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March 2016 Machinery Orders

March orders grow for first time in two months. Domestic demand enters moderate growth trend

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Summary

- According to statistics for machinery orders in March 2016, the leading indicator for domestic capex, private sector demand (excluding shipbuilding and electrical power), orders grew for the first time in two months at +5.5% m/m in defiance of market consensus (-2.0%). Results show Jan-Mar period domestic demand to have achieved growth of +6.7% in comparison to the previous quarter, and exceeded the Cabinet Office's official outlook of +6.4% q/q.

- Looking at orders by source of demand in March, the manufacturing industries grew for the first time in two months at +19.7% m/m. Non-ferrous metals and shipbuilding won major growth, helping to push up the amount in overall orders, defeating the effects of last February's steep reactionary decline. Non-manufacturing orders (excluding shipbuilding and electric power) declined for the first time in four months at -6.9% m/m. however, when non-manufacturing orders are averaged out, they are still approaching a growth trend.

- Machinery orders, the leading indicator for capex, are expected to mark time in the future. With supply and demand for labor remaining tight, the non-manufacturing industries, which are not so easily influenced by overseas demand, are expected to maintain stable business performance, which should encourage investment in rationalization and labor-saving devices. Meanwhile, demand for machinery is expected to expand, especially for equipment oriented toward restoration and reconstruction of production facilities lost or damaged in the recent Kumamoto earthquake. On the other hand, a worsening external environment as seen in the slowdown of the world economy and the accelerating tendency toward a strong yen/weak dollar situation will likely become a drag on the business performance of export-driven industries, especially in manufacturing, and this is cause for concern. If the assumption of good business performance, which provides the support for capex spending, should collapse, the number of corporations putting off capex spending could increase.

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

	2015 Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	2016 Jan	Feb	Mar
Machinery orders (private sector)*	3.2	2.9	-6.6	-3.0	-2.9	5.9	6.4	-9.7	1.0	15.0	-9.2	5.5
Market consensus (Bloomberg)												-2.0
DIR estimate												3.2
Manufacturing orders	2.5	3.7	-5.6	-4.0	-3.4	-3.5	6.2	-6.6	-3.0	41.2	-30.6	19.7
Non-manufacturing orders*	0.4	-0.4	-0.9	-7.3	-1.7	13.7	5.2	-12.7	4.5	1.0	10.2	-6.9
Overseas orders	-5.3	4.1	7.9	8.5	-17.1	4.4	31.6	-20.1	-2.2	-29.4	6.3	28.5

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

March orders grow for first time in two months. Domestic demand enters moderate growth trend

According to statistics for machinery orders in March 2016, the leading indicator for domestic capex, private sector demand (excluding shipbuilding and electrical power), orders grew for the first time in two months at +5.5% m/m in defiance of market consensus (-2.0%). Results show Jan-Mar period domestic demand to have achieved growth of +6.7% in comparison to the previous quarter, and exceeded the Cabinet Office's official outlook of +6.4% q/q. However, this was due to special factors – large-scale orders taken in by the steel industry in January. The amount of orders originating from domestic demand during the Jan-Mar period excluding steel grew by +2.2% q/q (DIR est), hence our assessment is that machinery orders are now in a moderate growth trend.

Manufacturing orders win major grow for first time in two months after suffering reactionary decline in February

Looking at orders by source of demand in March, the manufacturing industries grew for the first time in two months at +19.7% m/m. Non-ferrous metals and shipbuilding won major growth, helping to push up the amount in overall orders, defeating the effects of last February's steep reactionary decline.

