Current Trends in Financial Conditions of the Corporate Sector

(Summary)

This paper attempts to show the impact of post-COVID-19 changes on financial conditions, based on financial data provided by a third-party vender. In food and accommodation services industry, where the impact of the COVID-19 pandemic has been significant, earnings have recovered to pre-COVID-19 levels on average. On the other hand, while the debt burden of the same sector shows a sign of improvement towards FY2022, its level remains above pre-COVID-19 levels, warranting continued monitoring.

I. Purpose

The purpose of this paper is to understand the impact of post-COVID-19 changes on financial conditions and recent trends in the corporate sector, based on financial data provided by a third-party vender[1]. It should be noted that this analysis is based on the data up to December 2022, and therefore does not necessarily show the latest status, and that due to data limitations, there may be a sample bias.

II. Current trends in profitability

Figure 1 shows the median of profitability (return on total assets [ROA]) by industry since fiscal year (FY) 2016. Looking at the food and accommodation industries, the education and learning support industry, and the lifestyle-related services industry (hereinafter, lumped together and referred to as "food and accommodation services"), ROA declined in FY2020 but recovered toward FY2021, ending up in broadly the same as that before the COVID-19 pandemic in FY2022 (Fig. 1). When comparing the proportion of enterprises with net losses, it is found that the proportion in the food and

[1] Based on corporate financial data provided by Teikoku Databank, this paper analyzes data for 42,614 companies for which financial data is available for three consecutive years from FY2020 to 2022. For 2016 to 2019, the analytical sample is limited to companies with available data for each FY (number of samples: 2016: 30,733 companies, 2017: 32,584 companies, 2018: 33,887 companies, 2019: 35,689 companies).

accommodation services increased sharply in FY2020 compared with other industries but declined for two consecutive years in FY2021 and 2022, nearing the level of FY2019 (Fig. 2).

Figure 1 Return on total assets by industry (median)

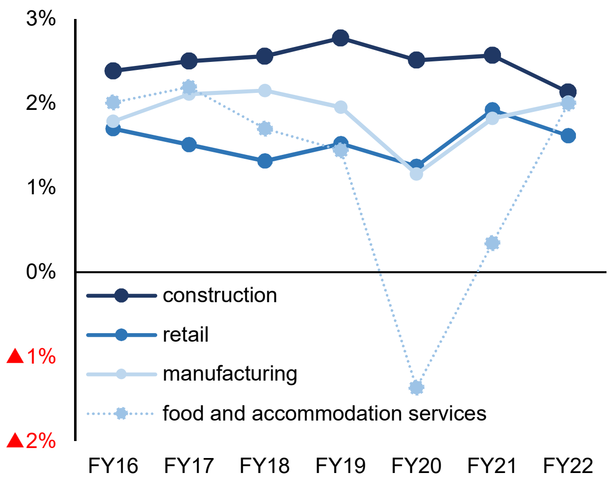
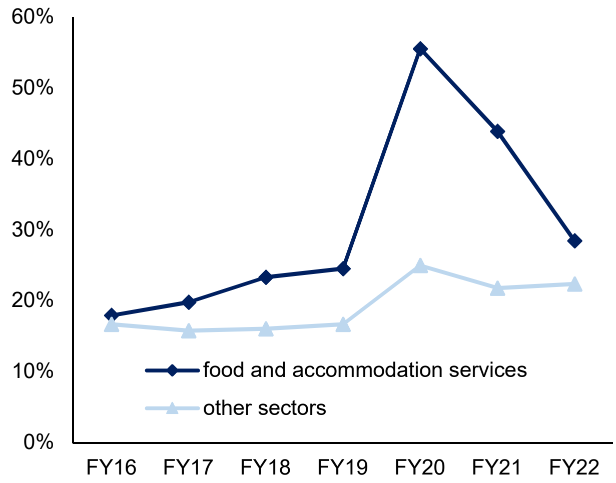
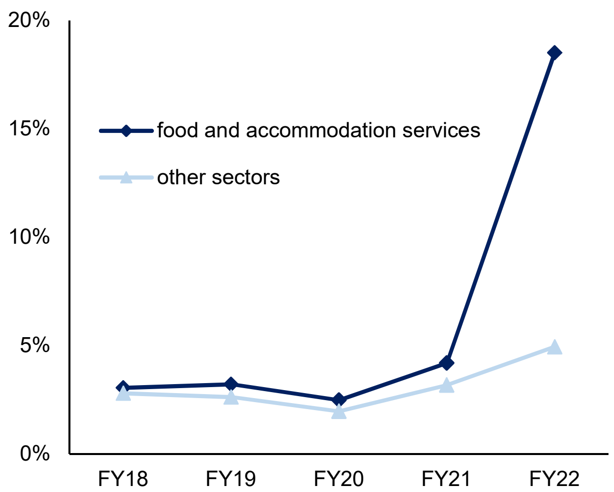


