

# JAPAN DATA RESPONSE

25<sup>th</sup> Oct. 2011



## SME Business Confidence (Oct.)

### *Business sentiment broadly stable*

- **Confidence amongst Japan's small and medium-sized enterprises (SMEs) dipped slightly in October. Sentiment had recovered rapidly from March's disaster and although it is expected to rebound in November, it has been broadly stable for several months with no sign of further improvement.**
- The Shoko Chukin Survey of SMEs is usually the first business survey released each month (the October manufacturing PMI will follow on Monday 31<sup>st</sup>), and is useful as it reflects conditions in an economically and politically important sector. The headline index fell to 46.4 in October from 47.2 in September, noticeably weaker than firms' own expectations of an improvement to 47.5 made at the time of the September survey.
- Overall, business sentiment appears to be broadly stable at a level comparable with before March's disaster. According to the headline index, confidence had recovered to 47.1 by July, a rapid rebound following the post-earthquake plunge to 36.1. The headline index is a weighted average of the manufacturing and non-manufacturing indices. (See Chart 1.) Business conditions in the manufacturing sector have been volatile since their rapid rebound from the disaster. In the non-manufacturing sector, conditions have been slower to recover – much like actual output in the tertiary sector.
- Firms' expectations for November are for a recovery in the headline sentiment index to 47.1, slightly below September's level. This may prove too optimistic. Firms' forecasts for the last three months have all been too strong, and other business surveys for the fourth quarter show conditions deteriorating. The forward-looking components of the manufacturing PMI deteriorated in September while the Tankan survey indicated that small and medium-sized enterprises expect conditions to worsen in Q4.
- Looking at the detail of the survey, there was a marked improvement in employment conditions and firms' financial position. (See Chart 2). The employment component reached its highest level in three years in October, but the improvement was limited to the non-manufacturing sector (manufacturing employment deteriorated), and is forecast to unwind in November. Likewise, manufacturing capacity utilisation deteriorated.
- Overall, **business conditions are at a level consistent with expanding output, but it is clear from the volatility of the index that sentiment is fragile.** Further turbulence in financial markets and yen strength are the main downside risks.

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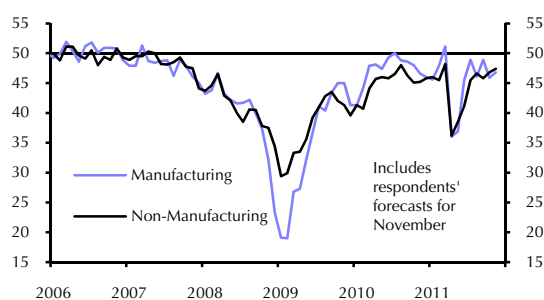
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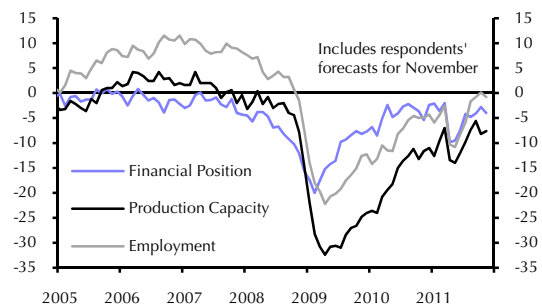
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Chart 1: SME Business Confidence



Source – Thomson Datastream

Chart 2: Selected Indicators



Source – Thomson Datastream