17 May 2017 (No. of pages: 5)

Japanese report: 17 May 2017

March Machinery Orders

March orders win +1.4% m/m growth. Apr-Jun period seen suffering decline in comparison to previous quarter

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Summary

- According to statistics for machinery orders in March, the leading indicator for domestic capex and private sector demand (excluding ships and electrical power), orders grew for the second consecutive month by +1.4% m/m, while at the same time falling below market consensus at +2.5%. Non-manufacturing (excluding ships and electric power) suffered a decline for the first time in four months at -3.9% m/m, while manufacturing grew for the second consecutive month by +0.6%, providing a lift for overall results.

- As a result of March activity, FY2016 private sector demand (excluding ships and electrical power) grew by +0.5% y/y, with manufacturing down by -4.6% and non-manufacturing (excluding ships and electric power) up by +4.3%. Non-manufacturing industry orders managed to bring overall results up, while manufacturing orders did poorly.

- The Cabinet Office forecast for the Apr-Jun 2017 period sees private sector demand (excluding ships and electrical power) down for the second consecutive quarter by -5.9% q/q. Looking at orders by source of demand we see declines for both manufacturing (-1.1%) and non-manufacturing (excluding ships and electric power) at -9.6%.

- Machinery orders, the leading indicator for capex, are expected to experience ups and downs in the future. Operating rates in the manufacturing industry have been in a growth trend since the second half of last year due to the increase in exports encouraged by recovery in the world economy. If the increase in operating rate continues, corporations may become more aggressive in carrying out capex spending. Meanwhile, the non-manufacturing industries are expected to carry out investments in transport and distribution infrastructure with the continuing growth in foreign visitors to Japan, as well as expectations regarding the 2020 Tokyo Olympics and Paralympics. However, there is always a possibility that a reactionary decline could occur in the future with orders having continued on such a high level until now.

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

	2016									2017		
	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar
Machinery orders (private sector)*	-6.4	-2.2	7.1	5.6	-5.9	0.3	3.4	-2.8	2.1	-3.2	1.5	1.4
Market consensus (Bloomberg)												2.5
DIR estimate												2.0
Manufacturing orders	-9.7	0.0	6.5	0.9	-3.1	-3.3	0.4	8.1	0.8	-10.8	6.0	0.6
Non-manufacturing orders*	-3.3	1.0	1.8	6.5	-3.1	0.7	2.7	-5.6	2.1	0.7	1.8	-3.9
Overseas orders	4.7	-16.3	9.7	-9.0	-0.7	2.8	7.1	16.3	-12.1	3.2	-1.1	-2.8

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

March orders: manufacturing up slightly, non-manufacturing down

According to statistics for machinery orders in March, the leading indicator for domestic capex and private sector demand (excluding ships and electrical power), orders grew for the second consecutive month by +1.4% m/m, while at the same time falling below market consensus at +2.5%. Non-manufacturing (excluding ships and electric power) suffered a decline for the first time in four months at -3.9% m/m, while manufacturing grew for the second consecutive month by +0.6%, providing a lift for overall results.

The Cabinet Office forecast for the Apr-Jun 2017 period sees private sector demand (excluding ships and electrical power) down for the second consecutive quarter by -5.9% q/q. Looking at orders by source of demand we see declines for both manufacturing (-1.1%) and non-manufacturing (excluding ships and electric power) at -9.6%. As for non-manufacturing, FY2016 results managed to come in on the plus side in y/y terms, but the Oct-Dec period in FY2016 hit -1.0% and the Jan-Mar 2017 period hovered at 0.0%. If Apr-Jun period results turn out as expected in the outlook we may see a slowing trend.

Manufacturing orders grow for the second consecutive month

Looking at orders by source of demand in March, the manufacturing industries grew for the second consecutive month at +0.6% m/m. Our evaluation is that on average, manufacturing orders are marking time.

