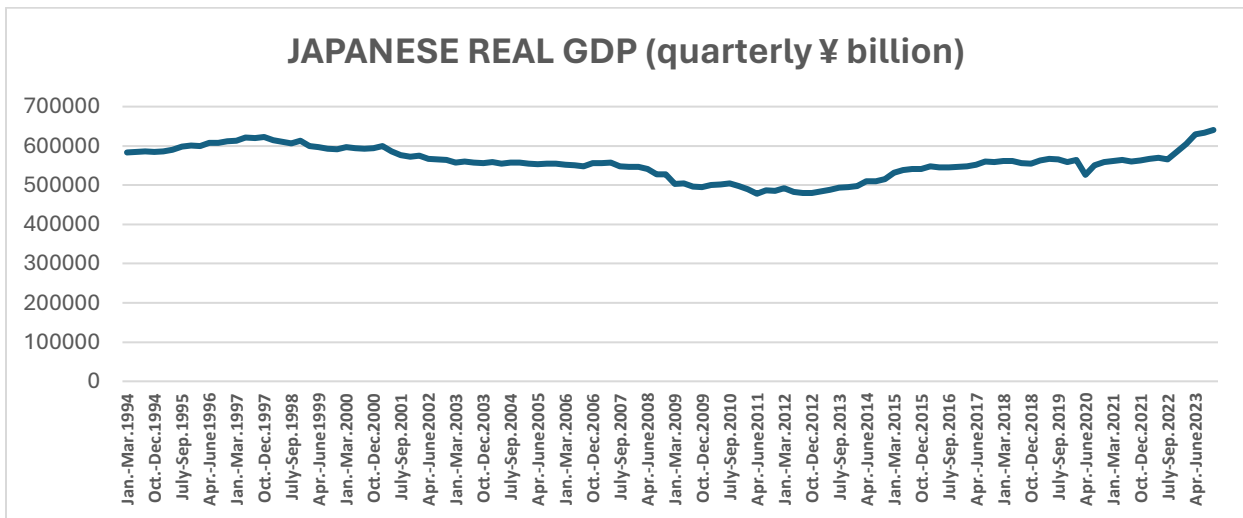
Graph 16.



**Current developments.**

[GDP](#) adjusted by the [GDP deflator](#) rose above its recent peak in 1997 for the first time. Of all the major economies, Japan has shown the least growth over the recent decades.

Graph 17.



This current growth spurt is unlikely to continue if the latest business survey turns out to be correct. The Policy Institute of the Ministry of Finance conducts quarterly surveys of business and business expectations which can be [viewed on this link](#). Ordinary profits are expected to fall this year in nominal terms and given inflation expectations even more so in real terms. We have seen how sensitive the degree of exploitation is to wage rises, and thus the expectation must be for a sharp fall in the 2024 rate of profit following the surge in wages. And all of this before summer hits. In addition, the BOJ decision to allow the

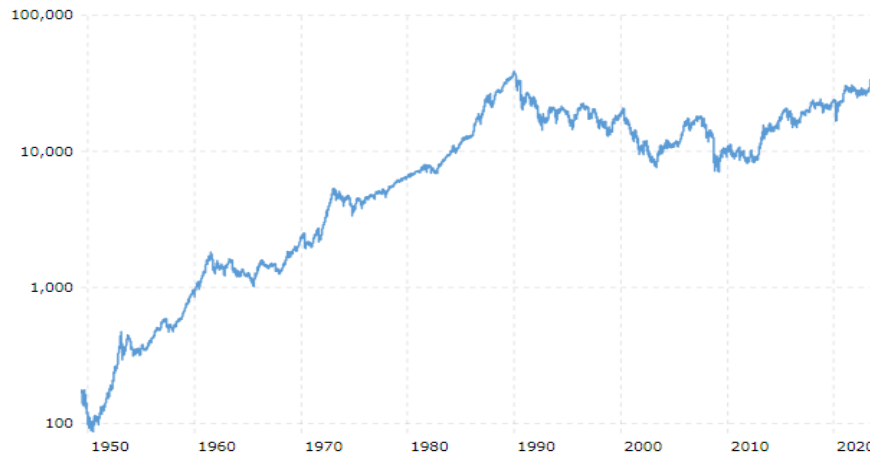
market a greater role in interest rate setting, i.e. an end to the repression of interest rates, means losses on the bond portfolios held by the larger corporation will further depress the gross rate of profit. Retail sales are expected to rise in line with inflation but no higher. In general the survey found that current conditions were flat this quarter but with expectations they would improve in the second quarter.

### Conclusion.

With inflation running above target at 2.8%: *“[Many board members](#) believe that the risk of Japan's economy slipping back into deflation has been reduced and inflation is likely to be led by sustained wage hikes, instead of spikes in import costs. The move follows news in the prior week that wage hikes for fiscal 2024 beginning next month will well surpass the pace of increase seen in the previous year.”* In addition exports rose above expectations though consumption within Japan remained muted, but should improve as wage rise expectations are met.

Does this mean the Japanese economy is normalizing, coming out of its stupor. The Nikkei Index certainly thinks so. It has regained its previous peak for the first time in over thirty years. However, it is far too soon to judge his. In any case as the BOJ said, if conditions warranted, the BOJ would be ‘nimble’ in its response to any potential issues as they arose.

**Graph 18.**



Japan has been cast as the canary in the coal mine. A warning about countries becoming too indebted. But far from being unique it shares many of the complaints besetting the major western economies. It is not only in Japan that wages have been repressed. In the USA male wages have been repressed since 1973. It is not only in Japan that negative interest rates have appeared. Adjusted for inflation, most of the countries in the West, up until 18 months ago enjoyed negative interest rates. No, what was unique about Japan and what set it apart from the USA, was the failure to purge excess capital, the failure to ‘brutally’ restructure the economy due to a greater density of owner manager corporations, the Keiretsu System of corporations orbiting a bank reluctant to write off their bad debts, and generally, corporations much younger than their counterparts in the USA. What Japan has taught the capitalist world is that recessions are not optional, that purging capital is not optional, that the alternative is more enduring stagnation. This is a lesson western countries are about to learn, for they too had resorted to cheap money to keep going.

Brian Green, 24<sup>th</sup> March 2023.