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BOJ June 2015 Tankan Survey

Business sentiment gains strength mainly amongst large corporations; capex plans revised upwards considerably

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Summary

- In the BOJ June Tankan survey of corporate sentiment, the current trend in business sentiment has strengthened, especially amongst large corporations in both manufacturing and non-manufacturing. In addition, capex plans for FY2015 have been revised upwards considerably, indicating a growing corporate willingness to invest.

- The business conditions DI for large manufacturers (+15%pt in comparison with last survey's +12%pt) improved, while at the same time exceeding market consensus (+12%pt). While indications that exports may soon be peaking out and overall production trends cast a shadow over the business sentiments of corporate management, other factors are also present which are working in a more positive direction. These include the yen weakening further in comparison to the previous survey, as well as the continued trend toward improvement in corporate business performance, especially amongst export driven industries.

- Business conditions DI for large non-manufacturing industries also improved at +23%pt in comparison to the previous survey (+19%pt) and exceeded market consensus (+22%pt). This represents the third consecutive quarter of improvement for business sentiment in the non-manufacturing industry. Looking at performance by industry, improvement was marked in the area of retailing and accommodations, eating & drinking services, due to improvement in sales for supermarkets and department stores brought on by growth in inbound consumption on the part of foreign tourists visiting Japan.

- Sales projections of large corporations (all industries) for FY2015 grew +0.6% y/y, with recurring profits expected to be up by +1.1% y/y, due to economic recovery. A modest improvement, but it represents expectations of growth in both earnings and profits. The amendment ratio in comparison to the previous survey shows a downward revision for sales (-2.0%) and an upward revision for recurring profits (+3.7%).

- The FY 2015 capex projection for large corporations in all industries (incl. investment in properties but excl. that in software; all industries, large companies) is +9.3% y/y, and exceeds market consensus considerably (+5.3%). Capital expenditure plans on the June survey reflect a certain quirk in statistics whereby upward revisions tend to occur, especially for small enterprises. Even so, upward revisions of capex projections on the current survey are considerably larger than the average year, encouraging an especially positive assessment.

Business sentiment improves for both manufacturing and non-manufacturing

In the BOJ June Tankan survey of corporate sentiment, the current trend in business sentiment has strengthened, especially amongst large corporations in both manufacturing and non-manufacturing. In addition, capex plans for FY2015 have been revised upwards considerably, indicating a growing corporate willingness to invest. However, it should be noted that the results of the BOJ Tankan survey do not include factors such as the possibility of negative effects stemming from the fiscal problems in Greece, which have rapidly increased the sense of uncertainty in recent weeks. Looking back at the year 2012 when the European debt crisis worsened, it is important to be aware of the downward pressure brought on business sentiment in some industries, due to the strengthening of the yen and progressively low price of crude oil resulting from the slowdown in overseas economies.

The business conditions DI for large manufacturers (+15%pt in comparison with last survey's +12%pt) improved, while at the same time exceeding market consensus (+12%pt). While the slowdown in exports and overall production cast a shadow over the business sentiments of corporate management, other factors are also present which are working in a more positive direction. These include the yen weakening further in comparison to the previous survey, as well as the continued trend toward improvement in corporate business performance, especially amongst export driven industries.

Performance by industry was as follows: in the materials industry, the situation had been worsening for pulp & paper and ceramics, stone & clay due to the rising cost of raw materials associated with the weak yen, but improvement was seen on the current survey. Meanwhile, petroleum and coal products continue to improve as the price of crude oil makes a comeback. On the other hand, iron & steel worsened considerably due to slow public investment, sluggish exports, and stagnant automobile sales, causing a sore point in current results. In the processing industries, the comeback in domestic demand has brought noticeable improvement in production machinery and business oriented machinery. Meanwhile, electrical machinery, where business sentiment had been sluggish of late, improved in comparison to the previous survey due to the effect of the weak yen. Meanwhile, overseas capex related demand shows signs of a decline, causing a slight deterioration in the situation for general machinery. A worsening situation was also unavoidable for automobiles due to stagnant domestic sales of new car models and slow exports.

