Daiwa
Daiwa Institute of Research

11 October 2012 (No. of pages: 3)

Japanese report: 11 Oct 12

August Machinery Orders

Still weak, centering on manufacturing orders

Economic Research Dept
Masahiko Hashimoto

Summary

- **Machinery orders remain at low level:** August machinery orders (Cabinet Office; private sector excl. those for shipbuilding and from electric utilities; this basis hereafter unless otherwise specified; leading indicator of domestic capex) declined 3.3% m/m, the first slide in three months. The slide was as expected, albeit wider than the market consensus (down 2.3%). Orders saw the first gain in four months on a three-month moving average basis but the value of orders remained at a low level, meaning the underlying weakness continues.

- **Manufacturing orders plunged, partly reflecting reactionary slide:** By demand source, manufacturing orders plunged 15.1% m/m, but non-manufacturing orders increased 3.6%. Orders from 11 out of 15 manufacturing industries declined m/m, while those from five out of 12 non-manufacturing industries declined—manufacturing orders drove the overall decline. Overseas orders declined 14.7% m/m, accelerating the slowdown amid the economic doldrums in China, the major destination of Japanese exports.

- **Jul-Sep likely flat q/q:** The Cabinet Office survey, released along with June figures, projected Jul-Sep machinery orders would decline 1.2% q/q, the second quarterly slide in a row. If orders declined 4.6% m/m in September, the projection will be met. If they declined 0.9%, we would see positive q/q growth. Thus, the hurdle is not too high for posting an expected or better-than-expected result. While the underlying trend has been weak as a whole, machinery orders will likely be flat q/q in Jul-Sep.

Machinery Orders (m/m %; SA) **Chart 1**

	2011				2012							
	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug
Machinery orders (private sector)*	-2.3	-0.6	3.1	-2.5	0.7	2.8	-2.8	5.7	-14.8	5.6	4.6	**-3.3**
Market consensus (Bloomberg)												**-2.3**
DIR estimate												**-0.5**
Manufacturing orders	-7.8	2.8	2.9	-4.0	-1.3	9.5	-8.4	3.4	-8.0	-2.9	12.0	**-15.1**
Non-manufacturing orders*	5.6	-4.8	5.4	-4.0	1.4	2.1	-3.9	5.7	-6.4	2.6	-2.1	**3.6**
Overseas orders	-16.0	1.6	14.1	4.1	14.6	-13.4	-14.4	0.3	0.3	-9.8	3.0	**-14.7**

Source: Cabinet Office, Bloomberg; compiled by DIR.
* excl. those for shipbuilding and from electric utilities.

IMPORTANT DISCLOSURES, INCLUDING ANY REQUIRED RESEARCH CERTIFICATIONS, ARE PROVIDED ON THE LAST TWO PAGES OF THIS REPORT.