Figure 2 Proportion of enterprises with net losses (SMEs)



As seen above, while there are signs of recovery in profitability on average, some enterprises are still suffering from deterioration in earnings. Looking at the percentage of enterprises that have posted net losses for the past three consecutive years, it is observed that, while there has been a slight increase in other industries, there was a sharp rise in the food and accommodation services industry in FY2022, and it can be confirmed that around 20% of enterprises have posted net losses for three consecutive years since FY2020 (Fig. 3).

Figure 3 Percentage of enterprises that have posted net losses for the past three consecutive years (SMEs)



III. Current trends in debt

There has been improvement from the perspective of debt, but the recovery has been more moderate than that in income. Figure 4 shows the median of capital ratios by industry.

In contrast to other sectors, whose capital ratio have remained more or less unchanged amid the post COVID-19 phase, that for the food and accommodation services industry declined significantly in FY2020 and did not recover to the pre-COVID-19 level, despite some signs of recovery in FY2022. The same trends can be observed in Figure 5, which shows the proportion of insolvent enterprises. While the share has remained at almost the same level for other sectors, the food and accommodation service industry experienced a sharp increase in FY2020 and then only slight decline in FY2022, remaining at a high level. Figure 6 shows the net interest-bearing debt to sales ratio, where net interest-bearing debt is calculated by subtracting cash and deposits from interest-bearing debt. In the food and accommodation services industry, the ratio rose sharply in FY2020 and FY2021 and then declined in FY2022 but was still higher than pre-COVID-19 levels.

Figure 4 Capital ratios by industry (median)

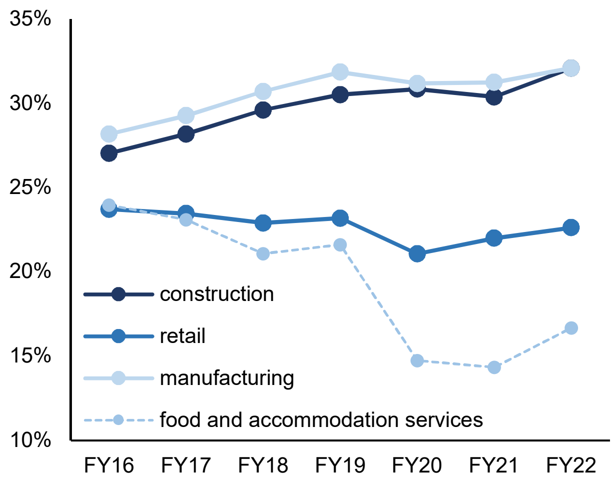


Figure 5 Proportion of insolvent enterprises (SMEs)

