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July 2016 Machinery Orders

July orders grow +4.9% -- good start towards achieving CAO outlook

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Summary

- According to statistics for machinery orders in July 2016, the leading indicator for domestic capex and private sector demand (excluding ships and electrical power), orders grew for the second consecutive month by +4.9% m/m, while also exceeding market consensus at -2.9%. The figure represents a good start towards achieving the Cabinet Office's outlook of +5.2% q/q for the Jul-Sep period.

- Looking at orders by source of demand in July, the manufacturing industries grew a small amount for the second consecutive month by +0.3% m/m. Non-manufacturing orders (excluding ships and electric power) also grew for the second consecutive month by +8.6% m/m. Overseas orders declined for the first time in two months by -11.7% m/m.

- Machinery orders, the leading indicator for capex, are expected to win moderate growth in the future. With supply and demand for labor remaining tight, investment in rationalization and labor-saving devices is likely, while at the same time, the non-manufacturing industries are expected to carry out investment in transport and distribution infrastructure. However, the slowdown of the world economy and the growing tendency toward a strong yen/weak dollar situation will likely effect domestic demand, and there is the growing sense that corporate earnings are about to peak out. In this context we must keep in mind the possibility that corporations may therefore become more cautious as regards capex spending.

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

	2015					2016						
	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	Jul
Machinery orders (private sector)*	-2.9	5.9	6.4	-9.7	1.0	15.0	-9.2	5.5	-11.0	-1.4	8.3	4.9
Market consensus (Bloomberg)												-2.9
DIR estimate												-2.5
Manufacturing orders	-3.4	-3.5	6.2	-6.6	-3.0	41.2	-30.6	19.7	-13.3	-6.4	17.7	0.3
Non-manufacturing orders*	-1.7	13.7	5.2	-12.7	4.5	1.0	10.2	-6.9	-3.9	-0.3	2.1	8.6
Overseas orders	-17.1	4.4	31.6	-20.1	-2.2	-29.4	6.3	28.5	-6.9	-14.8	10.8	-11.7

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

July orders grow for second consecutive month, continuing steady undertone of recent months

According to statistics for machinery orders in July 2016, the leading indicator for domestic capex and private sector demand (excluding ships and electrical power), orders grew for the second consecutive month by +4.9% m/m, while also exceeding market consensus at -2.9%. The figure represents a good start towards achieving the Cabinet Office's outlook of +5.2% q/q for the Jul-Sep period. Both the manufacturing and non-manufacturing sectors achieved growth in orders for the second consecutive month, leading to the conclusion that machinery orders are continuing the steady undertone of recent months.

Manufacturing orders grow slightly for second consecutive month despite reaction to previous month's results

Looking at orders by source of demand in July, the manufacturing industries grew a small amount for the second consecutive month by +0.3% m/m, likely reflecting a reaction to large size orders recorded during the previous month by other transport equipment. On the other hand, July saw favorable orders for iron & steel, and fabricated metal products, helping to keep the manufacturing industry overall in the positive numbers.

