

INDUSTRIAL SURVEY

Automotive

Where Have All the Profits Gone?

Finished car, truck and bus production will suffer the first setback in four years in fiscal 1986. This is due to the slowdown in exports as contrasted with relatively firm domestic demand. Japanese automotive industry ordinary profit (profit before extraordinary items) will plunge close to 50% from the fiscal 1985 level, reflecting the continued strength of the yen.

Domestic demand is likely to increase 2.5% from the fiscal 1985 level, thanks to stepped-up sales efforts by automakers. Toyota Motor Corp. has taken the occasion of the 50th anniversary of car production in Japan to intensify its sales offensive and expand its market share. Other automakers bolstered their sales efforts to keep from falling behind. Together, these factors have served to boost domestic demand. However, much of the increase was due to the earlier-than-usual replacement purchase by car owners. This will have an unfavorable effect on demand in fiscal 1987 and beyond.

Exports of finished cars, trucks and buses will decline for the first time in the four years since fiscal 1982. This is due partly to a likely plunge in exports to China, expected to come to only about a quarter of the fiscal 1985 level as a result of that country's deteriorating foreign exchange position. A steep drop in shipments to the Middle East, Australia and Southeast Asia will also make itself felt. A relative decline in the cost competitiveness of Japanese motor vehicles brought on by the sustained appreciation of the yen is partly to be blamed for the reduced shipments. However, the main cause is sluggish vehicle demand, brought on by economic slowdowns in each of these markets.

The nearly 50% decrease from the previous year in the combined ordinary profits of Japan's 11 finished vehicle man-



Japan's automobile exports have slowed down, resulting in cutbacks in production.

ufacturers is due mainly to the yen's precipitous appreciation against the U.S. dollar. Japanese automakers' exports to the United States are worth some \$20 billion a year. If the Japanese currency rises just ¥1 against the U.S. dollar, their foreign exchange losses will reach ¥20 billion. In fact, automakers' foreign exchange losses for all of fiscal 1986 will come to an estimated ¥1.5 trillion (about \$9.1 billion). Since they have already raised prices several times, actual foreign exchange losses will be somewhat below the estimate. However, prices in the U.S. are up only about 15%, just a third of the yen's gains against the dollar. Japanese automakers have pressured parts makers to lower their prices and have also worked to cut their costs in order to minimize profit declines. Nonetheless, they are certain to suffer heavy setbacks.

In fiscal 1987, finished car, truck and bus production is likely to increase over fiscal 1986. However, their profit outlook will remain bleak.

Domestic demand is forecast to grow only a small 0.4%—a far slower growth rate than in fiscal 1986. This reflects two factors: a decline in sales following on the somewhat excessive sales of fiscal 1986 resulting from aggressive promotion drives, and the introduction of a new mandatory car safety inspection system

in July 1983. Under the new system, new car owners are required to have their cars inspected three years after purchase instead of after two years as previously required. Second and subsequent inspections must also be conducted at two-year intervals. Therefore, car owners who bought their cars in 1983 will not need to have their cars inspected in 1987. As Japanese car owners have shown a strong tendency to buy new cars at inspection time, the new system is expected to have an unfavorable impact on domestic demand.

Exports in fiscal 1987 are likely to increase about 1% over the previous year. That is due partly to the likelihood of a comparatively good showing in commercial vehicle exports to the U.S. under the lead of four-wheel drive and multipurpose types. A likely recovery of exports to the Middle East and Australia following the declines of fiscal 1986 will also contribute. Exports of KD (knockdown) assembly sets will probably increase more than 20% in both fiscal 1986 and fiscal 1987. Japanese automakers are stepping up assembly overseas, particularly in the United States.

Reflecting the slight increase in car, truck and bus production, sales for the 11 automakers will likely increase slightly. However, ordinary profits will probably total about ¥450 billion (about \$2.7 billion), virtually unchanged from fiscal 1986, as they will find it nearly impossible to wrangle further price reductions from parts makers. In fiscal 1986, cuts in parts makers' prices will serve to prevent further drops in automakers' profits. In fiscal 1987, however, parts makers will not be able to afford to offer additional reductions. ●

Car, Truck and Bus Supply and Demand

	FY 1985	FY 1986 (estimate)	FY 1987 (forecast)
Domestic demand (1,000 units)	5,573 (1.6)	5,710 (2.5)	5,730 (0.4)
Exports (1,000 units)	6,848 (11.6)	6,710 (-2.0)	6,770 (0.9)
Production (1,000 units)	12,417 (7.1)	12,350 (-0.5)	12,420 (0.6)
Sales (¥ billion)	19,363.7	19,000.0	20,000.0
Ordinary profits (¥ billion)	834.1	450.0	450.0

Notes: 1. Sales and profits for top 11 finished car, truck and bus makers only
2. Figures in parentheses represent the rate of increase over previous year.

(Shigeki Yana, senior economist)