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February 2016 Machinery Orders

February orders exceed market expectations. Performance seen marking time in the future

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Summary

- According to statistics for machinery orders in February 2016, the leading indicator for domestic capex, private sector demand (excluding shipbuilding and electrical power), orders declined for the first time in three months at -9.2% m/m, while exceeding market consensus at -12.0%. January results saw major growth due to special factors, so the negative results in February were in line with market expectations. Hence the major m/m decline should not be viewed pessimistically. On average, domestic demand is evaluated as marking time.

- Looking at orders by source of demand in February, the manufacturing industries suffered declines for the first time in two months at -30.6% m/m. This is a reactionary decline after the major orders received by the iron & steel industry in January. Meanwhile, the non-manufacturing industries (excluding shipbuilding and electrical power) grew for the third consecutive month by +10.2% m/m. Non-manufacturing is now considered to be in a moderate growth trend despite some ups and downs.

- Machinery orders, the leading indicator for capex, are expected to continue marking time in the future. With the introduction of a negative interest rate by the BOJ, corporations are benefitting from a decline in the cost to procure capital, and this is expected to provide underlying support for capex spending. Meanwhile, supply and demand for labor remains tight, hence we should be able to expect the non-manufacturing industries, which are not so easily influenced by overseas demand, to invest in labor-saving and manpower-saving devices. On the other hand, a worsening external environment as seen in the economic slowdown in the emerging economies 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, corporations could become more cautious regarding capex.

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

	2015 Mar	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	2016 Jan	Feb
Machinery orders (private sector)*	0.6	3.2	2.9	-6.6	-3.0	-2.9	5.9	6.4	-9.7	1.0	15.0	-9.2
Market consensus (Bloomberg)												-12.0
DIR estimate												-8.5
Manufacturing orders	4.0	2.5	3.7	-5.6	-4.0	-3.4	-3.5	6.2	-6.6	-3.0	41.2	-30.6
Non-manufacturing orders*	0.6	0.4	-0.4	-0.9	-7.3	-1.7	13.7	5.2	-12.7	4.5	1.0	10.2
Overseas orders	-10.9	-5.3	4.1	7.9	8.5	-17.1	4.4	31.6	-20.1	-2.2	-29.4	6.3

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

February orders experience reactionary decline after major growth in January due to special factors, but no need for pessimism

According to statistics for machinery orders in February 2016, the leading indicator for domestic capex, private sector demand (excluding shipbuilding and electrical power), orders declined for the first time in three months at -9.2% m/m, while exceeding market consensus at -12.0%. January results saw major growth due to special factors, so the negative results in February were in line with market expectations. Hence the major m/m decline should not be viewed pessimistically. On average, domestic demand is evaluated as marking time. With the exception of iron & steel, domestic demand was up by +5.1% m/m.

Manufacturing experiences reactionary decline after January's large-scale orders in iron & steel – first decline in two months

Looking at orders by source of demand in February, the manufacturing industries suffered declines for the first time in two months at -30.6% m/m. This is a reactionary decline after the large-scale orders received by the iron & steel industry in January. Manufacturers other than iron & steel recorded a -4.6 m/m decline.

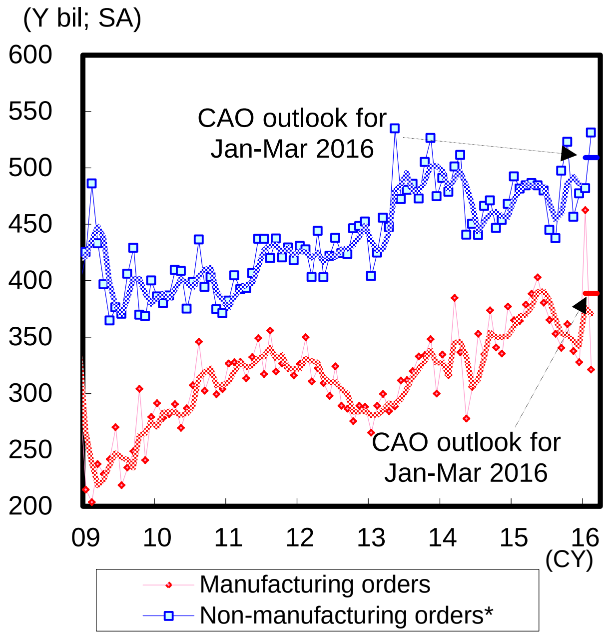
As for performance by industry, iron & steel was down by -92.7% m/m, while electrical machinery fell by -10.5% and information & communication electronics equipment declined by -24.6%. As for iron & steel, a reactionary decline was experienced in response to the major orders received in January. Electrical machinery declined for the second consecutive month, with orders continuing at a sluggish pace since the middle of last year. On the other hand, some industries chalked up month-to-month growth, including other manufacturing (+9.5%), pulp, paper & paper products (+109.8%), chemicals (+8.6%), and petroleum & coal products (+46.5%). As for other manufacturing, growth was achieved for the second consecutive month, while chemicals grew for the first time in three months. On average, performance continues to mark time. Petroleum & coal products grew considerably in comparison to the previous month, but orders are still at a low level, pointing to overall stagnation.

