

# Overproduction, Meager Exports Plague Industry

## Machine tools

Machine tool orders began to rebound in the second half of fiscal 1994 and solid internal and external demand was also sustained in fiscal 1995. Replacement investment, which had been held to a minimum over the past several years, finally began to pick up and this boosted internal demand growth. However, because the economy's outlook is uncertain, customers such as the auto and machinery industries have been cautious regarding new investment to increase capacity.

Healthy external demand continued in fiscal 1995, supported primarily by shipments to the U.S. This was largely because the automotive industry, led by the "Big Three" car manufacturers, invested heavily in restructuring. Exports to Asia also remained buoyant, with the focus on Japanese manufacturers who had expanded abroad.

Although machine tool orders will slow in fiscal 1996, the growth trend will

be sustained and an increase of 7.2% over the previous year is anticipated. Internal demand has always been driven by replacement demand and expectations are that this trend will continue in fiscal 1996, with sluggish growth through the latter half of the fiscal year. As a result, internal demand will be held to a 6.1% increase compared to the year before (see graph). Domestic machine tool demand is expected to hit an interim peak in fiscal 1996, but this will still be no more than 50% of the previous 1990 record high.

Growth will be similarly slow in external demand, with a year-on-year increase of 8.2% forecast (see graph). A lull in restructuring investment will result in declining exports to the U.S. and this will be the main factor in the slower growth rate. Exports to Asia should continue to remain satisfactory, on the other hand. However, with future growth predicted for Taiwanese and South Korean manufacturers, there is

some question whether the current high market share held by Japanese machine tools will remain secure.

## Construction machinery

Construction equipment demand got off to a slow start in 1995. Particularly within Japan, demand for hydraulic shovels, an industry mainstay, was weak as pessimism regarding the economic outlook increased in early spring. Signs of a recovery were gradually visible from the end of the first half, but the tone was still poor and, as a consequence, domestic demand in fiscal 1995 remained at

fiscal 1994 levels (see graph). Overseas demand from the leading destination, the U.S., was excellent from the beginning of 1995. However, as the U.S. economy decelerated, construction machinery exports also ran out of strength from the latter half of fiscal 1995. Domestic manufacturing also demonstrated strong growth at the start of the year, but misreading of demand led to substantial overproduction. Appropriate inventory levels of around 10-15% were consequently exceeded in the first half, yielding expectations of a continued revamping of production until the end of fiscal 1995 to reduce inventories.

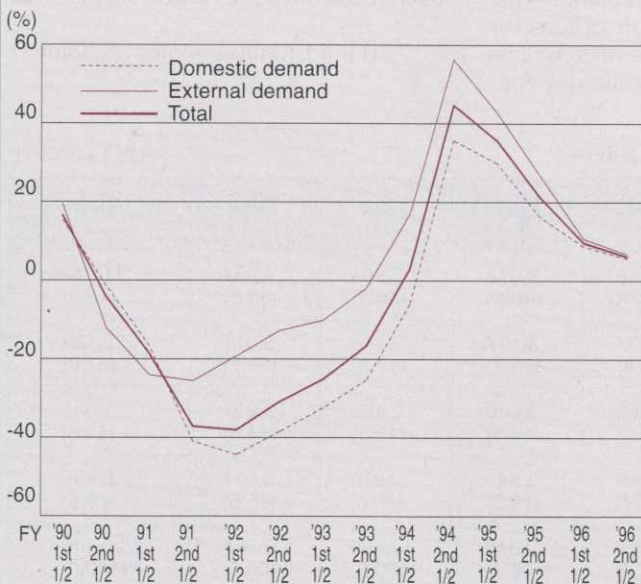
A continuing lag in demand is predicted in fiscal 1996. Private sector construction demand activity in particular has been quite slack and, while fiscal 1995's structural dependence on public works will continue, demand related to public works projects initiated under economic stimulus measures adopted in fiscal 1995 is likely to only gradually take shape in the first half of 1996. Predictions are that demand for construction machinery within Japan will consequently increase by about 1% and that the low levels of 1995 will persist.

With slack activity in the domestic construction industry, attention is focused on demand from the leasing and rental industries. With increasing construction equipment rentals—just under 30% of shipments of main construction equipment is for leasing and rental industry purposes—and larger shipments of equipment per lease/rental industry, customer heavy price competition has developed and this may spur price cuts.

Forecasts are that exports will lag in fiscal 1996 as demand in target markets in the U.S. and Europe declines and local manufacturing increases. Continued export strength, particularly for used equipment, is forecast for Asia, but new equipment from South Korea is expected to grab a portion of existing market share.

(Mitsuta Hideo, economist)

Year-on-Year Machine Tool Order Trends (by value)



Source: Japan Machine Tool Builders' Association (from second half of 1995, Industrial Bank of Japan, Ltd. forecasts)