

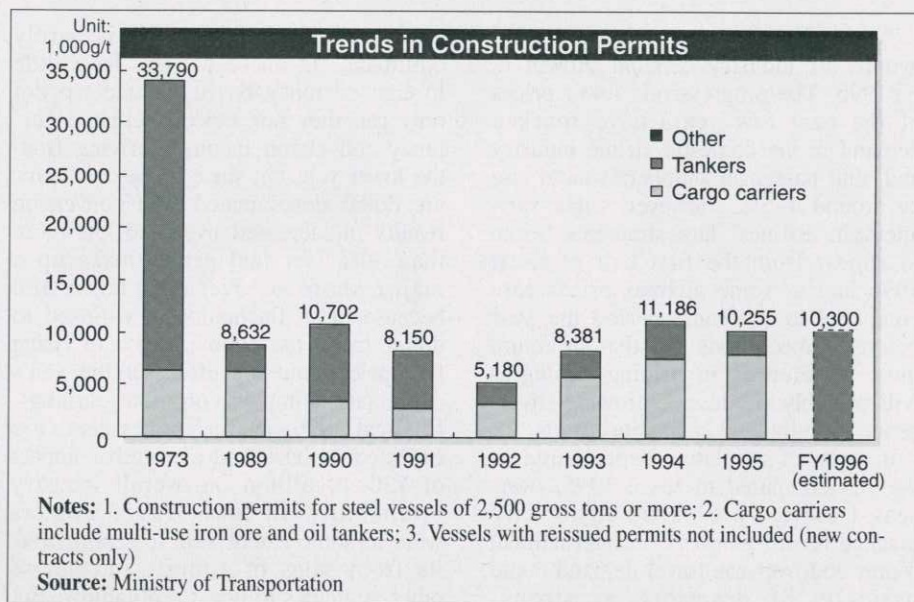
New Construction Orders Keep Shipbuilders Working at Full Capacity

Recent trends

Japanese shipbuilders received 5.77 million gross tons in new orders in the first half of fiscal 1996, an increase of 24.5% over the same period the year before, and were in a strong position to have broken the 10 million gross ton mark for the entire fiscal year. As a result, major Japanese shipyards appear set to achieve their 1998 forecasts and have acquired approximately two years' worth of back orders. With the abundance of back orders, the shipyards are all operating at full capacity and completed construction orders of around 9.5 million tons are forecast for all of fiscal 1996.

In the first half of FY1996, 76% of orders received by Japanese shipyards were for cargo carriers and with the hoped-for upturn in replacement demand for very large crude carriers (VLCC) failing to materialize, demand was driven by bulk carriers and container vessels. With increasing worldwide moves to eliminate substandard vessels, cargo vessels were scrapped in large quantities and the desire for economies of scale produced new orders for larger vessels. The recovery in Japanese cost competitiveness also contributed to strong order volumes. As the yen has continued to depreciate, substantial cost reductions have been achieved over the past two or three years, reducing the amount of the cost differential between Japan and South Korea to a few percentage points for the time being and, considering Japan's technological capabilities and the quality of services offered, what might be called the "Japan premium" (5-10%), has placed Japan in an actual overall position of superiority.

In terms of prices, however, dollar-based ship orders have remained nearly flat while yen-denominated orders exhibited a substantial rise reflecting the continued weakening of the yen. However, fiscal 1996 sales figures will reflect orders booked during the period from the latter half of fiscal 1994 to the first half of 1995 when the yen was strong, and although the volume of com-



pleted construction orders has remained at high levels, strains on the shipbuilding sector's profitability were expected to have continued in fiscal 1996.

Future outlook

While replacement orders for VLCC will rebound in fiscal 1997, orders for bulk carriers and container ships will experience a downturn and it is expected that new orders totaling 9.5 million gross tons will lag behind the previous year by around 10%. However, the abundance of back orders will allow shipyards to continue operating at full capacity and completed construction orders of 9.7 to 9.9 million gross tons are forecast for fiscal 1997.

As a result of the large volume of orders since 1994, worldwide completion of bulk carriers and container vessels continued to exceed scrap levels, leading to an increasingly strong sense of overcapacity. Under these conditions, orders for bulk carriers and container ships, which have remained at high levels for three years, are expected to steadily begin to decline. In the tanker sector, however, long-delayed replacement of aging vessels and the deferred orders of the past several years have resulted in tightening

cargo capacity supply and demand and a steady upturn in demand for replacement of the large numbers of VLCCs built between 1974 and 1978 is anticipated after fiscal 1997. With this in mind, core demand should steadily shift from bulk carriers and container ships to tankers.

Because increased costs are predicted for South Korea due to rising write-off costs for substantial plant expansion and soaring wages, Japan should continue to maintain its superior position in international competition for orders in fiscal 1997 if exchange rates remain at their current levels.

While completed construction orders will continue at high levels, orders taken in the past strong-yen period will be completed in fiscal 1997 as the first stage, and as proceeds from the completed ships will rise, shipbuilding companies should move past their periods of poorest earnings. As for order prices, while declining bulk carrier and container ship orders will have a bearish impact, rising tanker replacement demand should make a positive contribution.

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