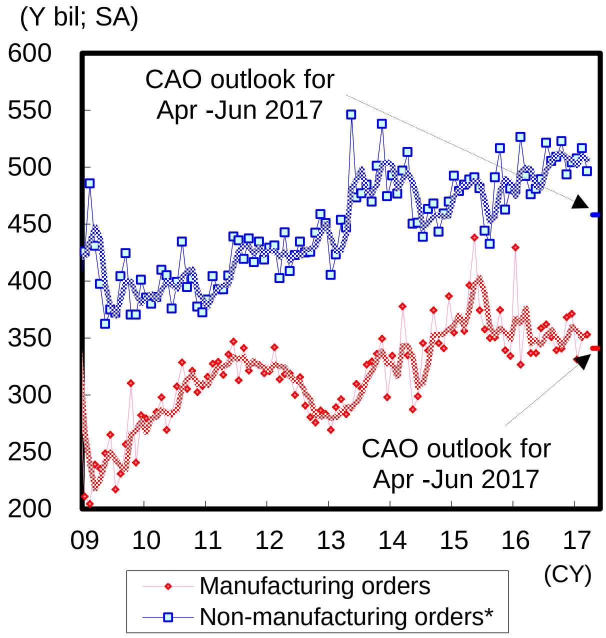
As for performance by industry, growth was seen in non-ferrous metals (+862.5% m/m), general-purpose and production machinery (+10.0%), and automobiles, parts and accessories (+21.1%). As for non-ferrous metals, performance was most likely due to large-scale orders. Meanwhile, general-purpose and production machinery appears to be maintaining the moderate growth trend which it has maintained since the beginning of 2016. As for automobiles, parts and accessories, positive performance is thought to represent a rebound from the previous month's decline. On the other hand, some industries suffered declines in comparison with the previous month, including electrical machinery (-27.1%), pulp, paper & paper products (-77.4%), and other transport equipment (-30.3%). Electrical machinery declined for the second consecutive month, showing a continued lack of energy.

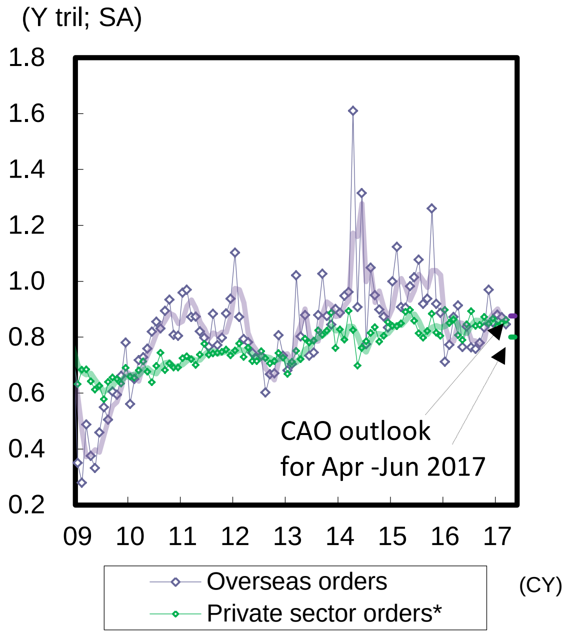
Non-manufacturing orders decline for the first time in four months

Non-manufacturing orders (excluding ships and electric power) suffered a decline for the first time in four months at -3.9% m/m. Non-manufacturing orders continue to mark up a high level of orders, but on the whole, performance has suffered ups and downs.

Looking at performance by industry, month-to-month declines were seen in other non-manufacturing (-30.6%), transportation and postal activities (-23.5%), and finance & insurance (-15.0%). Other non-manufacturing likely experienced a reactionary decline after the previous month's major growth (+69.0%). On average it continues its growth trend. As for transportation and postal activities, a declining trend has continued since fall of last year. On the other hand, some industries experienced growth. These were construction (+66.3%), telecommunications (+36.0%), and real estate (+33.1%). The construction industry brought in strong results due to favorable business for real estate, and infrastructure demand.

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.