Business conditions DI for large non-manufacturing industries also improved at +23%pt in comparison to the previous survey (+19%pt) and exceeded market consensus (+22%pt). This represents the third consecutive quarter of improvement for business sentiment in the non-manufacturing industry. Looking at performance by industry, improvement was marked in the area of retailing and accommodations, eating & drinking services, due to improvement in sales for supermarkets and department stores brought on by growth in inbound consumption on the part of foreign tourists visiting Japan. Personal services worsened in comparison to the previous survey, but maintained a steady undertone, with business conditions DI remaining at a fairly high level. Housing starts, which experienced a downtrend after the increase in the consumption tax, appear to be making a comeback, while the office vacancy rate has been declining, bringing welcome improvements to the real estate industry. However, public investment has been sluggish and the shortage in manpower continues, causing the construction industry to worsen. Electric & gas utilities saw improvement in its business conditions DI (-2%pt on the previous survey to 0%pt on the current survey) thanks to the fall in energy prices. This area managed to shake off negative performance for the first time in 17 quarters.

Business conditions DI to maintain high level despite worsening expectations for future in non-manufacturing

Looking at the future outlook for business conditions DI, large manufacturers see +16%pt (an improvement of +1pt in comparison to the current survey), while +21%pt is seen for major non-manufacturers (a decline of -2pt). While the corporate earnings environment as continued to improve recently, the downturn for non-manufacturing is a sign that a certain amount of care should be taken as regards the future. However, considering the high DI levels which are expected to be maintained, an especially negative view is uncalled for. In the manufacturing industries, improvement in future expectations for the auto industry stands out considering the fears that arose due to stagnant domestic sales of new car models and slow exports. Meanwhile, the non-manufacturing industries show signs of a lull coming up in the future for a broad range of industries including retailing, which had been improving till now thanks to the recovery in personal consumption, accommodations, eating & drinking services, and personal services. Hence care should be taken.

As for the business conditions DI of small enterprises, results were the reverse of the large corporations. The business conditions DI of small manufacturers overall was 0%pt, a decrease of -1pt in comparison with the previous forecast. Looking at results by industry, worsening business sentiment was especially outstanding for electrical machinery and automobiles. However, small non-manufacturers saw an improvement at +4%pt, a modest improvement of +1pt in comparison with the previous survey. Improvements were made in accommodations, eating & drinking services, and personal services thanks to the recovery in personal consumption. On the other hand, retailing is marking time due to the major shortage of manpower, and construction also worsened.

Overseas supply and demand for products expected to improve for both the materials and processing industries

Taking a look at large corporations' supply-demand conditions DI for domestic products and services, we see that the non-manufacturing industry gained a small improvement in comparison with the previous survey due to the recovery in the domestic economy. On the other hand, the processing industries were sluggish due to the slowdown in domestic production, while the manufacturing industries remained flat. Overseas supply and demand for products and services is marking time for large corporations due to the economic slowdown in China and the other emerging nations. However, there are signs of recovery in the US and EU economies, which is expected to bring improvements for the materials and processing industries. As for price conditions DI, the comeback in the price of crude oil March of 2015 and the progressively weak yen has brought an increase in input price conditions DI for both the manufacturing and non-manufacturing industries. This has brought a deterioration in the terms of trade (output price conditions DI – input price conditions DI). The result is that care should be taken in regards to corporate earnings in the future.

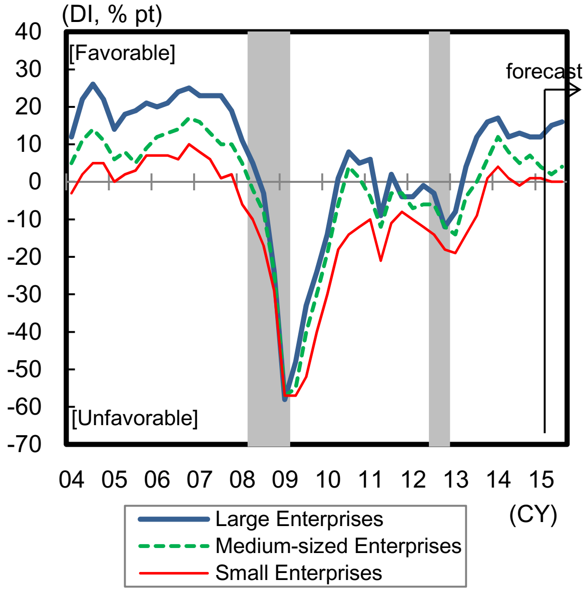
Though modest, large corporations see both income and profits increasing due to economic recovery

