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December Machinery Orders

Both Manufacturing and Non-Manufacturing Orders Suffer Major Declines, Falling Below Market Expectations

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Summary

- According to statistics for machinery orders in December 2013, the leading indicator for domestic equipment investment, private sector demand (excluding for shipbuilding and from electric power), suffered an m/m decline for the first time in three months at -15.7%, falling considerably below consensus (-4.0% m/m).

- As for performance by source of demand, manufacturing industries registered an m/m decline for the first time in two months at -17.3%. Non-manufacturing orders (excluding for shipbuilding and from electric power) also suffered a m/m decline for the first time in three months at -17.2%.

- Overseas orders achieved m/m growth for the first time in three months at +8.6%. However, considering the dramatic declines suffered in October and November of last year, results left something to be desired.

- The CAO projected the first decline in four quarters in its Jan-Mar 2014 outlook, with private sector demand (excluding for shipbuilding and from electric power) seen down 2.9% in comparison with the previous period. By industry, manufacturing industries are expected to be down by 1.8% in comparison with the previous quarter, with non-manufacturing expecting a decline of 5.9%, reflecting the cautious tone.

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

	2013 Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
Machinery orders (private sector)*	-7.5	4.2	14.2	-8.8	10.5	-2.7	-0.0	5.4	-2.1	0.6	9.3	-15.7
Market consensus (Bloomberg)												-4.0
DIR estimate												-3.2
Manufacturing orders	-10.0	4.9	13.3	-7.3	3.8	2.4	4.8	0.8	4.1	-0.2	6.0	-17.3
Non-manufacturing orders*	-4.5	0.3	14.3	-6.0	25.4	-17.5	0.0	6.2	-7.0	11.5	8.1	-17.2
Overseas orders	-3.7	1.0	52.1	-19.9	10.3	-16.7	1.4	22.4	12.1	-16.0	-12.2	8.6

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

December Machinery Orders Fall Considerably Below Market Expectations

According to statistics for machinery orders in December 2013, the leading indicator for domestic equipment investment, private sector demand (excluding for shipbuilding and from electric power), suffered an m/m decline for the first time in three months at -15.7%, falling considerably below consensus (-4.0% m/m). Looking at the 3-month moving average, this represents the first time a decline was recorded in six months. It seems that machinery orders are taking a breather from their recent growth trend. However, machinery orders are quite a broad-ranging statistic, and hence require taking a good look at the entire range of factors in interpreting findings in a single month. This month's major declines are considered to be due to special factors, and a sharp eye must be kept on future trends.

Both Manufacturing and Non-manufacturing Industries Suffer Major Declines

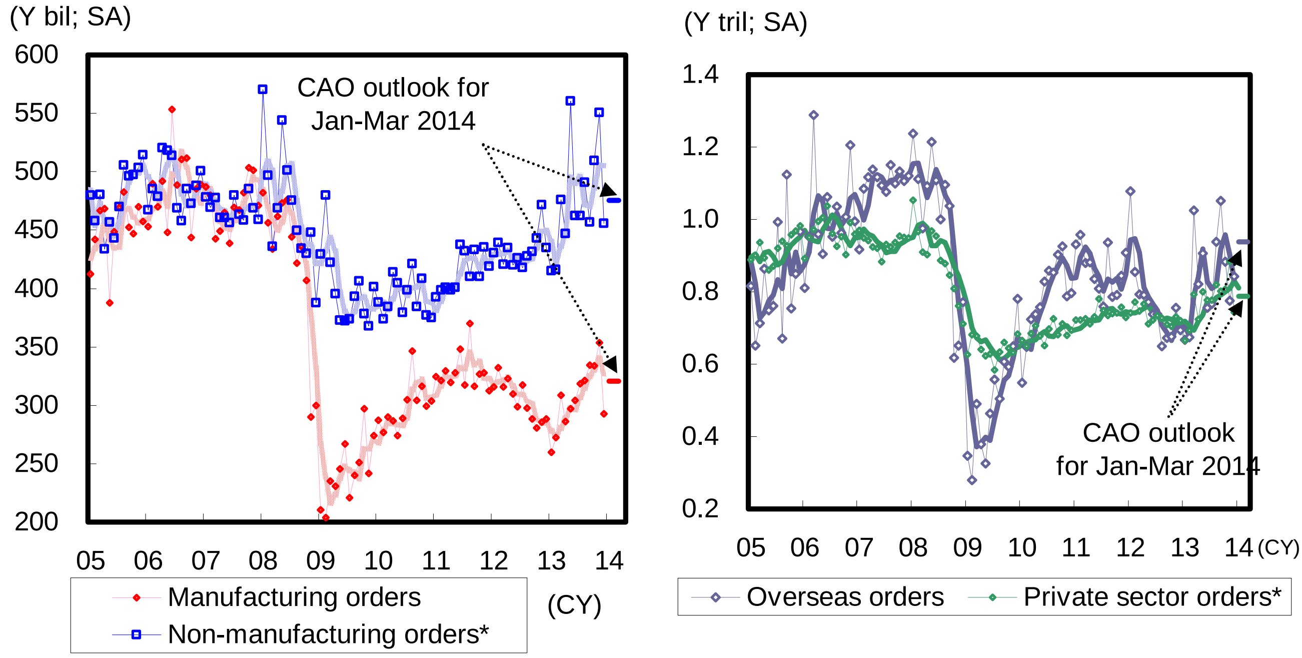
As for performance by source of demand, manufacturing industries registered an m/m decline for the first time in two months at -17.3%.

