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August 2016 Machinery Orders

August orders decline by 2.2%, but stand an excellent chance of achieving outlook for growth

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Summary

- According to statistics for machinery orders in August 2016, the leading indicator for domestic capex and private sector demand (excluding ships and electrical power), orders declined for the first time in three months by -2.2% m/m, while at the same time exceeding market consensus at -4.7%. Both manufacturing and non-manufacturing suffered declines, for the first time in three months, but on average, machinery orders are seen as continuing the steady undertone shown in recent months.

- Looking at orders by source of demand in August, the manufacturing industries declined for the first time in three months by -4.0% m/m. Non-manufacturing orders (excluding ships and electric power) also declined for the first time in three months by -1.9% m/m. Overseas orders grew for the first time in two months by +6.8% 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							
	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug
Machinery orders (private sector)*	5.9	6.4	-9.7	1.0	15.0	-9.2	5.5	-11.0	-1.4	8.3	4.9	-2.2
Market consensus (Bloomberg)												-4.7
DIR estimate												-3.0
Manufacturing orders	-3.5	6.2	-6.6	-3.0	41.2	-30.6	19.7	-13.3	-6.4	17.7	0.3	-4.0
Non-manufacturing orders*	13.7	5.2	-12.7	4.5	1.0	10.2	-6.9	-3.9	-0.3	2.1	8.6	-1.9
Overseas orders	4.4	31.6	-20.1	-2.2	-29.4	6.3	28.5	-6.9	-14.8	10.8	-11.7	6.8

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

August orders decline for first time in three months, but continue steady undertone

According to statistics for machinery orders in August 2016, the leading indicator for domestic capex and private sector demand (excluding ships and electrical power), orders declined for the first time in three months by -2.2% m/m, while at the same time exceeding market consensus at -4.7%. Both manufacturing and non-manufacturing suffered declines, for the first time in three months, but on average, machinery orders are seen as continuing the steady undertone shown in recent months.

Manufacturing orders decline for first time in three months. iron & steel and fabricated metal products contribute to negative results

Looking at orders by source of demand in August, the manufacturing industries declined for the first time in three months by -4.0% m/m.

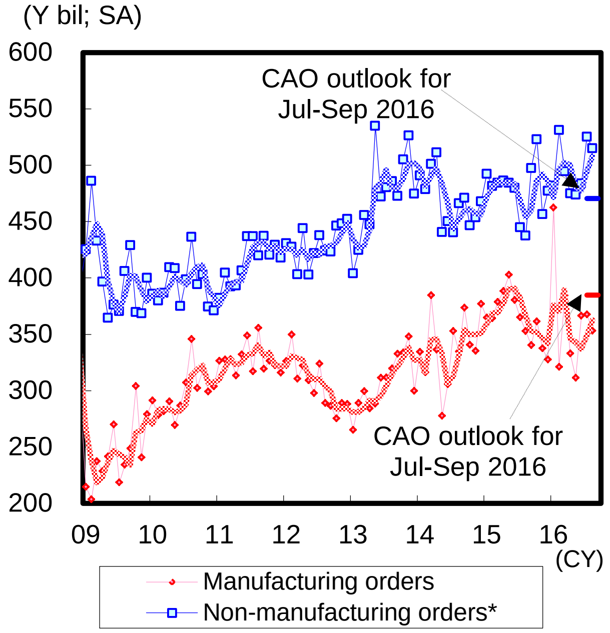
As for performance by industry, declines were recorded by iron & steel (-62.3%), fabricated metal products (-52.3%), and chemicals (-31.7%). Iron & steel suffered declines for the first time in three months. While there are growing expectations of an influx of public investment in the future, there is also a worldwide trend toward excess production capacity due to the economic slowdown in China, and this situation has not yet completely recovered. As for fabricated metal products, this industry also suffered declines for the first time in three months due to a reactionary decline following major growth recorded during the previous month. However, on average, the industry is beginning to show signs of a comeback. In contrast, month-to-month growth was seen in other manufacturing (+26.4%), electrical machinery (+6.6%), and other transport equipment (+14.9%). Electrical machinery achieved growth for the first time in two months. The industry continued to mark time for some months after recovering from a slump which occurred at the beginning of the year.