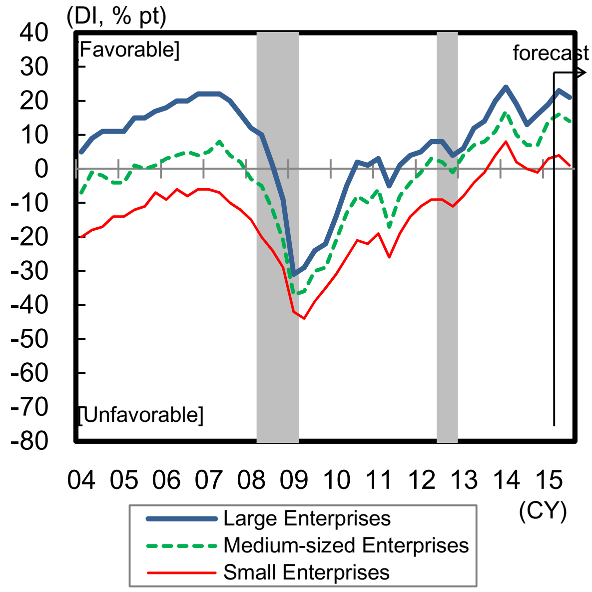
Sales projections of large corporations (all industries) for FY2015 grew +0.6% y/y, with recurring profits expected to be up by +1.1% y/y, due to economic recovery. A modest improvement, but it represents expectations of growth in both earnings and profits. The amendment ratio in comparison to the previous survey shows a downward revision for sales (-2.0%) and an upward revision for recurring profits (+3.7%). On an industry by industry basis, manufacturing was especially outstanding in the major upward revision in its recurring profits in comparison to the previous survey (+5.5%). The assumed exchange rate in the first half of FY2015 for major manufacturers is 115.59 yen to the dollar. Considering the current yen exchange rate, manufacturers are being fairly conservative in their projections. This means that we must remain on guard for the possible effects which the increasingly uncertain situation in Greece may have on the global financial markets. At the same time, if the yen rate remains at around its current level, there will likely be upward revisions in corporate earnings in the future for export driven manufacturing industries.

FY2015 capex projections revised considerably upwards

The FY 2015 capex projection for large corporations in all industries (incl. investment in properties but excl. that in software; all industries, large companies) is +9.3% y/y, and exceeds market consensus considerably (+5.3%). Capital expenditure plans on the June survey reflect a certain quirk in statistics whereby upward revisions tend to occur, especially for small enterprises. Even so, upward revisions of capex projections on the current survey are considerably larger than the average year, encouraging an especially positive assessment. On an industry by industry basis, large manufacturers revised projections by +18.7% y/y, while non-manufacturing revised projections downwards by +4.7%. Comparing with past tendencies, both industries won major upward revisions. The manufacturing industry shows an especially strong propensity to invest in capex. This is most probably due to the weak yen and the moderate recovery in domestic demand, which is expected to bring continued improvement in corporate earnings. Meanwhile, production capacity DI for major manufacturers was +2%pt, down by -1pt from the previous survey, meaning that the sense of overcapacity is continuing to resolve itself. Meanwhile, major non-manufacturers were slightly worse in comparison to the previous survey, continuing negative levels of capex (deficiency). Both industries see declines in the future (meaning improvement), encouraging a positive assessment. These levels of production capacity DI and forecast DI should also provide support for a future comeback in capex.

Business Conditions DI — Chart 1





Source: Bank of Japan; compiled by DIR.
Note: 1. Shaded areas denote economic down turns.
2. Due to changes in samples used in the forecast, there is some discontinuity between the December 2014 and March 2015 results.

(DI, % pt)

