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# BOJ December 2015 Tankan Survey

## Business sentiment marking time, future uncertain

Economic Intelligence Team  
**Satoshi Osanai**  
**Shunsuke Kobayashi**

### Summary

- In the BOJ December Tankan survey of corporate sentiment, the current trend in business sentiment is unexpectedly marking time despite predictions that it would worsen. However, corporations have become more cautious regarding the future. Behind the sense of caution lies fears of worldwide economic slowdown centering on China, as well as worries regarding stagnant exports and production, as well as slow pace of recovery in personal consumption. Our assessment of Japan's economy is that it is in a temporary lull, and that the December BOJ Tankan reflects this, showing the recent domestic economy to be in a temporary lull overall. As for capex, the non-manufacturing industries remain positive, while manufacturing is somewhat on the cautious side.
- The business conditions DI for large manufacturers (+12%pt in comparison with last survey's +12%pt) is marking time, while at the same time exceeding market consensus (+11%pt). Business conditions DI for large non-manufacturing industries also marked time (+25%pt) in comparison to the previous survey. A reactionary decline was expected for the non-manufacturing industries due to the fast pace of growth it had experienced recently, but business sentiment has retained underlying strength.
- Sales projections of large corporations (all industries) for FY2015 are down by -1.1% y/y, with recurring profits expected to be up by +6.5% y/y. Sales are weak due to the personal consumption situation, and stagnant exports have led to a slight decline in earnings. On the other hand, recurring profits are expected to win a healthy increase due to improved margins associated with price hikes and the low price of natural resources.
- The FY 2015 capex projection for all corporations in all industries (incl. investment in properties but excl. that in software; all industries, large companies) is +7.8% y/y, an upward revision from the previous report (+6.4%). Capital expenditure plans on the December survey reflect a certain quirk in statistics whereby upward revisions tend to occur, especially for small enterprises. As in the case of the September Tankan, upward revisions of capex projections are considerably larger than the usual pattern, especially for the non-manufacturing industries.

## Business sentiment marking time amongst major manufacturers

In the BOJ December Tankan survey of corporate sentiment, the current trend in business sentiment is unexpectedly marking time despite predictions that it would worsen. However, corporations have become more cautious regarding the future. Behind the sense of caution lies fears of worldwide economic slowdown centering on China, as well as worries regarding stagnant exports and production, as well as slow pace of recovery in personal consumption. Our assessment of Japan's economy is that it is in a temporary lull, and that the December BOJ Tankan reflects this, showing the recent domestic economy to be in a temporary lull overall. As for capex, the non-manufacturing industries remain positive, while manufacturing is somewhat on the cautious side.

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The materials industries were marking time. Margins improved due to low prices for natural resources and energy, but while this was a plus for business conditions DI, the worsening of the commodities market was a drag on performance in some industries. As for performance of individual industries, chemicals and iron & steel saw improvements. Chemicals continued to reap the benefits of cheap crude oil leading to improved earnings, as well as bringing a positive contribution to overall industry performance. On the other hand, iron & steel are still faced with a difficult business environment, and it is thought that current results are merely a reaction to the two previous quarters of negative performance. Meanwhile, petroleum and coal products marked time. On the September survey business sentiment for the industry was foreseen as improving greatly in the future. However, the price of crude oil fell much more than had been predicted at the time, bringing major declines falling well below the September outlook. Other industries which saw business sentiment worsen include non-ferrous metals. A decline in the price of products for the non-ferrous metals industry associated with a worsening commodities market is thought to be behind the negative performance. Other industries recording poor performance were textiles, pulp & paper, lumber & wood products, and ceramics, stone & clay.

The processing industries saw a worsening of business sentiment for the second consecutive quarter. Negative factors included stagnant exports and production due to the downturn in overseas economies. In addition, the slow pace of recovery in personal consumption has also weighed down on corporate business sentiment. As for performance of individual industries, worsening was especially noticeable in production machinery, electrical machinery, and automobiles. As for production machinery, on average things were improving in recent months, but due to the slowdown in both domestic and overseas capital investment demand, this area is now showing strong signs of peaking out. Electrical machinery has been weighed down by stagnant exports and production. Meanwhile, automobiles have seen some improvement in domestic sales of new vehicles, which had temporarily declined in association with the increase in tax on light vehicles in April of 2015, but all in all, number of units sold was still down, bringing a negative contribution to overall performance on this month's survey. As for other industries, shipbuilding, heavy machinery, and other transport machinery are seen a gradual comeback in orders leading to improvement, while general-purpose machinery, business oriented machinery, and food & beverages saw improvement due to rebound from the negative results of September.