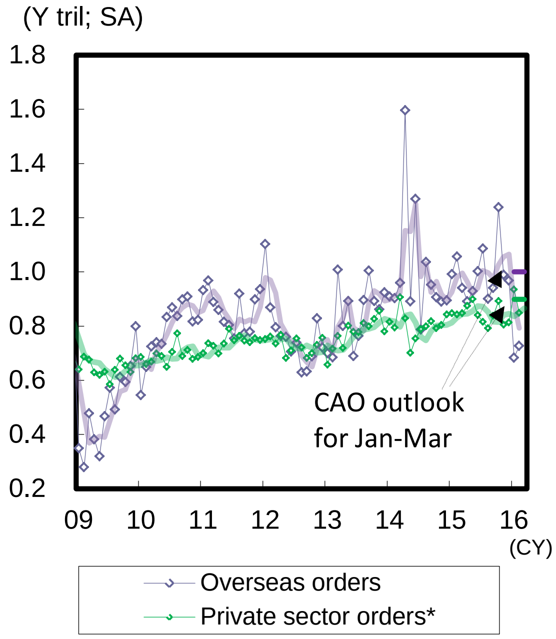
Non-manufacturing industries grow for third consecutive month, move into moderate growth trend

Non-manufacturing orders (excluding shipbuilding and electric power) grew for the third consecutive month at +10.2% m/m. The non-manufacturing industries are in a moderate growth trend despite some ups and downs.

Looking at performance by industry, positive contributions were made by transportation & postal activities (+34.8%), information services (+28.3%), and other non-manufacturing (+11.3%). Transportation & postal activities grew for the first time in two months and is continuing in a growth trend despite some ups and downs. As for information services, growth was achieved for the first time in two months, indicating that orders are clearly growing in recent weeks in comparison to the lows experienced in autumn of last year. On the other hand, declines were suffered by the wholesale and retail trade (-26.6%), real estate (-34.1%), and goods leasing (-8.8%). Wholesale and retail trade suffered a major decline for the first time in four months, but this was not enough to cause a reversal from the growth trend experienced until now. Meanwhile, the goods leasing industry suffered a decline for the second consecutive month, revealing a weak tone.

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



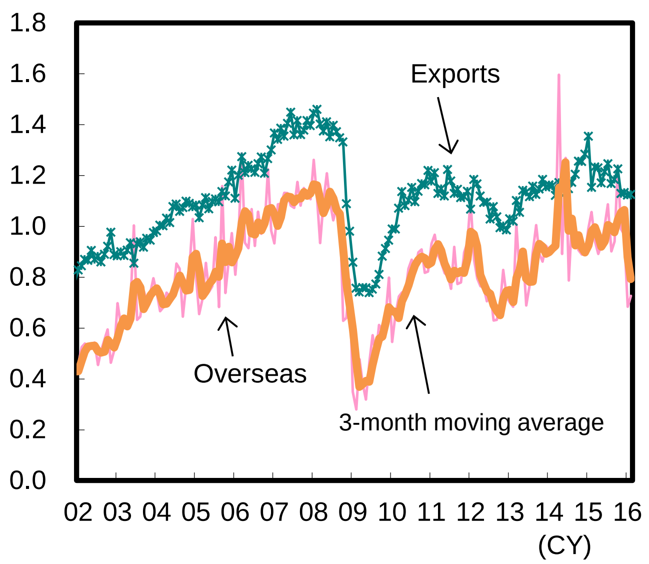


Source: Cabinet Office (CAO); compiled by DIR.
*excl. those for shipbuilding and from electric utilities.
Note: Thick lines 3M/MA basis.