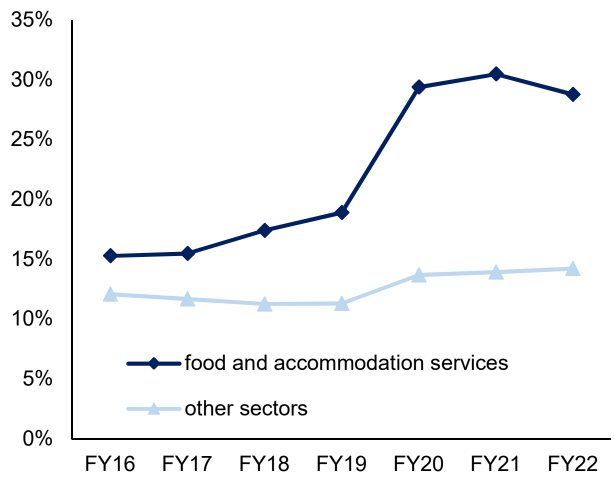
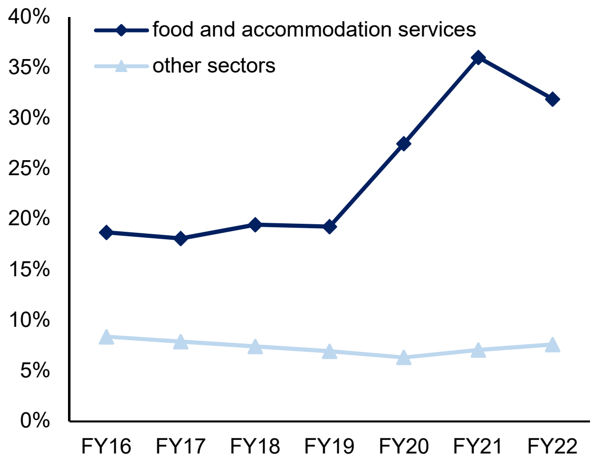


Figure 6 Real interest-bearing debt to sales ratio (median, SMEs)



IV. Current trends in profits and liabilities of low-profit enterprises

In order to understand the subsequent trends of enterprises with prolonged deterioration in profits, this section analyzes financial trends after deterioration in profits for enterprises who recorded net losses for three consecutive years between FY2001 and 2019 before COVID-19 (hereinafter referred to as “low-profit enterprises”).

First, with regard to profits, many enterprises that recorded continuous net losses turned profitable within a few years, while some enterprises remain in the red. Figure 7 shows the profitability of low-profit enterprises as of two data points, one year and three years after the time when they first incurred losses for three consecutive years, respectively. Around 50% of low-profit enterprises turned black one year after they posted losses for three consecutive years, however, around 20% remained in the red even after three years.

Next, looking at the debt of low-profit enterprises, it can be seen that the debt burden has generally improved in line with the recovery in profits. Figure 8 shows the changes in the capital ratio and the ratio of net interest-bearing debt to sales (both medians) for low-profit enterprises since they first incurred losses for three consecutive years. All indicators show a gradual recovery in the period.