Business conditions DI for large non-manufacturing industries also marked time (+25%pt) in comparison to the previous survey. A reactionary decline was expected for the non-manufacturing industries due to the fast pace of growth it had experienced recently, but business sentiment has retained underlying strength.

Looking at performance by industry, improvements were especially noticeable in construction and accommodations, eating & drinking services. Business conditions DI worsened for construction due to the decline in public investment and slow growth for housing starts, but the number of construction projects is at a high, bringing a positive note to performance. As for accommodations, eating & drinking services, the domestic travel market retains a steady undertone, while inbound tourist consumption associated with visits to Japan by foreign tourists has been favorable. Meanwhile, electric & gas utilities were seen worsening according to the outlook in the September survey, but profit margins continue to improve thanks to the fall in energy import prices, thereby contributing improvement in business sentiment despite the outlook on the previous survey. On the other hand, some industries worsened, including retailing and services for individuals. However, the worsening in these industries is also thought to be due to the reaction to the quick pace of improvement in the previous months, and hence should not be interpreted negatively. Real estate has seen the benefits of a decline in the vacancy rate, but sluggish condominium sales and the negative influence of the recent incident regarding falsification of condominium construction data have caused results to worsen for the first time in five quarters. Meanwhile, goods rental & leasing and services for businesses suffered a major worsening of results. It appears that the sense of uncertainty regarding the business environment has grown stronger despite the favorable performance experienced until now.

### **Large corporations in both manufacturing and non-manufacturing industries see worsening in future**

Looking at the future outlook for business conditions DI, both the manufacturing and non-manufacturing industries see conditions worsening, with large manufacturers expecting +7%pt (down by -5pt in comparison to the current survey), and +18%pt seen for major non-manufacturers (a decline of -7pt). Corporations appear to have become more cautious regarding the future due to fears of worldwide economic slowdown centering on China, stagnant exports and production, and the slow pace of recovery in personal consumption. The fact that a broad range of industries in both manufacturing and non-manufacturing see business worsening is cause of concern.

### **Overseas supply and demand worsens slightly in manufacturing industry**

Taking a look at large corporations' supply-demand conditions DI for domestic products and services, we see that the manufacturing industry is marking time, while the non-manufacturing industry has worsened. As for large corporations' supply-demand conditions DI for overseas products and services, there was a modest drop in comparison to the previous report due to the influence of the worldwide economic slowdown especially in China. The weakness of overseas demand is becoming clearer.

Meanwhile, looking at price conditions DI, the price of crude oil has dropped further since the previous survey, bringing a decline in input price conditions DI for both the manufacturing and non-manufacturing industries. This has brought an improvement in the terms of trade (output price conditions DI – input price conditions DI).

### **Upward revision of recurring profits seen for large corporations**

Sales projections of large corporations (all industries) for FY2015 are down by -1.1% y/y, with recurring profits expected to be up by +6.5% y/y. Sales are weak due to the personal consumption situation, and stagnant exports have led to a slight decline in earnings. On the other hand, recurring profits are expected to win a healthy increase due to improved margins associated with price hikes and the low price of natural resources. The amendment ratio in comparison to the previous survey shows a downward revision for sales (-1.5%) and an upward revision for recurring profits (+1.7%).

Recurring profits were revised downwards in the manufacturing industry (-0.5%), but revised upwards for non-manufacturing (+4.0%). The assumed exchange rate in the second half of FY2015 for major manufacturers is 118 yen to the dollar. Considering the current yen exchange rate, it appears that manufacturers are being a bit conservative in their projections.

## **FY2015 capex projections favorable for non-manufacturing**

The FY 2015 capex projection for all corporations in all industries (incl. investment in properties but excl. that in software; all industries, large companies) is +7.8% y/y, an upward revision from the previous report (+6.4%). Capital expenditure plans on the December survey reflect a certain quirk in statistics whereby upward revisions tend to occur, especially for small enterprises. As in the case of the September Tankan, upward revisions of capex projections are considerably larger than the usual pattern, especially for the non-manufacturing industries.

