

# Strong Yen Leads to Sluggish Growth

Based upon shipped automotive units, the 1993 forecast for domestic demand will be 8% less than the previous year, posting the third consecutive year of decline. New models exhibited at the October/November 1993 Tokyo Motor Show had been expected to benefit from investments in modifications. But, paralleling the general slump in sales, the benefits one would expect to derive from new models did not last long for some vehicles, and there was no recovery in demand.

The prediction that vehicles which were sold during the expanded demand phase of the late 1980s (which are now due for compulsory regular inspections) would form the nucleus of replacement units has turned hollow. Lagging private consumption due to cuts in disposable income brought on by the rapid business slowdown (along with dropping corporate demand due to stagnating corporate profitability from the impact of the strong yen) has resulted in a sharp drop in domestic demand.

Exports of fully assembled vehicles turned in negative growth again in fiscal 1992, and in fiscal 1993 there is a strong likelihood that the situation will deteriorate even more, for a total of less than 5 million units. The abrupt strengthening of the yen, increased local production by Japanese car manufacturers, and a serious slump in the European market were the main factors for this situation.

Surveying exports by destination, although new car sales have rebounded in the U.S. market, the recovery is occurring in the small truck market where the share held by Japanese makers is comparatively small. Japanese manufacturers have been increasing their local North American production, and Japanese vehicles are already priced higher than their American counterparts. The strengthening of the yen has served to increase the impression that Japanese vehicles are more expensive, inevitably leading to a decline in sales.

Sales on the European continent have

largely slumped and the initial 1.1 million unit "voluntary" restriction on exports to the EC was cut to 980,000 last September. Honda, Nissan, and Toyota have all increased local production, primarily at their U.K. plants and this also contributed to a broad drop in exports.

In other regions as well, because exports to Asia are primarily yen-based, this quickly tied in to declines by volume due to the impact of the strong yen and the growth rate was sluggish in the latter half. Furthermore, although exports to China exhibited high growth in fiscal 1992 and continued favorably in the first half of fiscal 1993, they fell off sharply from summer onward due to the effects of financial belt tightening and foreign currency restrictions.

Reacting to the effects of sluggish internal and external demand, fully assembled vehicle production in fiscal 1993 fell off by about 10% compared to the previous year and there is a growing possibility that it will tumble to around

11 million units. Operating ratios at domestic factories have declined and although attempts have been made to compensate by slowing assembly lines there is an increasing sense that surplus employment cannot be handled simply by cutting seasonal workers, leading to temporary lay-offs.

With declining domestic production of fully assembled vehicles and falling export receipts due to the strong yen, all but two or three manufacturers of fully assembled vehicles have been unable to avoid operating losses in terms of actual income. Under these conditions they have increasingly demanded that parts makers cut their costs and, other than a few parts manufacturers who possess bargaining strength due to their development capabilities, cost competitiveness or the lack thereof has greatly affected



There are slight hopes for increased domestic demand in the automotive industry for 1994. (30th Tokyo Motor Show held last autumn)



business results.

Looking at passenger vehicle demand in fiscal 1994, the timing of changes in consumer intentions is the greatest uncertainty factor. In the past, rough substitute demand predictions could be made based upon the number of vehicles subject to compulsory regular inspections, but the current recession has taken on an aspect in which demand is not manifested without the impression that the economy is recovering.

With cuts in disposable income due to reduced overtime, cuts in income tax led to high expectations. But with lagging consumer confidence, the portion saved from tax cuts was in many cases diverted to savings or purchases other than automobiles, and there is a strong possibility that these savings will not immediately be used to purchase cars. As such it is difficult to assume that auto purchases will propel the economy out of this recession, as they have done in the past. There is the strong possibility that a recovery in demand for automobiles will lag until the latter half of 1994, when other economic indicators show signs of a recovery, and it appears that passenger vehicle demand in fiscal 1994 will be about the same as in fiscal 1993. The initial pace of the recovery will probably be leisurely, but since replacement demand pressure is increasing a high demand growth rate can probably be expected once the economy enters an actual recovery phase.

In addition, considering that commercial vehicles form a portion of purchasing corporations' investment in plant and equipment and that companies are trying to cut expenditures as they are



faced with worsening business results, growth in vehicle replacement trends should remain unchanged for the present period and it is doubtful that there will be great growth in demand in the first half of fiscal 1994. As such, commercial vehicle demand will probably parallel sales of passenger vehicles.

There is a strong probability that even if exchange rates shift to a slight weakening of the yen, exports of fully assembled vehicles in 1994 will decline due to increased overseas production.

In the U.S., fully assembled Japanese vehicles are also meeting with difficulties, with the expansion of local production being the primary reason. In addition to production capacity that will be boosted to 200,000 units at the Toyota No. 2 plant in Kentucky in spring 1994, there are also moves to switch all Japanese exports that are currently sold in the U.S. to local production as model changes are implemented. It is also predicted that any increase in sales will also be supplied through local production.

Concurrently, the Big Three are restricting price increases and concen-

trating their energies on models that compete directly with Japanese cars. In addition, with restored consumer confidence in the improvement in quality of American cars, it is thought that Japanese vehicles will continue to face a difficult competitive situation in the U.S. and will be unable to avoid export cuts.

Amid pessimism that the European market will recover rapidly in 1994 and considering the production increases at the Toyota and Honda U.K. plants, there is a strong possibility that exports to Europe will decline further.

Exports to Asia will depend upon exchange rates, but the likelihood is strong that a renewed upswing in exports to China will come in the latter half of fiscal 1994 and conditions are such that it is difficult to foresee strong growth.

Considering declining exports, predictions are that the situation for fully assembled vehicle production will continue to be difficult in fiscal 1994 and, with the exception of what happens to the consumption tax and other special factors, there are sufficient factors pointing to a drop in production below 11 million units and companies will continue to be confronted with employment and other issue pressures.

Bearing in mind that the situation is such that there is not much hope for an increase in either domestic or external demand for cars and that export profits cannot be increased due to the strong yen, quick and effective implementation of restructuring measures to cut costs, efforts to normalize domestic sales, and attempts to achieve appropriate production levels will be urgent issues for all manufacturers.

Further, there is a growing impression that Japanese vehicles are expensive, particularly in the U.S. market, necessitating a rethinking of product strategies toward cost performance for the long term.

(Okada Mitsuhiro, economist)

### Automobile Supply and Demand

(10,000 units)

	FY1992	FY1993 (estimated)	FY1994 (anticipated)
Domestic Demand	688	633	633
Exports	566	477	466
Domestic Production	1,234	1,099	1,078

Note: Domestic demand includes imported vehicles