Overseas orders win growth for first time in four months, but rebound is weak

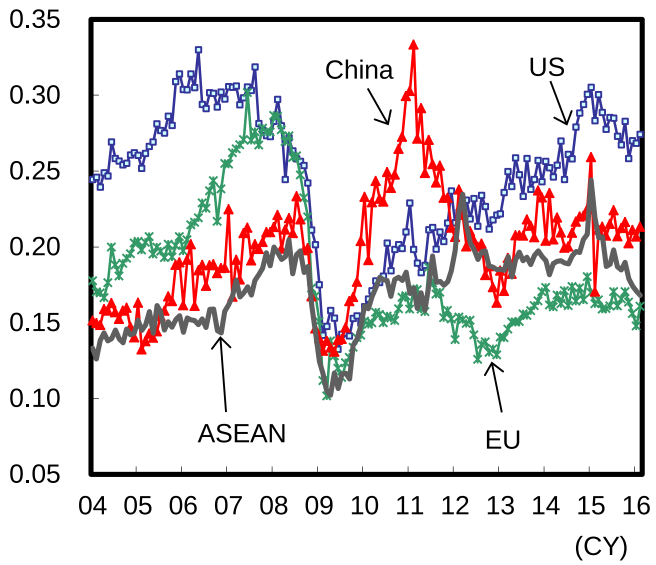
Overseas demand achieved growth for the first time in four months at +6.3% m/m, but considering the major declines suffered over the past three months, the rebound is weak. With the continued uncertainty as regards the future of the world economy, overseas demand should be viewed cautiously for the short-term.

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)

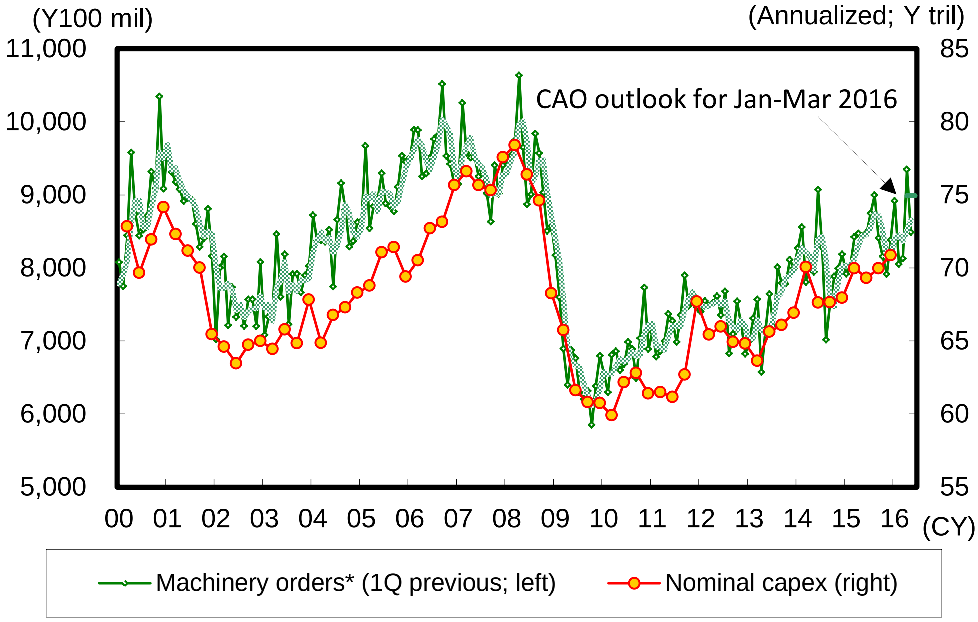


Source: Ministry of Finance; compiled by DIR.
Note: SA by DIR.

Machinery orders expected to continue marking time

Machinery orders, the leading indicator for capex, are expected to continue marking time in the future. With the introduction of a negative interest rate by the BOJ, corporations are benefitting from a decline in the cost to procure capital, and this is expected to provide underlying support for capex spending. Meanwhile, supply and demand for labor remains tight, hence we should be able to expect the non-manufacturing industries, which are not so easily influenced by overseas demand, to invest in labor-saving and manpower-saving devices. On the other hand, a worsening external environment as seen in the economic slowdown in the emerging economies 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, corporations could become more cautious regarding capex.

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.