Large corporations attracting the most attention from the market revised projections by +10.8% y/y (+10.9% on the previous report), a downward revision in comparison to the previous survey. This exceeded market consensus at +10.2%. On an industry by industry basis, major manufacturers revised their capex projections for FY2015 upwards by +15.5% y/y, while major non-manufacturers revised their capex projections upwards by +8.5% y/y. Upward revisions of capex projections on the current survey show a bit of caution on the part of major manufacturers, while non-manufacturers remain favorable in their level of willingness to invest. The manufacturing industry appears to have been somewhat influenced by the slowdown in overseas economies, as well as stagnant exports and production.

Meanwhile, production capacity DI for major manufacturers was +3%pt, an increase of +2pt in comparison to the previous survey (representing a worsening). Meanwhile, major non-manufacturers marked time in comparison to the previous survey at -1%pt, continuing negative DI levels (deficiency). No sense of overcapacity was seen in production capacity DI. However, the manufacturing industry does seem somewhat more cautious as regards capital expenditure plans. Moreover, the worsening of production capacity DI is cause for concern.

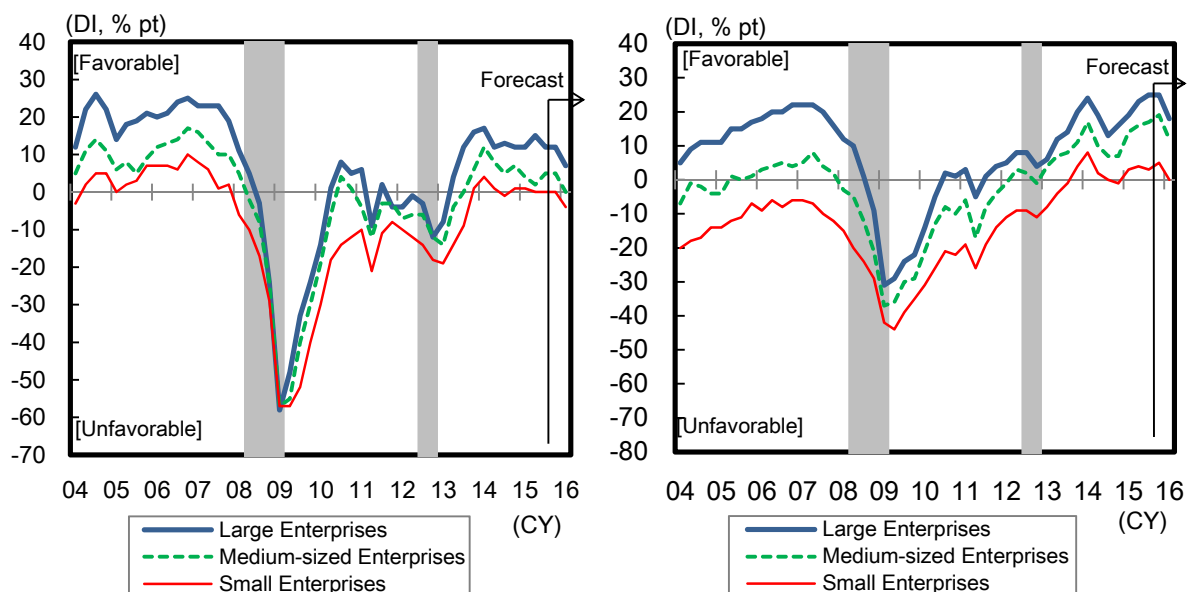
## **Focus for the future is risk of downswing in inflation outlook**

The December BOJ Tankan results show growing uncertainty as regards the future, yet there is still no sign of expectation for new economic or monetary policy measures in the immediate future.

The BOJ gives the same assessment in its September financial and economic monthly report. However, these statements are on the strong side in consideration of recent economic indices and this month's Tankan. Considering the negative outlook on the BOJ Tankan and the real GDP growth rate for the Jul-Sep 2015 period, which is expected to be weak, these assessments of the economy may be revised downward in the future.

As for monetary policy, the BOJ has been saying that it will be carefully watching CPI results (less fresh foods and energy), and that from the viewpoint of prices, it would be difficult to decide immediately on additional monetary easing. The issue which we are watching closely is the fact that downward risk is rising in relation to Japan's economic and price situation with the drop in the price of natural resources and energy since summer beginning with crude oil. The factor to watch in the immediate future is the December 15 announcement of the BOJ's inflation outlook of enterprises. Of note will be whether or not the expected inflation rate of companies is revised downwards.

