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December 2015 Machinery Orders

Orders grow for first time in two months. Growth trend seen continuing in Jan-Mar Period of 2016

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Summary

- According to statistics for machinery orders in December 2015, the leading indicator for domestic capex, private sector demand (excluding shipbuilding and electrical power), orders grew for the first time in two months at +4.2% m/m, pretty much in tune with market consensus at +4.4%. Moreover, the Oct-Dec period's performance in comparison to the previous period was +4.3%, exceeding the Cabinet Office's outlook by +2.9%. However, considering the fact that Jul-Sep period performance fell by -10.0% q/q, the extent of growth is not great, though Oct-Dec period performance shows orders to be definitely making a comeback.

- Looking at orders by source of demand in December, the manufacturing industries suffered declines for the second consecutive month at -3.4% m/m. However, our assessment is that on average, performance continues to mark time. Meanwhile, the non-manufacturing industries (excluding shipbuilding and electrical power) grew for the first time in two months at +8.5% m/m.

- Machinery orders are expected to gradually recover to a growth trend. According to the December BOJ Tankan, manufacturers are cautious in regard to capex, while non-manufacturing maintains a healthy attitude toward capital expenditure. With favorable domestic demand, the non-manufacturing industries are expected to carry out investment in energy saving and labor saving as a means of dealing with the shortage of manpower. The BOJ's introduction of negative interest is expected to bring down capital procurement costs for corporations, and this should bring further underlying support for capex. However, the sense of uncertainty regarding the future of the world economy is growing stronger, and this is a point which gives pause. Corporations may become even more cautious in regard to capex spending due to the worsening of the external environment, especially amongst export driven manufacturers.

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

	2015 Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec
Machinery orders (private sector)*	2.5	-1.4	2.9	3.8	0.6	-7.9	-3.6	-5.7	7.5	10.7	-14.4	4.2
Market consensus (Bloomberg)												4.4
DIR estimate												8.5
Manufacturing orders	-3.2	-0.6	0.3	10.5	9.9	-14.0	-5.3	-3.2	-5.5	14.5	-10.2	-3.4
Non-manufacturing orders*	8.0	-5.0	4.7	-0.6	-4.0	0.6	-6.0	-6.1	14.3	10.7	-18.0	8.5
Overseas orders	14.2	6.6	-13.5	-7.0	3.7	20.3	10.2	-26.1	4.8	41.6	-25.0	-3.1

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

December orders grow for first time in two months, but lacking in energy

According to statistics for machinery orders in December 2015, the leading indicator for domestic capex, private sector demand (excluding shipbuilding and electrical power), orders grew for the first time in two months at +4.2% m/m, pretty much in tune with market consensus at +4.4%. Moreover, the Oct-Dec period's performance in comparison to the previous period was +4.3%, exceeding the Cabinet Office's outlook by +2.9%. However, considering the fact that Jul-Sep period performance fell by -10.0% q/q, the extent of growth is not great, though Oct-Dec period performance shows orders to be definitely making a comeback.

Manufacturing orders suffer decline for second consecutive month, but on average, performance continues to mark time

Looking at orders by source of demand in December, the manufacturing industries suffered declines for the second consecutive month at -3.4% m/m. However, our assessment is that on average, performance continues to mark time.

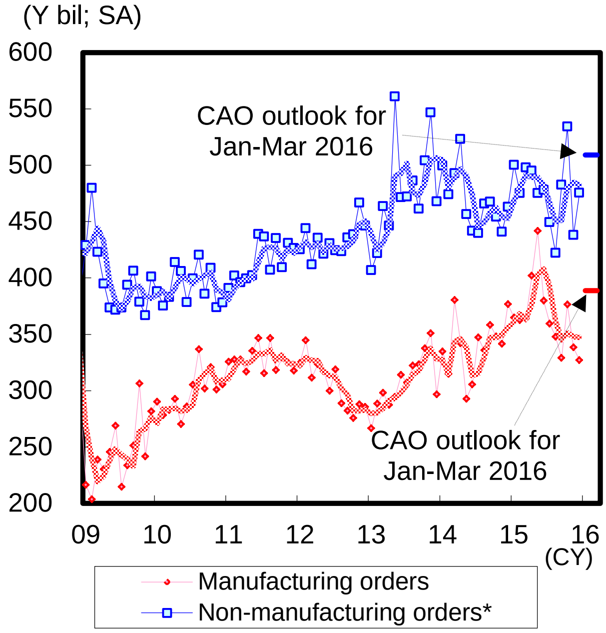
As for performance by industry, the following industries especially contributed to the overall decline: Other manufacturing (-21.4% m/m), chemicals (-26.3%), automobiles, parts & accessories (-7.9%), and general machinery (-3.3%). Other manufacturing recorded its second consecutive month of decline, while automobiles, parts & accessories continued to mark time, and chemicals are actually in the midst of a gradual growth trend despite this month's decline. On the other hand, general machinery declined for the second consecutive month and is showing signs of orders peaking out. In contrast to these industries, electrical machinery (+29.4%) and information & communication electronics equipment (+35.3%) achieved major rebounds after having contributed to negative performance during the previous month.