FY2016: Outlooks for manufacturing and non-manufacturing contrast sharply

As a result of March activity, FY2016 private sector demand (excluding ships and electrical power) grew by +0.5% y/y, with manufacturing down by -4.6% and non-manufacturing (excluding ships and electric power) up by +4.3%. Favorable orders in the non-manufacturing industry managed to bring overall results up, while manufacturing orders did poorly.

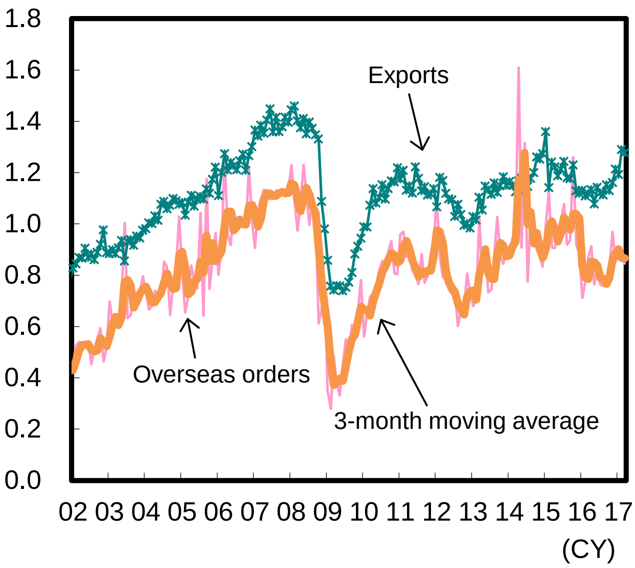
Manufacturing: non-ferrous metals win growth, but what stands out is that most industries suffered declines

Looking at results for manufacturing in FY2016, we see declines in iron and steel (-53.6% y/y), electrical machinery (-7.6%), and information and communication electronics equipment (-23.8%). Iron and steel suffered a major decline in reaction to the major growth recorded during FY2015. Meanwhile, electrical machinery showed signs of a comeback during the first half of FY2016, but then suffered declines for two consecutive months in February and March, ultimately finishing the year in a decline in comparison with the previous year. On the other hand, growth was seen in non-ferrous metals (+102.3%), other manufacturing (+6.6%), and general-purpose and production machinery (+0.8%). Non-ferrous metals brought in major growth thought to be due to large-scale projects multiple times during FY2016.

Non-manufacturing: transportation and postal activities brings overall numbers up

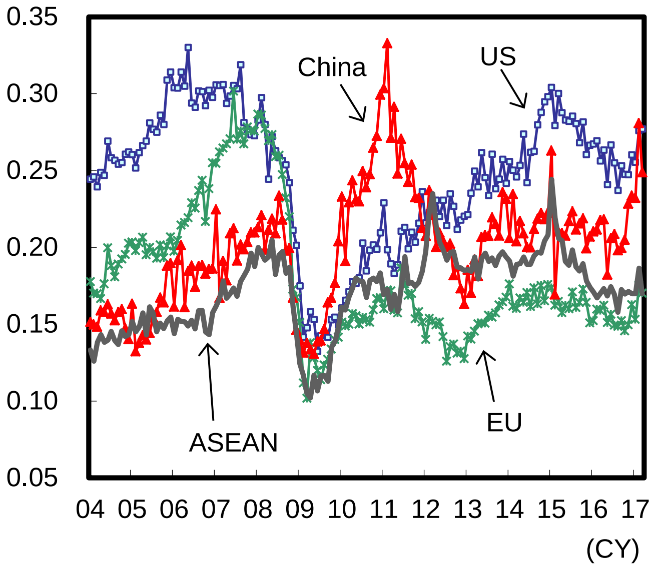
Looking at results for non-manufacturing in FY2016, growth was seen in transportation and postal activities (+19.3% y/y), other non-manufacturing (+2.6%), and construction (+6.8%). As for transportation and postal activities, the first half recorded +51.6% y/y, falling back to -5.4% in the second half. Ultimately, orders for railroad cars during the first half helped push up overall results. Meanwhile, favorable business for real estate, and infrastructure demand helped the construction industry to maintain favorable orders. On the other hand, declines were experienced in finance & insurance (-13.2%), real estate (-7.2%), and information services (-1.4%). As for finance & insurance, the industry suffered a reactionary decline in response to large-scale IT investments carried out in 2015, but recently orders are recovering. It is possible that the negative influences have finally run their course.