Business Conditions DI Chart 1



Source: Bank of Japan, Cabinet Office; 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					
	Sept. 2015 Survey		Dec. 2015 Survey				Sept. 2015 Survey		Dec. 2015 Survey			
	Actual result	Forecast	Actual result	Changes	Forecast	Changes	Actual result	Forecast	Actual result	Changes	Forecast	Changes
Manufacturing	12	10	12	0	7	-5	0	-2	0	0	-4	-4
Textiles	6	6	-5	-11	0	5	-16	-20	-8	8	-14	-6
Lumber & Wood products	18	0	17	-1	6	-11	-5	-9	1	6	-10	-11
Pulp & Paper	7	7	3	-4	3	0	-5	-6	-8	-3	-10	-2
Chemicals	14	11	20	6	13	-7	12	10	14	2	7	-7
Petroleum & Coal products	-11	0	-11	0	5	16	-17	-23	-9	8	-20	-11
Ceramics, Stone & Clay	14	14	13	-1	9	-4	2	1	6	4	-4	-10
Iron & Steel	-5	-7	0	5	-9	-9	-4	-5	-8	-4	-15	-7
Nonferrous metals	11	14	0	-11	-5	-5	-2	-3	-4	-2	2	6
Food & Beverages	13	13	17	4	9	-8	0	-1	5	5	4	-1
Processed metals	-5	2	0	5	5	5	0	0	-2	-2	-5	-3
General-purpose machinery	14	12	16	2	14	-2	19	10	9	-10	4	-5
Production machinery	32	17	22	-10	9	-13	19	4	7	-12	-1	-8
Business oriented machinery	16	14	20	4	16	-4	13	10	9	-4	6	-3
Electrical machinery	12	9	3	-9	6	3	-5	-3	-5	0	-9	-4
Shipbuilding & Heavy machinery, etc.	7	3	18	11	10	-8	18	11	12	-6	10	-2
Motor vehicles	14	11	11	-3	3	-8	5	6	7	2	7	0
Basic materials	9	7	9	0	6	-3	-3	-5	-1	2	-7	-6
Processing	14	11	12	-2	8	-4	3	0	2	-1	-1	-3
Nonmanufacturing	25	19	25	0	18	-7	3	1	5	2	0	-5
Construction	38	31	41	3	31	-10	10	3	11	1	-1	-12
Real estate	38	32	35	-3	26	-9	10	5	9	-1	6	-3
Goods rental & Leasing	34	26	23	-11	23	0	14	12	17	3	10	-7
Wholesaling	9	6	8	-1	7	-1	-5	-3	-2	3	-4	-2
Retailing	25	19	22	-3	14	-8	-9	-9	-9	0	-10	-1
Transport & Postal activities	23	17	26	3	17	-9	6	0	9	3	0	-9
Communications	33	6	44	11	5	-39	19	12	21	2	26	5
Information services	25	27	30	5	27	-3	10	8	15	5	16	1
Electric & Gas utilities	0	-5	2	2	-5	-7	22	13	10	-12	10	0
Services for businesses	31	24	20	-11	20	0	6	1	8	2	-1	-9
Services for individuals	35	23	32	-3	16	-16	2	-1	7	5	-2	-9
Accommodations, Eating & Drinking services	31	15	32	1	18	-14	7	1	9	2	4	-5
All industries	19	14	18	-1	13	-5	3	0	3	0	-2	-5