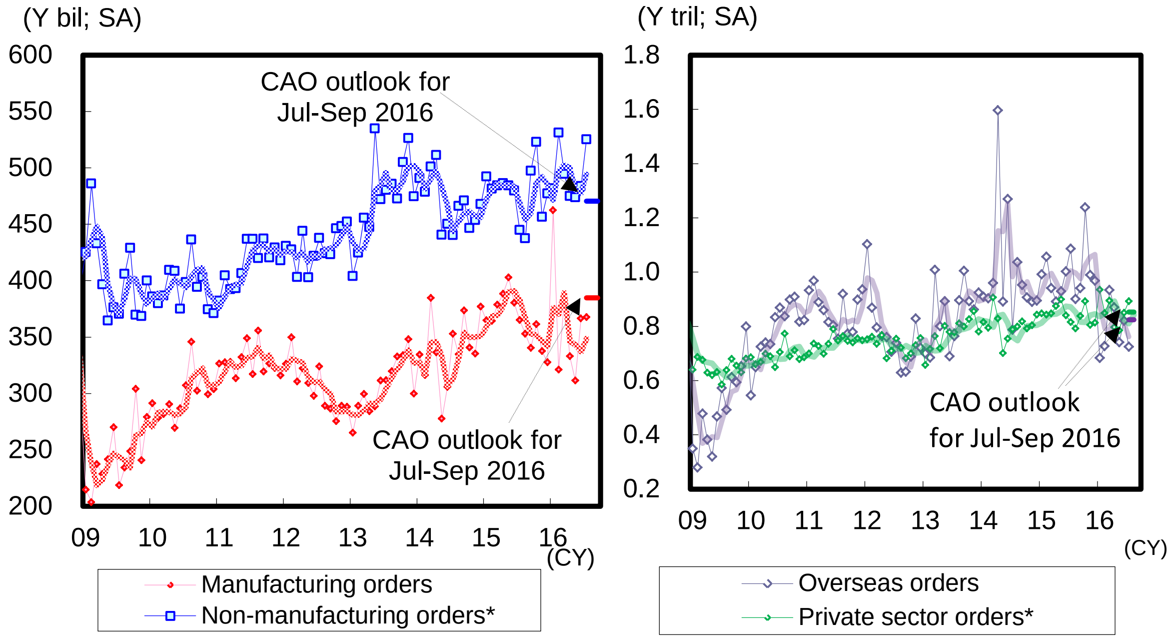
As for performance by industry, month-to-month growth was recorded by iron & steel (+75.8%), fabricated metal products (+109.3%), and chemicals (+23.8%). Iron & steel recorded growth for the second consecutive month, with rumors that a budget for large-scale supplemental orders would be announced in August and rising expectations for future public works related demand indicating the possibility of more growth to be expected. Fabricated metal products, also achieved its second consecutive month of growth, bringing signs of a comeback. On the other hand, a reactionary decline in response to the previous month's gains was seen in other transport equipment (-69.3% m/m), non-ferrous metals (-64.4%), and electrical machinery (-5.9%). As for non-ferrous metals, large-scale orders were received in May, and the industry is still feeling the reaction from that excessively productive month. Meanwhile, electrical machinery suffered a decline for the first time in four months. The industry hit bottom at the beginning of the year and has maintained a firm undertone ever since. The more recent declines are considered to be merely signs of taking a breather.

Non-manufacturing orders grow for second consecutive month. Maintaining high level, with ups and downs

Non-manufacturing orders (excluding ships and electric power) also grew for the second consecutive month by +8.6% m/m. Overall, non-manufacturing orders are at a relatively high level, with some ups and downs.

Looking at performance by industry, month-to-month growth was seen in telecommunications (+49.9%), finance and insurance (+17.7%), and wholesale and retail trade (+6.0%). Telecommunications registered its second consecutive month of growth and on average appears to have shifted into a growth phase. Meanwhile, results in finance and insurance indicate the possibility that investments to upgrade systems as a means of handling recent changes in the operating environment may be taking place. Other industries suffering declines in comparison to the previous month include transportation and postal activities (-18.0%), construction (-18.6%), and other non-manufacturing (-3.7%). Transportation and postal activities suffered a decline for the first time in three months, but order volume continues to grow. Transportation and postal activities may be gaining underlying support from investments in streamlining and labor-saving as the problem of the shortage in manpower continues to grow larger.

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



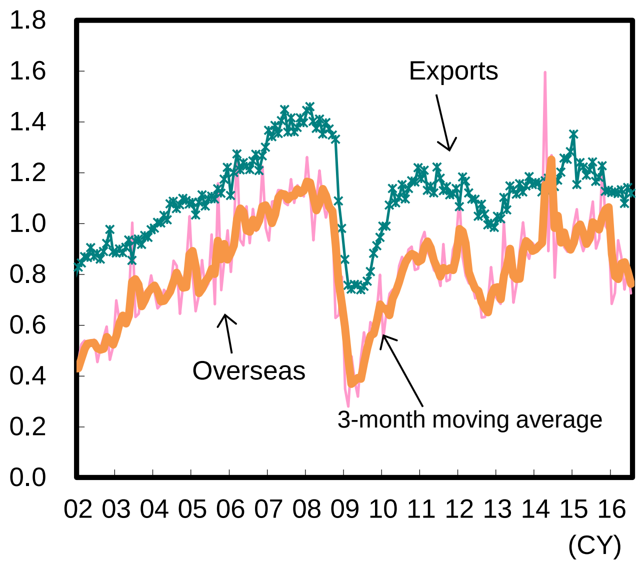
Source: Cabinet Office (CAO); compiled by DIR.
*excl. those for ships and from electric utilities.
Note: Thick lines 3M/MA basis.