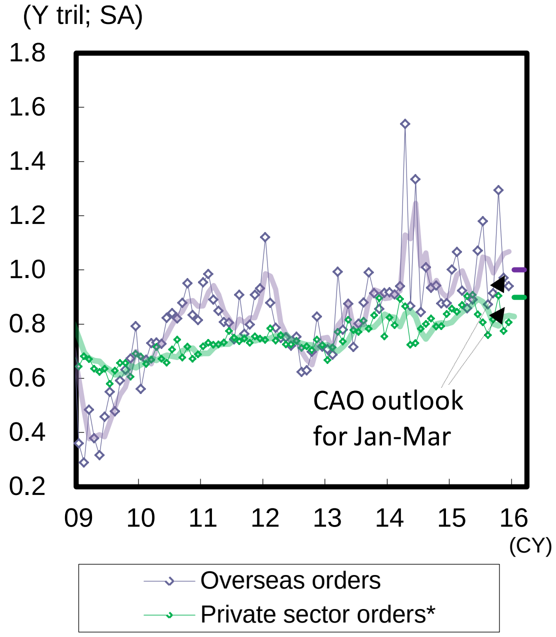
Non-manufacturing industries achieve growth for first time in two months in rebound from the previous month's steep declines

Non-manufacturing orders (excluding shipbuilding and electric power) grew for the first time in two months at +8.5% m/m. This is considered to be most likely a rebound from November's steep declines (-18.0%), but one lacking somewhat in energy. However, all in all, non-manufacturing is continuing to mark time.

Looking at performance by industry, finance and insurance (+43.2%), telecommunications (+31.4%), and transportation and postal activities (+18.1%) contributed to the positive results. As for finance and insurance, fluctuations continue on a monthly basis, but on average, the growth trend is continuing. As for transportation and postal activities, here too the growth trend continues. On the other hand, other non-manufacturing (-9.3% m/m) as well as construction (-8.3%) suffered declines. Construction has recorded declines for the past three months straight and is clearly in a declining phase.

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



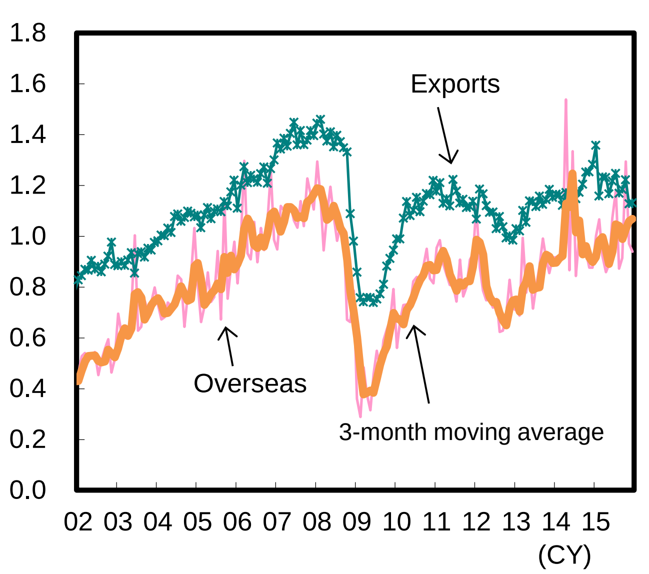


Source: Cabinet Office (CAO); compiled by DIR.
*excl. those for shipbuilding and from electric utilities.
Note: Thick lines 3M/MA basis.