Figure 7 Profitability of low-profit enterprises

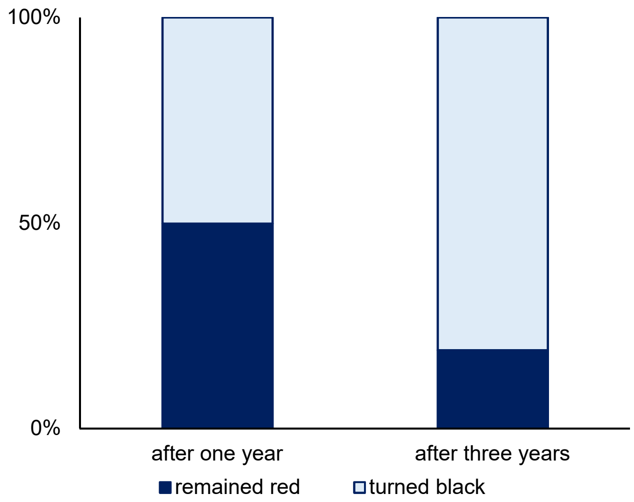
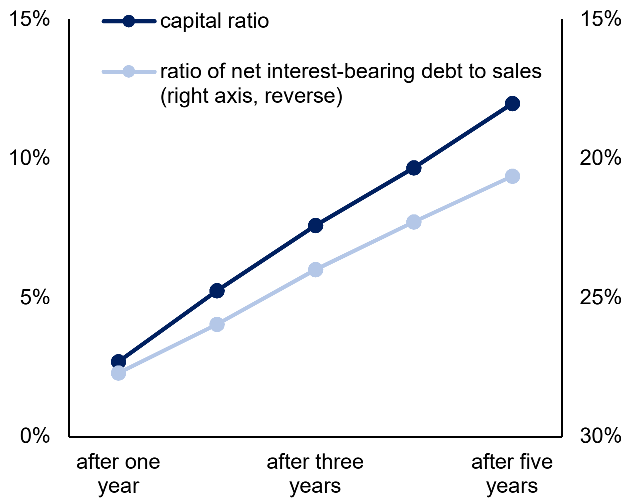
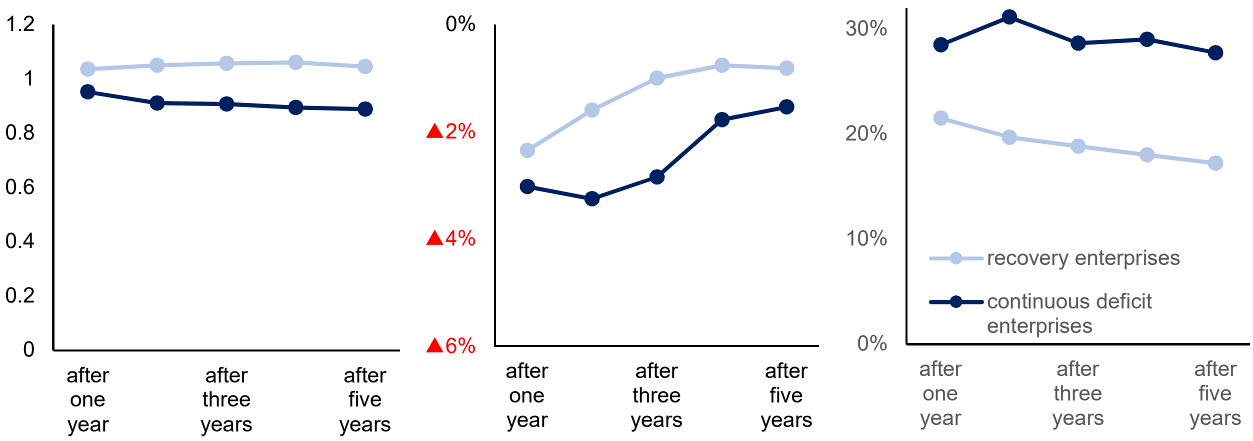


Figure 8 Capital ratio and the ratio of net interest-bearing debt to sales (median)



As can be seen from the above, low-profit enterprises are reducing their debt burden on average. On the other hand, enterprises that are lagging in improving their profits are continuing to have sluggish business. Figure 9 shows the trend in sales, growth rate of fixed assets, and ratio of net interest-bearing debt to sales for low-profit enterprises divided into two groups: those that turned black for two consecutive years (hereinafter referred to as "recovered enterprises") and those that remained in the red for two consecutive years (hereinafter referred to as "continuous deficit enterprises"), after posting losses for three consecutive years. In terms of sales, recovered enterprises made a steady recovery, while continuous deficit enterprises remained sluggish. As for investment in fixed assets, both groups reduced assets for several years after posting losses for three consecutive years, however, continuous deficit enterprises recorded a relatively larger decreasing rate compared to recovered enterprises whose decreasing rate gradually become moderate. Regarding the ratio of net interest-bearing debt to sales, recovered enterprises shows a decreasing trend, while the ratio remained high for continuous deficit enterprises.

Figure 9 Sales, investment, and debt for low-profit enterprises[2]
(divided into profit group, median within group)
(Left: sales / Middle: growth rate of fixed assets (YoY) / Right: ratio of real interest-bearing debt to sales)



V. Conclusion

As a summary, in food and accommodation services industry, where the impact of the COVID-19 pandemic has been significant, earnings have recovered to pre-COVID-19 levels on average, although some enterprises' earnings have continued to slump. On the other hand, while the debt burden of the same sector shows a sign of improvement towards FY2022, its level remains above pre-COVID-19 levels, warranting continued monitoring. Going forward, the FSA will continue to analyze the impact of COVID-19 on financial conditions in the corporate sector using various data and utilize the results in its dialogues with financial institutions and policy discussions.

[2] Sales are standardized to a value of 1 for the year in which the company has been in the red for three consecutive years.