Overseas orders decline for first time in two months due to sluggish business for engines and turbines, as well as industrial machinery

Overseas orders declined for the first time in two months by -11.7% m/m. According to the Cabinet Office, orders for heavy electric machinery and ships grew, while orders for engines and turbines, as well as industrial machinery declined.

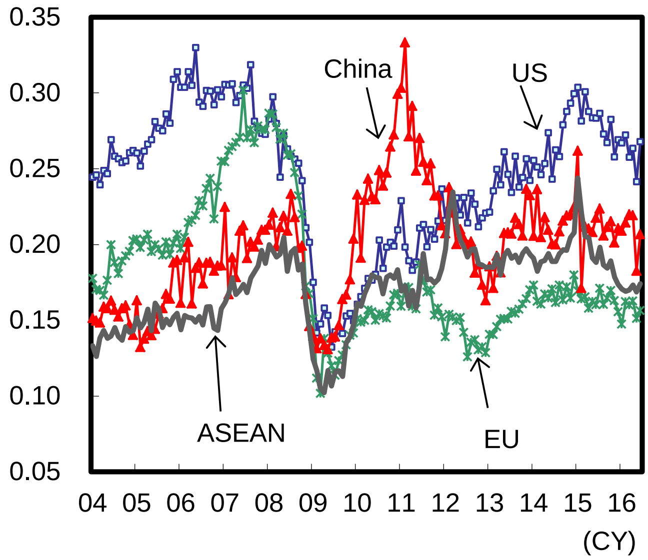
While the feeling is growing that the world economy is beginning to settle down now in comparison to the sluggish performance at the beginning of the year, new worrisome factors have emerged. The US economy is stagnating and a variety of uncertain factors have begun to surface in the world economy, such as the UK’s decision to leave the EU (Brexit). As for the future of overseas orders, we expect a gradual comeback, but we advise continuing to take a cautious approach to world economic developments.

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**

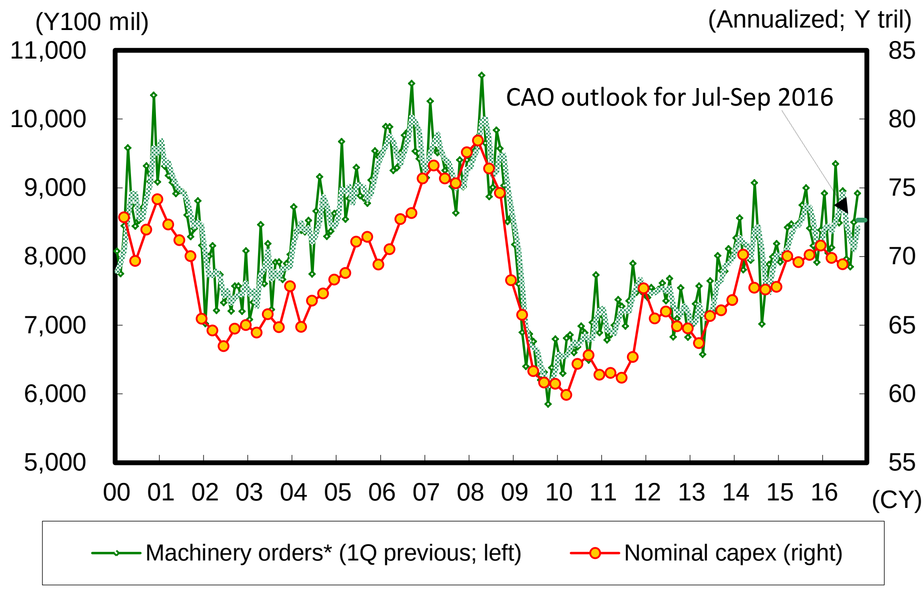


Source: Ministry of Finance; compiled by DIR.
Note: SA by DIR.

Moderate growth seen for machinery orders in future

Machinery orders, the leading indicator for capex, are expected to win moderate growth in the future. With supply and demand for labor remaining tight, investment in rationalization and labor-saving devices is likely, while at the same time, the non-manufacturing industries are expected to carry out investment in transport and distribution infrastructure. However, the slowdown of the world economy and the growing tendency toward a strong yen/weak dollar situation will likely effect domestic demand, and there is the growing sense that corporate earnings are about to peak out. In this context we must keep in mind the possibility that corporations may therefore become more cautious as regards capex spending.

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



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