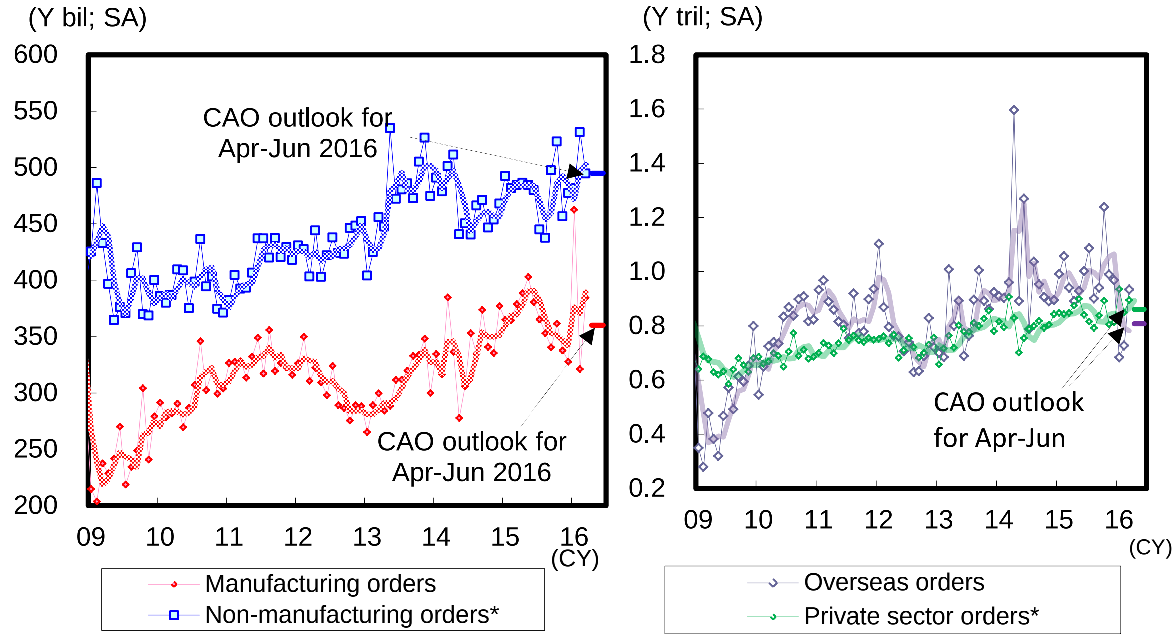
As for performance by industry, positive contributions were made by non-ferrous metals (+270.4% m/m), shipbuilding (+89.7%), general purpose and production machinery (+17.8%), and other manufacturing (+19.4%). Non-ferrous metals have been chalking up major gains since last month and are thought to have received large-scale orders. Meanwhile, shipbuilding achieved major growth for the first time in two months, but considering the fact that the world economy has been stagnant, this may be merely a temporary spike in orders. General purpose and production machinery grew for the first time in two months, and appears to have shifted into a moderate growth phase. On the other hand, four industries suffered declines, including electrical machinery (-19.1% m/m), other transport equipment (-21.5%), pulp, paper & paper products (-51.6%), and information & communication electronics equipment (-10.5%). As for electrical machinery, declines were experienced for the third consecutive month, a clear sign that orders are in a downward trend. Demand for smartphones is in a worldwide downward trend, hence the decline in demand for the type of machinery manufactured by this industry. Other transport equipment declined for the second consecutive month, reflecting the declining trend in that industry which has continued since the middle of last year.

Non-manufacturing industries decline for first time in four months, but on average the growth trend continues

Non-manufacturing orders (excluding shipbuilding and electric power) declined for the first time in four months at -6.9% m/m. however, when non-manufacturing orders are averaged out, they are still approaching a growth trend.

Looking at performance by industry, overall results were pulled down by finance and insurance (-27.7% m/m), transportation & postal activities (-20.5%), and information services (-19.0%). Finance and insurance declined for the second consecutive month, though on average orders are marking time. As for transportation & postal activities, the industry has been moving toward peaking out since the end of last year due to the slowdown in the domestic economy. On the other hand, growth was seen in other non-manufacturing (+18.3% m/m), wholesale and retail trade (+9.9%), and real estate (+51.8%). Real estate has been in a growth trend since the end of last year, having become more vibrant after lower interest rates were introduced.

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

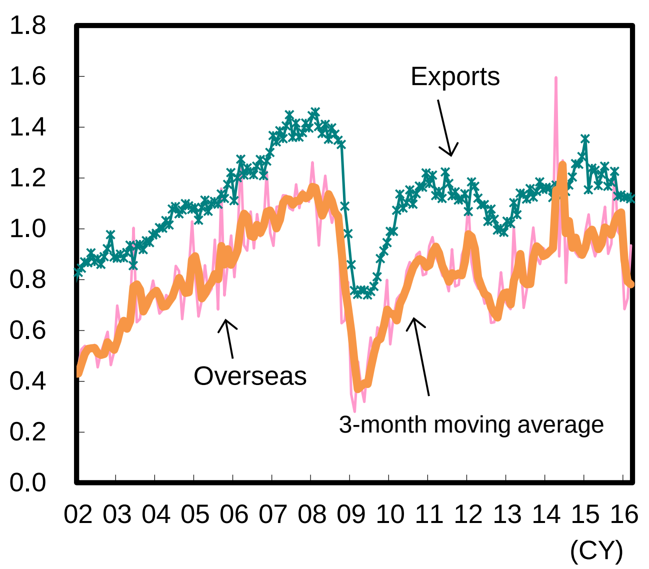


Source: Cabinet Office (CAO); compiled by DIR.
*excl. those for shipbuilding and from electric utilities.
Note: Thick lines 3M/MA basis.