Economic Research

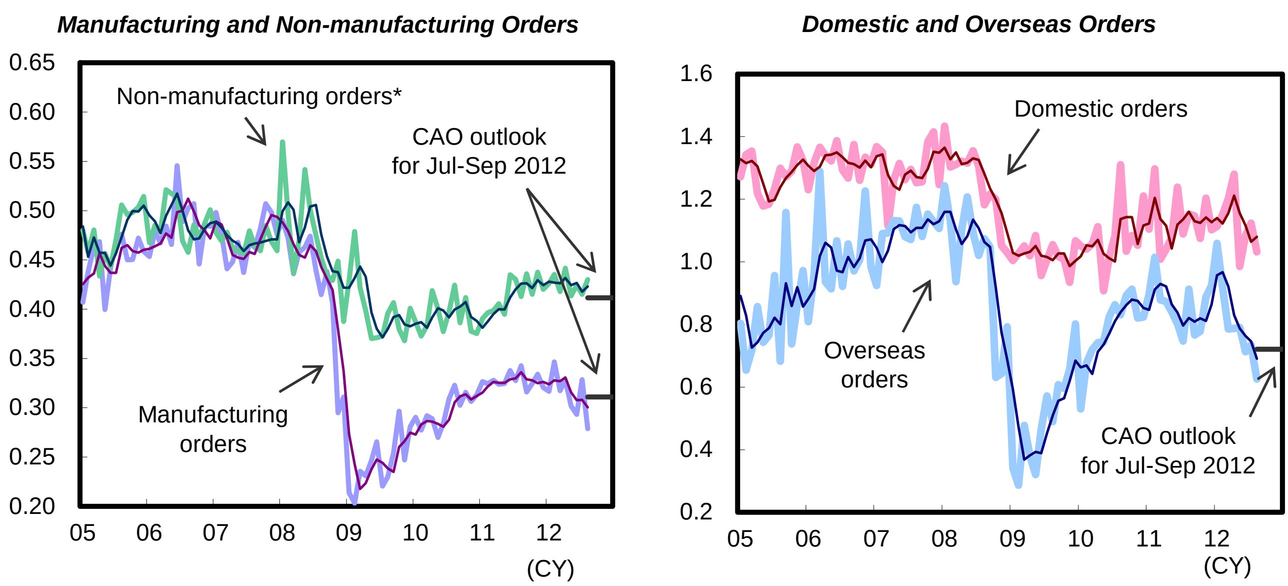
Machinery Orders Remain at Low Level

August machinery orders (Cabinet Office; private sector excl. those for shipbuilding and from electric utilities; this basis hereafter unless otherwise specified; leading indicator of domestic capex) declined 3.3% m/m, the first slide in three months. The slide was as expected, albeit wider than the market consensus (down 2.3%). Orders saw the first gain in four months on a three-month moving average basis, but the value of orders remained at a low level, meaning the underlying weakness continues.

Manufacturing Orders Plunged, Partly Reflecting Reactionary Slide

By demand source, manufacturing orders plunged 15.1% m/m, but non-manufacturing orders rose 3.6%. Orders from 11 out of 15 manufacturing industries declined m/m, while those from five out of 12 non-manufacturing industries dropped—manufacturing orders drove the overall decline. Among manufacturing orders, reactionary declines to July surges were seen for those from iron/steel (down 72.3%) and “other” transportation equipment industries (down 70.3%), dragging down overall manufacturing orders. Manufacturing orders, regardless of those from materials or assembling industries, have been on a downtrend, although accompanied by monthly fluctuations. Among non-manufacturing orders, those from the financial/insurance industry turned around (up 55.7%) from July’s substantial decline, driving overall non-manufacturing orders, and those from the transportation/postal services industry increased (up 18.3%), thanks to those for railroad vehicles. Those from a wide range of non-manufacturing industries have been flat in general, although accompanied by monthly fluctuations. However, those from the communications services have lost momentum after a moderate uptrend driven by propagation of smartphones, and posted a decline of 5.6%, which is a worrisome development and warrants watching going forward. Meanwhile, overseas orders declined 14.7% m/m, accelerating the slowdown amid the economic doldrums in China, the major destination of Japanese exports.

Machinery Orders by Demand Source (Y tril; SA) **Chart 2**

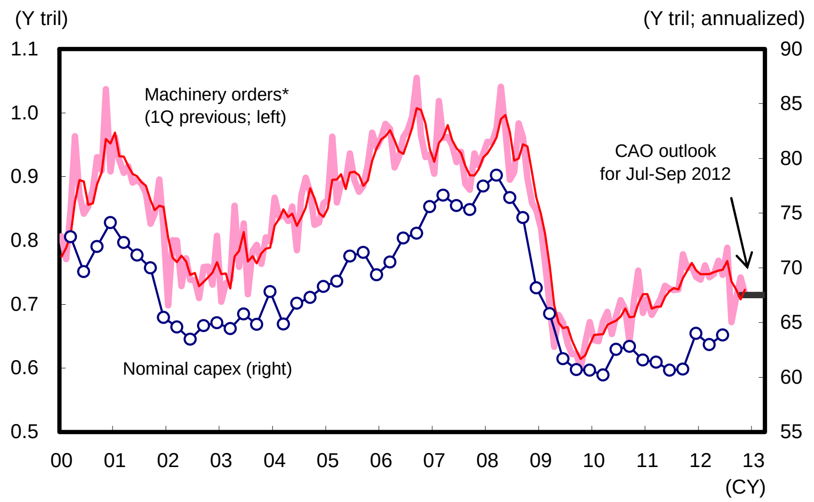


Source: Cabinet Office (CAO); compiled by DIR.
* excl. those for shipbuilding and from electric utilities.
Note: Thick lines and thin lines denote actual results and 3-month moving averages, respectively.

Jul-Sep Likely Flat Q/q

The Cabinet Office survey, released along with June figures, projected Jul-Sep machinery orders would decline 1.2% q/q, the second quarterly slide in a row. If orders declined 4.6% m/m in September, the projection will be met. If they declined 0.9%, we would see positive q/q growth. Thus, the hurdle is not too high for posting an expected or better-than-expected result. While the underlying trend has been weak as a whole, machinery orders will likely be flat q/q in Jul-Sep. Given the tendency that machinery orders lead GDP-based capex by around three months, capex will likely decline in Jul-Sep and level off in Oct-Dec. Nevertheless, a production turnaround is a prerequisite for a capex recovery, but production is unlikely to see a proper recovery before 2013 due to overseas economic conditions. Thus, capex will likely remain at a low level at least through end-2012.

Machinery Orders and Nominal GDP-based Capex Chart 3



Source: Cabinet Office; compiled by DIR.
* excl. those for shipbuilding and from electric utilities; thick line and thin line denote actual result and 3-month moving average, respectively.