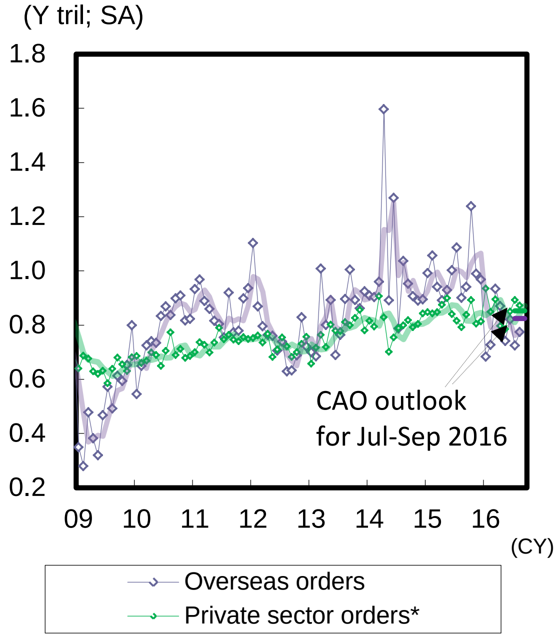
Non-manufacturing orders decline for first time in three months, but level of orders remains favorable

Non-manufacturing orders (excluding ships and electric power) also declined for the first time in three months by -1.9% m/m. Overall, non-manufacturing orders are at a relatively high level, and are expected to continue the favorable trend in the future.

Looking at performance by industry, month-to-month declines were seen in telecommunications (-22.7%), agriculture, forestry, and fishing (-26.2%), and finance & insurance (-12.7%). Telecommunications declined for the first time in three months, taking a breather from its recent growth trend. Industries exhibiting month-to-month growth were transportation and postal activities (+20.6%), other non-manufacturing (+21.2%), and information services (+12.8%). Transportation and postal activities achieved growth for the first time in two months, and on average, is continuing a growth trend in orders received. 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**





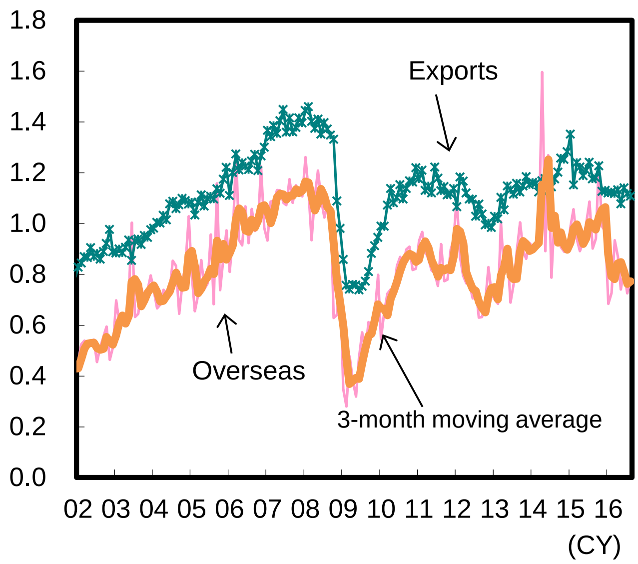
Source: Cabinet Office (CAO); compiled by DIR.
*excl. those for ships and from electric utilities.
Note: Thick lines 3M/MA basis.

Overseas orders achieve growth for first time in two months. Orders for aircraft and industrial machinery grow

Overseas orders grew for the first time in two months by +6.8% m/m. According to the Cabinet Office, orders for ships and heavy electric machinery declined, while orders for aircraft, as well as industrial machinery grew.