	Large Enterprises						Small Enterprises					
	March. 2015 Survey		June 2015 Survey				March. 2015 Survey		June 2015 Survey			
	Actual result	Forecast	Actual result	Changes	Forecast	Changes	Actual result	Forecast	Actual result	Changes	Forecast	Changes
Manufacturing	12	10	15	3	16	1	1	0	0	-1	0	0
Textiles	3	6	3	0	13	10	-18	-23	-21	-3	-23	-2
Lumber & Wood products	0	-12	-29	-29	0	29	-16	-19	-20	-4	-20	0
Pulp & Paper	-7	0	7	14	-3	-10	-16	-13	-15	1	-12	3
Chemicals	16	13	15	-1	11	-4	2	5	8	6	8	0
Petroleum & Coal products	-11	0	0	11	17	17	-6	-13	-15	-9	-18	-3
Ceramics, Stone & Clay	2	9	20	18	18	-2	3	-2	1	-2	-2	-3
Iron & Steel	14	5	-3	-17	10	13	6	7	5	-1	7	2
Nonferrous metals	14	8	17	3	14	-3	0	8	-6	-6	4	10
Food & Beverages	10	9	18	8	17	-1	-6	-3	0	6	2	2
Processed metals	0	-7	-7	-7	0	7	4	12	2	-2	2	0
General-purpose machinery	25	16	23	-2	23	0	15	11	16	1	6	-10
Production machinery	26	25	37	11	36	-1	10	11	11	1	7	-4
Business oriented machinery	19	13	22	3	24	2	13	7	17	4	10	-7
Electrical machinery	15	15	19	4	17	-2	8	3	1	-7	2	1
Shipbuilding & Heavy machinery, etc.	14	7	14	0	4	-10	23	19	19	-4	20	1
Motor vehicles	15	6	11	-4	16	5	18	7	12	-6	10	-2
Basic materials	8	7	8	0	11	3	-4	-4	-6	-2	-5	1
Processing	15	11	17	2	18	1	5	4	4	-1	3	-1
Nonmanufacturing	19	17	23	4	21	-2	3	-1	4	1	1	-3
Construction	36	26	34	-2	33	-1	15	2	11	-4	5	-6
Real estate	33	29	35	2	30	-5	7	4	11	4	9	-2
Goods rental & Leasing	28	23	28	0	28	0	16	12	12	-4	11	-1
Wholesaling	4	7	10	6	9	-1	-5	-5	-2	3	-2	0
Retailing	5	13	22	17	19	-3	-13	-14	-13	0	-12	1
Transport & Postal activities	15	15	24	9	15	-9	0	-2	0	0	-4	-4
Communications	16	22	28	12	17	-11	18	19	17	-1	15	-2
Information services	23	22	28	5	27	-1	7	11	9	2	5	-4
Electric & Gas utilities	-2	-2	0	2	-5	-5	15	12	17	2	17	0
Services for businesses	27	23	29	2	29	0	7	2	8	1	5	-3
Services for individuals	27	30	24	-3	22	-2	2	-3	8	6	3	-5
Accommodations, Eating & Drinking services	17	13	26	9	22	-4	-7	-5	5	12	4	-1
All industries	16	14	19	3	18	-1	2	0	2	0	1	-1

Source: Bank of Japan.
Note: 1. DI = “Favorable” minus “Unfavorable”; % pt.
2. Shaded areas denote economic down turns.
3. Changes in forecast = "Forecast of the current survey" minus "Actual result of the current survey"

Sales and Current Profits Projections Chart 2

Sales (Year-to-year % change)

		FY2014 (Forecast)	FY2015 (Forecast)	Revision rate
Large Enterprises	Manufacturing	1.3	0.9	0.4
	Domestic Sales	-0.6	0.1	-0.9
	Exports	5.9	2.8	3.6
	Nonmanufacturing	0.5	0.3	-3.6
	All industries	0.8	0.6	-2.0
Medium-sized Enterprises	Manufacturing	1.9	1.4	0.1
	Nonmanufacturing	0.2	1.2	0.2
	All industries	0.6	1.2	0.2
Small Enterprises	Manufacturing	1.2	0.5	-0.8
	Nonmanufacturing	0.0	-0.9	0.4
	All industries	0.2	-0.6	0.1
All Enterprises	Manufacturing	1.4	0.9	0.1
	Nonmanufacturing	0.3	0.1	-1.5
	All industries	0.6	0.4	-1.0

Current Profits (Year-to-year % change)

		FY2014 (Forecast)	FY2015 (Forecast)	Revision rate
Large Enterprises	Manufacturing	11.5	0.8	5.5
	Basic materials	0.1	8.2	1.8
	Processing	16.1	-1.8	7.0
	Nonmanufacturing	3.7	1.5	1.8
	All industries	7.6	1.1	3.7
Medium-sized Enterprises	Manufacturing	11.8	0.0	5.4
	Nonmanufacturing	-0.6	-2.3	0.5
	All industries	3.1	-1.6	2.0
Small Enterprises	Manufacturing	8.6	-1.5	-1.2
	Nonmanufacturing	0.8	-5.6	2.2
	All industries	2.6	-4.6	1.3
All Enterprises	Manufacturing	11.2	0.5	4.8
	Nonmanufacturing	2.2	-1.0	1.6
	All industries	5.9	-0.4	3.0

Note: Revision rates are calculated as the percentage change of the figures between the current and the previous survey.
Source: Bank of Japan.