Overseas orders do not encourage an optimistic view of the future

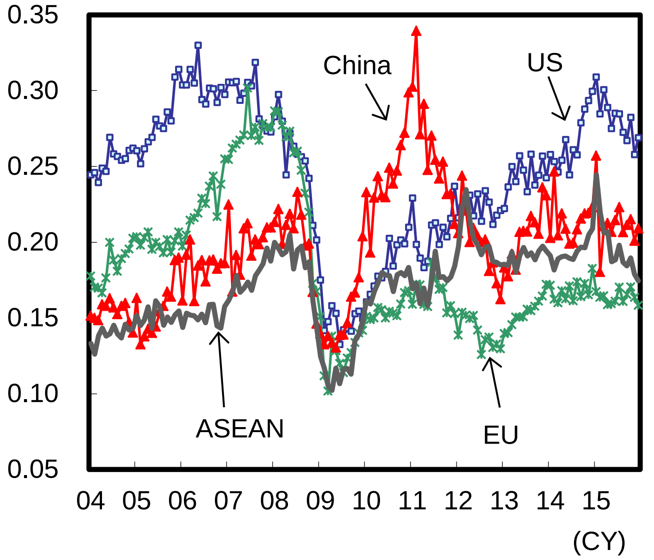
Overseas demand declined for the second consecutive month at -3.1% m/m, but in terms of the three-month moving average, it appears to be maintaining a growth trend. However, the future of overseas demand does not encourage optimism. The sense of uncertainty regarding the world economy is growing stronger with the Fed's interest rate hikes, the low price of crude oil, and fears that China's economic growth will grow even more sluggish. Japan's exports of capital goods may become stagnant in the future.

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 3M/MA basis.

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

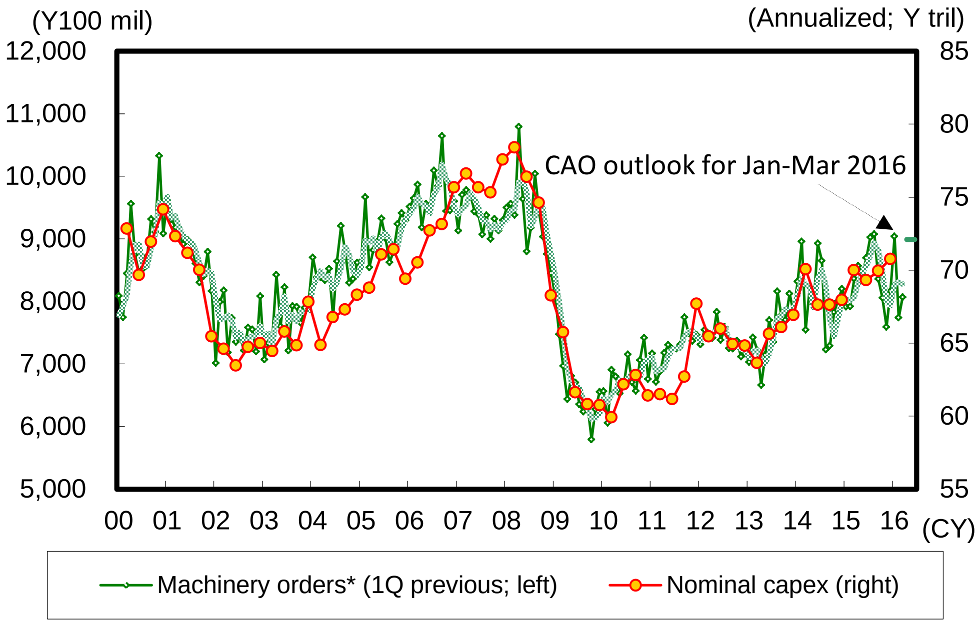


Source: Ministry of Finance; compiled by DIR.
Note: SA by DIR.

Machinery orders expected to gradually recover to a growth trend

Machinery orders are expected to gradually recover to a growth trend. According to the December BOJ Tankan, manufacturers are cautious in regard to capex, while non-manufacturing maintains a healthy attitude toward capital expenditure. With favorable domestic demand, the non-manufacturing industries are expected to carry out investment in energy saving and labor saving as a means of dealing with the shortage of manpower. The BOJ’s introduction of negative interest is expected to bring down capital procurement costs for corporations, and this should bring further underlying support for capex. However, the sense of uncertainty regarding the future of the world economy is growing stronger, and this is a point which gives pause. Corporations may become even more cautious in regard to capex spending due to the worsening of the external environment, especially amongst export driven manufacturers.

Domestic Demand and Nominal Capex **Chart 5**



Source: Cabinet Office (CAO); compiled by DIR.
Note: Excluding those for shipbuilding and from electric utilities; thick lines 3M/MA basis.