Overseas orders win growth for second consecutive month, with aircraft and railroad cars especially brisk

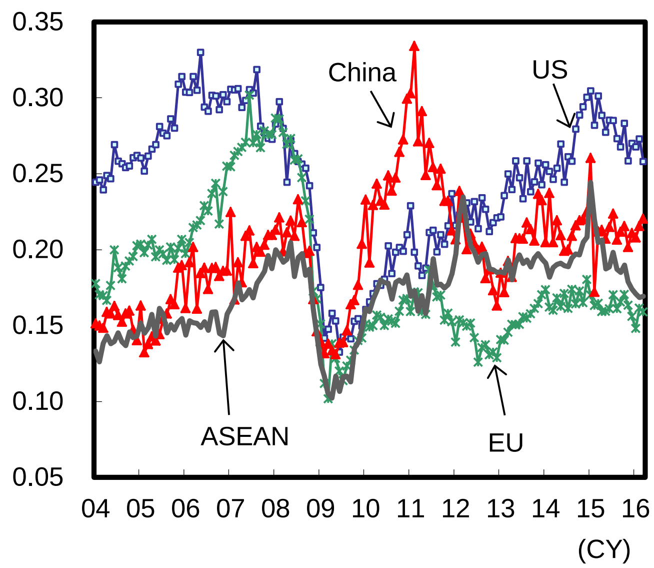
Overseas demand achieved growth for the second consecutive month at +28.5% m/m. The source of major growth was aircraft and railroad cars. However, the world economy has been quieting down somewhat in comparison to the beginning of the year and the US economy, which maintained a favorable tone last year, is also beginning to slow down. Hence a variety of uncertain factors have begun to surface. As for the future of the overseas demand, we expect a gradual comeback, but in the short-term, we prefer to approach the situation with care.

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**



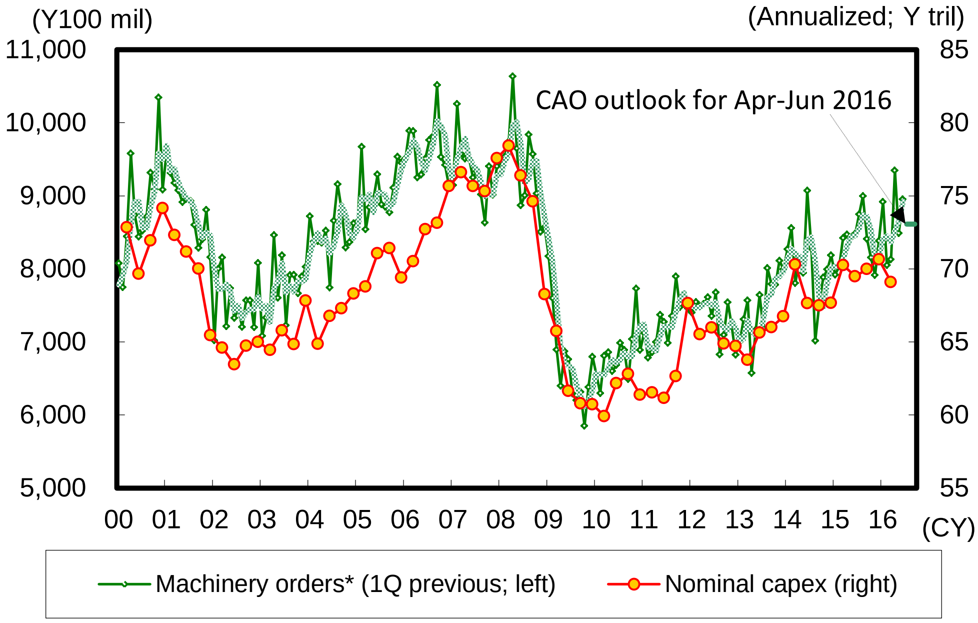
Source: Ministry of Finance; compiled by DIR.
Note: SA by DIR.

Machinery orders expected to mark time in the future

The Cabinet Office has announced its official outlook for the Apr-Jun period, predicting a decline of -3.5% q/q for domestic demand (excluding shipbuilding and electrical power), representing a turnaround in the negative direction in comparison to the Jan-Mar period.

Machinery orders, the leading indicator for capex, are expected to mark time in the future. With supply and demand for labor remaining tight, the non-manufacturing industries, which are not so easily influenced by overseas demand, are expected to maintain stable business performance, which should encourage investment in rationalization and labor-saving devices. Meanwhile, demand for machinery is expected to expand, especially for equipment oriented toward restoration and reconstruction of production facilities lost or damaged in the recent Kumamoto earthquake. On the other hand, a worsening external environment as seen in the slowdown of the world economy and the accelerating tendency toward a strong yen/weak dollar situation will likely become a drag on the business performance of export-driven industries, especially in manufacturing, and this is cause for concern. If the assumption of good business performance, which provides the support for capex spending, should collapse, the number of corporations putting off capex spending could increase.

Domestic Demand and Nominal Capex (seasonally adjusted figures) **Chart 5**



Source: Cabinet Office (CAO); compiled by DIR.

Note: Excluding those for shipbuilding and from electric utilities; thick lines 3M/MA basis.