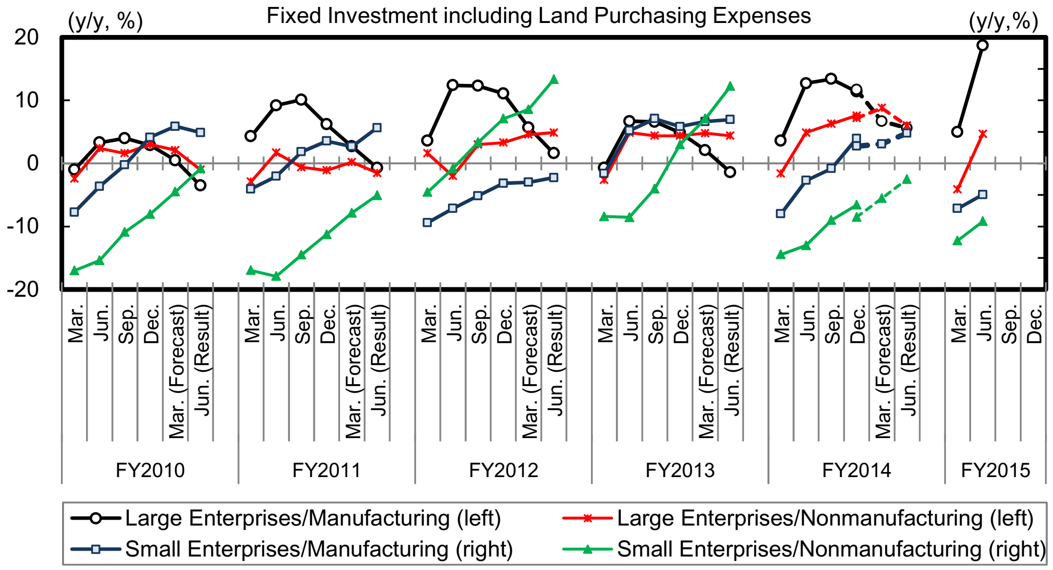
Developments of Fixed Investment including Land Purchasing Expenses (excl. software investment) Chart 3

Fixed Investment including Land Purchasing Expenses (Year-to-year % change)

		FY2014 (Forecast)	FY2015 (Forecast)	Revision rate
Large Enterprises	Manufacturing	5.6	18.7	11.8
	Nonmanufacturing	6.0	4.7	6.3
	All industries	5.9	9.3	8.2
Medium-sized Enterprises	Manufacturing	8.7	11.8	7.3
	Nonmanufacturing	1.9	-3.2	6.1
	All industries	4.2	2.1	6.6
Small Enterprises	Manufacturing	9.6	-9.9	8.5
	Nonmanufacturing	-5.0	-18.4	15.4
	All industries	-0.8	-15.7	13.0
All Enterprises	Manufacturing	6.8	12.3	10.6
	Nonmanufacturing	3.1	-1.0	7.6
	All industries	4.3	3.4	8.7

Software Investment (Year-to-year % change)

		FY2014 (Forecast)	FY2015 (Forecast)	Revision rate
Large Enterprises	Manufacturing	5.5	3.5	2.2
	Nonmanufacturing	-1.5	2.4	2.7
	All industries	0.8	2.8	2.5
Medium-sized Enterprises	Manufacturing	3.6	11.0	5.1
	Nonmanufacturing	-1.2	-1.3	8.6
	All industries	-0.4	0.7	8.0
Small Enterprises	Manufacturing	1.3	-13.1	1.2
	Nonmanufacturing	29.7	-9.1	5.8
	All industries	19.7	-10.3	4.5
All Enterprises	Manufacturing	5.1	2.8	2.3
	Nonmanufacturing	0.6	0.9	3.8
	All industries	2.0	1.5	3.3



Source: Bank of Japan
Note: 1. Revision rates are calculated as the percentage change of the figures between the current and the previous survey.
2. The graph indicates the revision pattern of fixed investment. Namely, the first survey for each fiscal year (March survey) is on the left, and the last survey (June survey of the following year; actual result) is on the right.