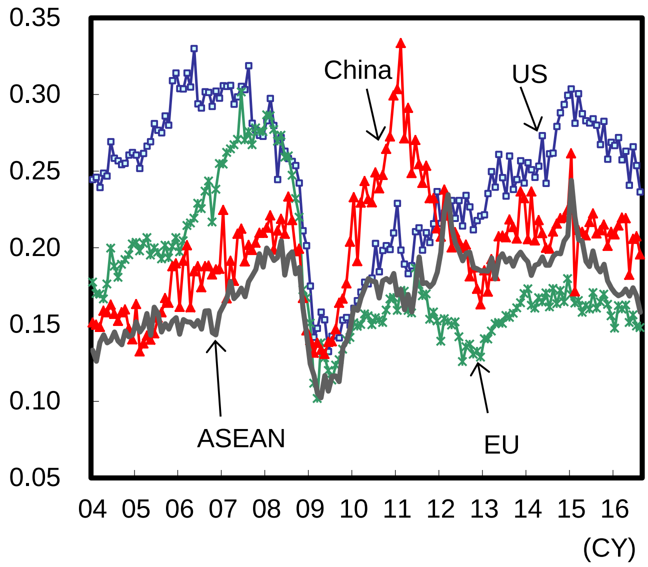
While the feeling is growing that the world economy is beginning to settle down now in comparison to the sluggish performance at the beginning of the year, new worrisome factors have emerged. The US economy is stagnating and a variety of uncertain factors have begun to surface in the world economy, such 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 Chart 3
(Y tril; SA)



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 Chart 4
(Y tril; SA)



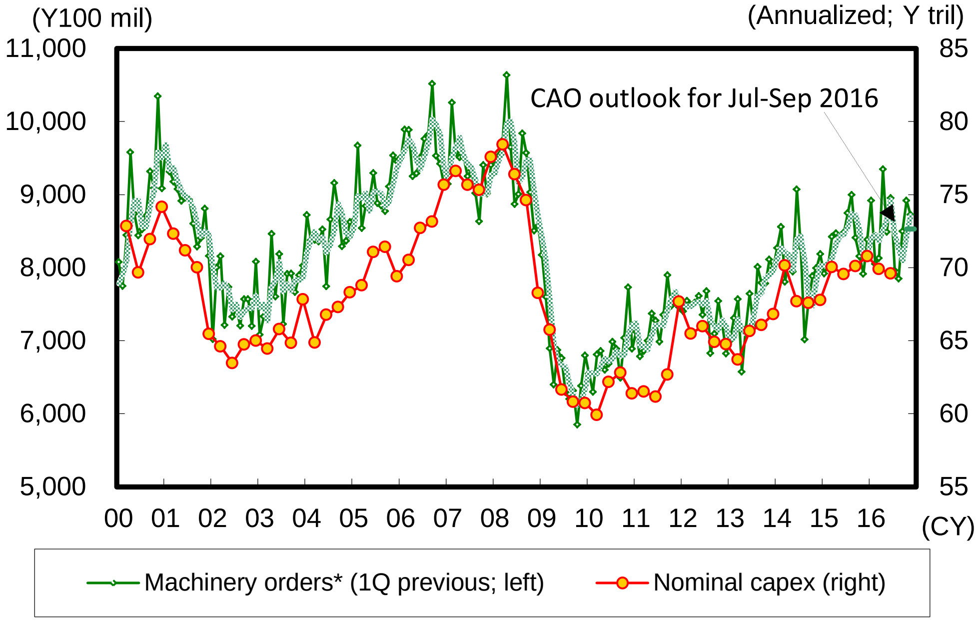
Source: Ministry of Finance; compiled by DIR.
Note: SA by DIR.

Moderate growth seen for machinery orders in future

The Cabinet Office outlook for the Jul-Sep period sees private sector demand (excluding ships and electrical power) up by +5.2% q/q, a shift back to growth in comparison to the previous quarter. Considering the results for the months of July and August, this outlook can be achieved if September orders obtain results of -8.9% m/m or better. We therefore believe that there is a high probability that the Cabinet Office outlook will be achieved.

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.