Areas suffering m/m declines were as follows: electrical machinery down 31.6% m/m, pulp & paper/paper products down 77.5%, most likely due to a rebound from the previous month. In addition, chemicals were down 26.1% m/m seemingly taking a short break after having maintained a growth trend for some time. On the other hand, auto parts and accessories achieved m/m growth of 11.5%, with continued improvements in auto related business performance, resulting in robust equipment investment in that industry.

Non-manufacturing orders (excluding for shipbuilding and from electric power) also suffered a m/m decline for the first time in three months at -17.2%.

In performance by industry, the financial and insurance industries suffered a decline of 41.4% m/m, while transportation and postal activities were down 22.5% and the wholesale & retail industry recorded a m/m decrease of 29.9%, helping to bring down overall results. On the other hand, agriculture, forestry and fisheries made m/m gains of 7.3%, while the mining, mineral extraction, and sand & gravel extraction industries boasted growth of 69.7%, with real estate up 4.8%, and information/communications equipment up 0.5%.

Orders by Demand Source (seasonally adjusted figures) **Chart 2**

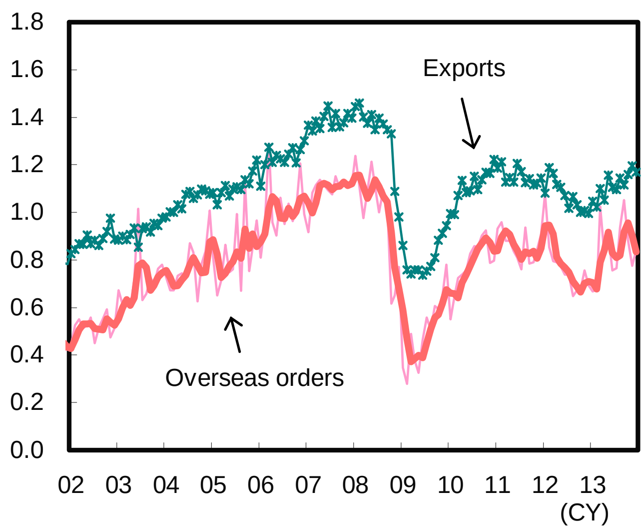


Source: Cabinet Office (CAO); compiled by DIR.
*excl. those for shipbuilding and from electric utilities.
Note: Thick lines 3MMA basis.

Overseas Orders Achieve Growth for First Time in Three Months

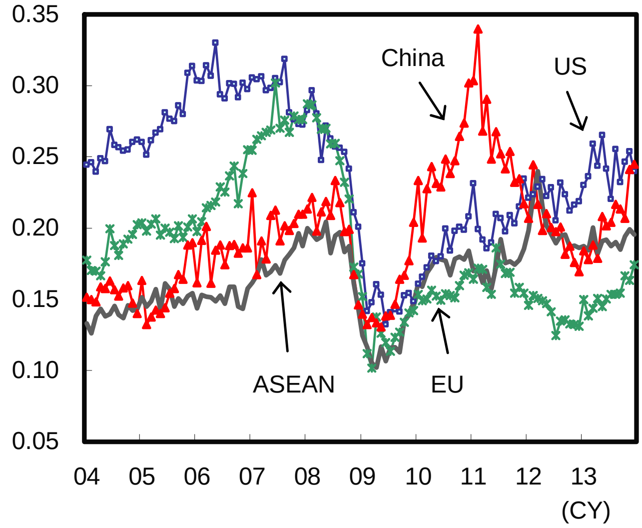
Overseas orders achieved m/m growth for the first time in three months at +8.6%. However, considering the dramatic declines suffered in October and November of last year, results left something to be desired. A look at trends in exports of general machinery reveals that exports to China are growing rapidly. Meanwhile, though exports to the U.S. remain stagnant, they are expected to gradually increase in the future. In addition, exports of general machinery to the ASEAN are seen picking up, and are expected to become a factor supporting overseas orders.