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

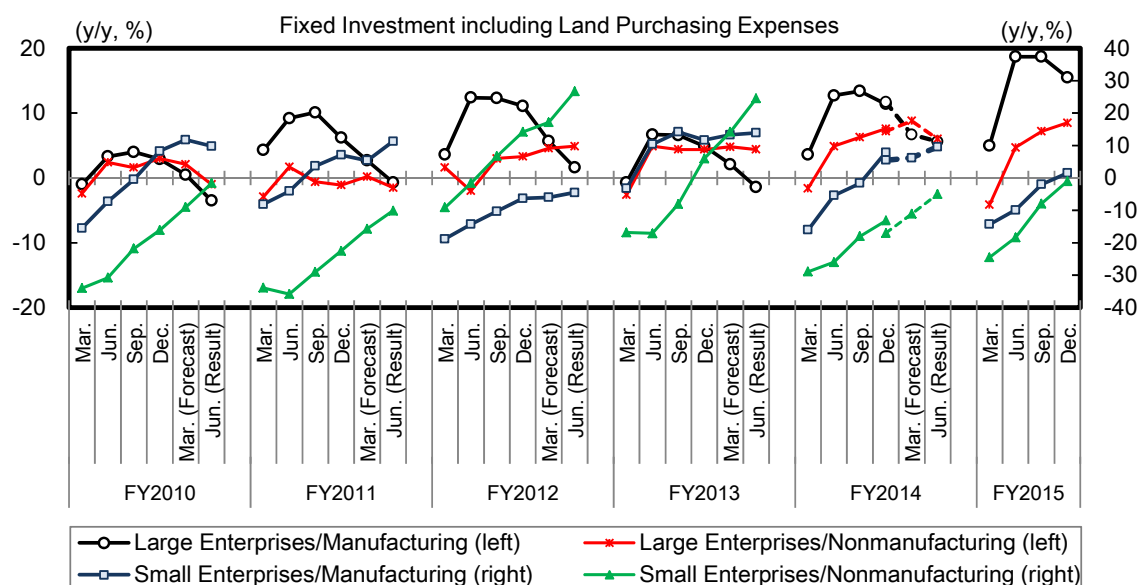
Sales		(Year-to-year % change)			Current Profits		(Year-to-year % change)		
		FY2014	FY2015 (Forecast)	Revision rate			FY2014	FY2015 (Forecast)	Revision rate
Large Enterprises	Manufacturing	1.3	-0.3	-1.1	Large Enterprises	Manufacturing	11.5	3.3	-0.5
	Domestic Sales	-0.6	-1.8	-1.7		Basic materials	0.1	8.9	-1.3
	Exports	5.9	3.4	0.2		Processing	16.1	1.3	-0.2
	Nonmanufacturing	0.5	-1.6	-1.7		Nonmanufacturing	3.7	9.9	4.0
	All industries	0.8	-1.1	-1.5		All industries	7.6	6.5	1.7
Medium-sized Enterprises	Manufacturing	1.9	1.6	0.0	Medium-sized Enterprises	Manufacturing	11.8	8.6	2.2
	Nonmanufacturing	0.2	0.8	-0.3		Nonmanufacturing	-0.6	3.1	4.1
	All industries	0.6	1.0	-0.2		All industries	3.1	4.9	3.5
Small Enterprises	Manufacturing	1.2	0.1	-0.3	Small Enterprises	Manufacturing	8.6	3.1	0.2
	Nonmanufacturing	0.0	-0.5	0.0		Nonmanufacturing	0.8	1.5	2.6
	All industries	0.2	-0.4	0.0		All industries	2.6	1.9	2.0
All Enterprises	Manufacturing	1.4	0.1	-0.8	All Enterprises	Manufacturing	11.2	3.8	-0.1
	Nonmanufacturing	0.3	-0.7	-0.9		Nonmanufacturing	2.2	6.5	3.7
	All industries	0.6	-0.5	-0.8		All industries	5.9	5.4	2.0

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)				Software Investment (Year-to-year % change)					
		FY2014	FY2015 (Forecast)	Revision rate			FY2014	FY2015 (Forecast)	Revision rate
Large Enterprises	Manufacturing	5.6	15.5	-2.7	Large Enterprises	Manufacturing	5.5	3.4	-0.9
	Nonmanufacturing	6.0	8.5	1.3		Nonmanufacturing	-1.5	1.9	-0.8
	All industries	5.9	10.8	-0.1		All industries	0.8	2.4	-0.8
Medium-sized Enterprises	Manufacturing	8.7	11.3	1.1	Medium-sized Enterprises	Manufacturing	3.6	4.0	-5.2
	Nonmanufacturing	1.9	1.3	3.4		Nonmanufacturing	-1.2	11.5	7.0
	All industries	4.2	4.8	2.5		All industries	-0.4	10.3	4.9
Small Enterprises	Manufacturing	9.6	1.5	3.5	Small Enterprises	Manufacturing	1.3	-3.7	-0.5
	Nonmanufacturing	-5.0	-1.0	7.6		Nonmanufacturing	29.7	-1.9	1.2
	All industries	-0.8	-0.2	6.3		All industries	19.7	-2.5	0.7
All Enterprises	Manufacturing	6.8	12.2	-1.1	All Enterprises	Manufacturing	5.1	2.9	-1.2
	Nonmanufacturing	3.1	5.6	2.7		Nonmanufacturing	0.6	3.1	0.6
	All industries	4.3	7.8	1.3		All industries	2.0	3.0	0.1



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.