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**

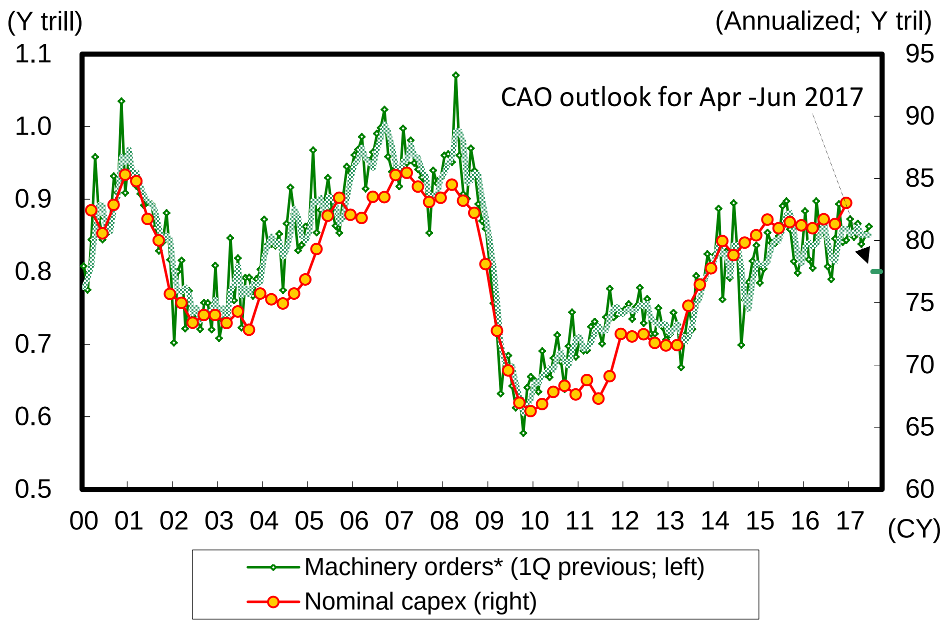


Source: Ministry of Finance; compiled by DIR.
Note: SA by DIR.

Overseas orders decline for second consecutive month

Overseas orders declined for the second consecutive month at -2.8% m/m. According to the Cabinet Office, orders for electrical motors and aircraft grew, while orders for industrial machinery and electronics & telecommunications equipment declined. As a result, overseas demand suffered a decline of -10.2% y/y on the FY2016 result.

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.

Machinery orders to experience ups and downs in future

Machinery orders, the leading indicator for capex, are expected to experience ups and downs in the future. Operating rates in the manufacturing industry have been in a growth trend since the second half of last year due to the increase in exports encouraged by recovery in the world economy. However, it is difficult to see this reaching a high enough level to encourage more aggressive investment in increasing capacity. We will continue to monitor operating rates closely as a means of predicting the industry’s future. Meanwhile, the non-manufacturing industries are expected to carry out investments in transport and distribution infrastructure with the continuing growth in foreign visitors to Japan, as well as expectations regarding the 2020 Tokyo Olympics and Paralympics. However, there is always a possibility that a reactionary decline could occur in the future with orders having continued on such a high level until now.

The future of overseas demand according to our main scenario sees a continuation of gradual expansion backed by the recovery of the world economy. On the other hand, geopolitical risk is on the rise with the tense situation with North Korea, and there are growing doubts regarding the Trump administration’s policies and the possibility of world economic slowdown if protectionist trade policies go into effect. We urge caution as it is possible that yen appreciation could accelerate due to these factors, bringing downward pressure on export value.