General Machinery: Overseas Orders and Exports (Y tril; SA) **Chart 3**



Source: Cabinet Office, Ministry of Finance; compiled by DIR.
Notes: 1) Exports seasonally adjusted by CAO, general machinery exports by DIR.
2) Thick line for overseas orders 3MMA basis.

General Machinery: Exports by Trading Partner (Y tril; SA) **Chart 4**

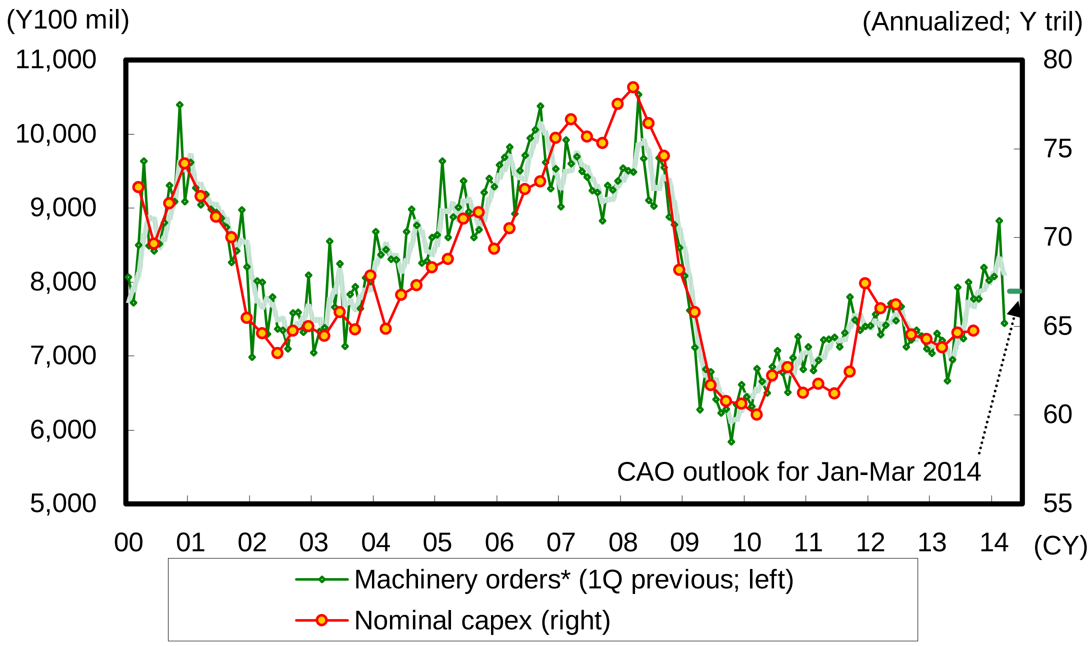


Source: Ministry of Finance; compiled by DIR.
Note: SA by DIR.

CAO Projects First Decline in Four Quarters for Jan-Mar 2014 Machinery Orders

The CAO projected the first decline in four quarters in its Jan-Mar 2014 outlook, with private sector demand (excluding for shipbuilding and from electric power) seen down 2.9% in comparison with the previous period. By industry, manufacturing industries are expected to be down by 1.8% in comparison with the previous quarter, with non-manufacturing expecting a decline of 5.9%, reflecting the cautious tone. The outlook for private sector demand (excluding for shipbuilding and from electric power) can be achieved if m/m growth of 2.9% can be attained in each month of the first quarter of 2014. Meanwhile, in order to achieve growth in comparison with the previous quarter, each month during the Jan-Mar 2014 period must post gains of 4.4% in comparison with the previous quarter. We see Jan-Mar 2014 machinery orders to remain stagnant. However, equipment investment is expected to continue growing in the future due to expanding domestic demand and the weak yen, which are contributing to improvements in corporate earnings.

Machinery Orders and Nominal Capex (SA) **Chart 5**



Source: Cabinet Office (CAO); compiled by DIR. *excl. those for shipbuilding and from electric utilities; thick line 3MMA basis.