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Expecting ETF funds to become mad popular…

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Apart form the wealthy people US households do not hold at all securities

In previous report I mentioned that Japanese individuals were still overall sellers but for a leading developed country like US households direct equity investment fallout is remarkable. US individuals are selling at high pace relative to their Japanese counterparts. In addition most of investment trusts, pensions & insurance equities holdings are based on individual's money and even foreigners rising market share is targeted at either institutional investor's international diversification or hedge funds for the wealthy. In the first place and regardless of borders individuals still represent the vast majority (in fact the percentage of U-turn type money invested through offshore accounts is quite large). Therefore if indirect investments are taken into account US individuals are not turning their back to equity investments.

As I wrote this I received an article form a securities analyst magazine specialized in individual's wealth management. It was a well documented article; particularly exiting were the articles from Hiroshima University Matsuura professor as to 'why is Japanese households equity investments share so low' and Hitotsubashi University professor Iwaisa article regarding 'households asset allocation'.

According to professor Matsuura the Japanese households equity holding percentage was stable at 15-20 % from 1960 to 2000. And above the 1983 UK level of 9 % and 1995 US level of 15,3 %, Japan was therefore well ranked among OECD developed countries for such a ratio. However as state owned companies privatization expanded in Europe and US an equity boom materialized .By 1998 the holding ratio increased to 27 % in UK,19.2 % in the USA, 17 % in Germany, 15 % in France and 14 % in Holland.

As a consequence by year 2000 equities share in financial assets had went up to 23 % in UK, 27 % in Germany,46 % in France (but this figure is to be taken with care), 23 % in Holland and 23 % for US. Compared to this Japan ratio was a meager 6 %. Furthermore in the USA at this time a tremendous shift from direct equity holding toward investment trust holding had started.

By breaking down US Japanese households net assets by class bracket (including real estate for the US and only financial assets for Japan) households lower 50 % range did not show a substantial difference between Japan and US (6 %). However looking at all household's equity holding share by class US was 0.6 % and Japan 9 % showing a substantial difference. On the other hand for the top 5 % super rich class US household's equity holding ratio was 69 %, Japan was 51 %. In Japan majority of super rich people do not hold any stocks. For this precise social class equity holding is up to 79 % in the US and only 49 % in Japan.
In the shares holding by the upper income bracket is excessively concentrated; by going down the ladder such holding nearly disappears. On the reverse in Japan wealthy people with no share holding are numerous but Japan has the particularity to show a high percentage of average citizens holding stocks.

From next year I feel ETF investment trusts will prove extremely popular.

In the US high income earners invest a substantial part of their money in equities; they are heavily felt in the marketplace contrary to the average income earners who hold few stocks. On the other side Japan overwhelmingly beats the US for stock holding average income earners contrary to high net worth individuals holding few stocks (or no stock at all). Professor Matsubara thinks the reason explaining why Japanese super rich remain negative toward equity investment lies with Japanese companies low payout ratio and low dividend yield. This is convincing.

Long ago Matsushita Konusuke (the Matsushita group founder) was literally looted from 93 % of its Matsushita stock holding profit (before tax) in income tax, only 7 % of that was left to him! Because of this he lamented that entrepreneurs would quickly disappear. The tax system was then largely improved but this has made high net worth individuals weary of stock investment in Japan.
The tax system has now greatly improved due to corporation tax reduction and equities favorable tax treatment. Companies are now rapidly putting strong emphasis on high dividend payout ratio. Considering equity loath top income earners will soon face their life end we can presume that the super wealthy attraction for equities will gradually improving.

Professor Iwaisa is carefully analyzing households assets distribution pattern, in the US the peak age for equities money allotment is the 40's, although in Japan it's the 60's.

In the US pension money reserves are used for equity investment and long term commitment is important. In Japan the tendency is rather to use retirement allowance to invest in equities. Despite being aware of Professor Matsubara theory professor Iwaisa believe that, in Japan, due to social and psychological hurdles stock investment is nearly considered a gamble which would explain the differences between US Japanese investment behaviors.

Professor Iwaisa core theory main points are that: Japan has several large financial deficits to handle therefore his forecast is based on what should be household's correct allocation. By going direct to his conclusion; 1. Japanese deficit is worsening; due to deficit expansion inflation is created. Or else 2. Financial problem is solved and a real grow out deflation happens. In both points a mild inflation is created and as a consequence an increase in real assets is inevitable. Said in other words it is appropriate to invest in either equities or real estate but with easing of supply demand in real estate expected return would be low therefore demand for stocks is going to increase. This is also a correct conclusion I believe.

Very long term oriented equity index funds should be the more appropriate , there has been widely known academic research on this subject in the US for 30 years, such products has been developed for 20 years. Based on this there are high chances to see part of Japanese retirement money flow to TOPIX type ETF from next year with a bandwagon effect consequence.