

31 May 2013 (No. of pages: 3)

Japanese report: 31 May 2013

April Industrial Production

Ongoing recovery vs. cautious projections

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Summary

- In *Indices of Industrial Production* (preliminary; Ministry of Economy, Trade and Industry [METI]), industrial production posted the fifth consecutive monthly gain in April (up 1.7% m/m) and overshoot market expectations (up 0.6%), confirming that the underlying recovery continues. By industry, thanks to steady domestic sales and exports to the US, transportation equipment jumped (up 11.8% m/m), driving overall production. Reflecting higher production of MOS memory ICs for smartphones, electronic components/devices posted a gain, also contributing to pushing up overall production, while the industry projected a slide in the previous METI report.
- The current METI survey projects overall production to remain flat 0.0% m/m in May and to decline 1.4% in June, meaning industries expect production to decelerate going forward. Although production has been firm in transportation equipment, the industry projects slides for both months, likely dragging down overall production.
- The current METI projection was bearish, raising concerns that overall production could decelerate going forward. However, we believe production should continue to increase. Whether production sees a stable recovery will depend on the export volume trend, which is expected to gain momentum as effects of a weaker yen since end-2012 are likely to emerge in full swing with a lag. Another positive factor is the ongoing improvement in the inventory-shipment balance, meaning downward pressure arising from inventory adjustments has gradually weakened.

| Industrial Production (m/m %; SA basis) | | | | | | | | Chart 1 |
|-----------------------------------------|------|------|------|------|------|------|------|------------|
| | 2012 | | | | 2013 | | | |
| | Sep | Oct | Nov | Dec | Jan | Feb | Mar | Apr |
| Industrial Production | -4.1 | 1.6 | -1.4 | 2.4 | 0.3 | 0.6 | 0.9 | 1.7 |
| Market consensus (Bloomberg) | | | | | | | | 0.6 |
| DIR estimate | | | | | | | | 0.5 |
| Shipments | -4.3 | -0.1 | -0.8 | 4.0 | -0.3 | 1.4 | 1.2 | 1.1 |
| Inventories | -0.9 | -0.1 | -1.2 | -1.2 | -0.4 | -2.0 | 0.2 | 0.6 |
| Inventory ratio | 4.2 | -2.1 | -0.3 | -0.6 | -3.2 | -1.1 | -1.2 | 0.5 |

Source: Ministry of Economy, Trade, and Industry; Bloomberg; compiled by DIR.

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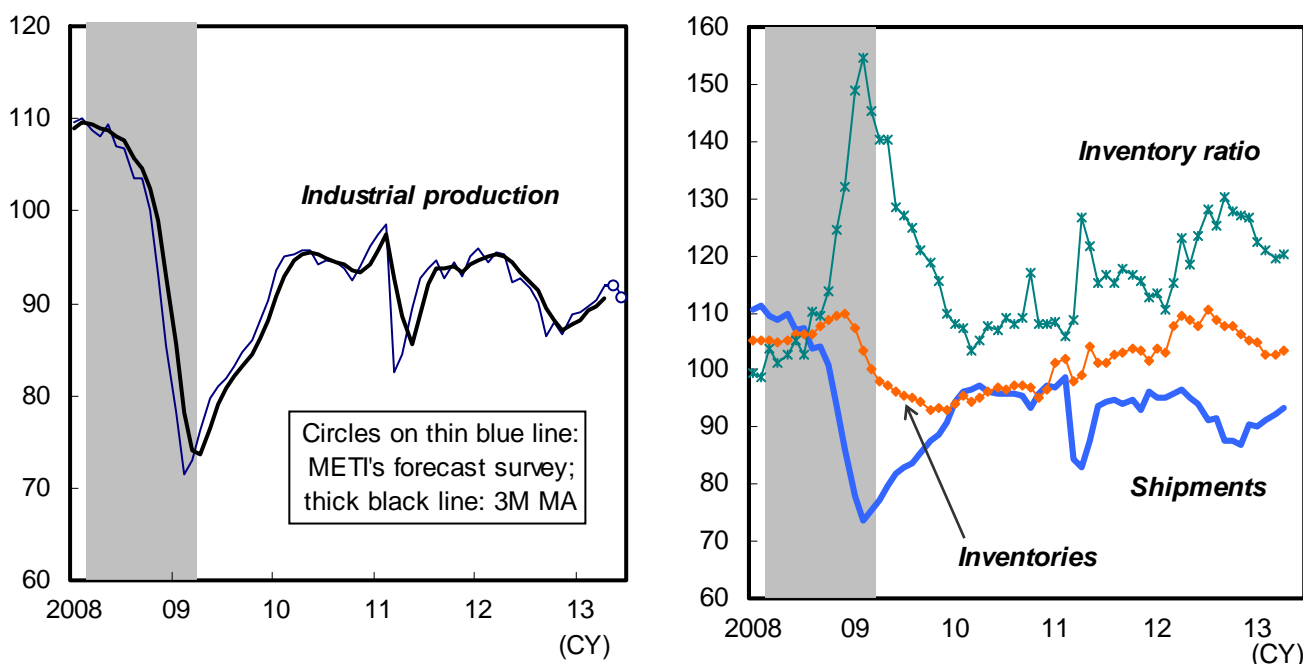
Economic Research

Fifth consecutive monthly gain in production

In *Indices of Industrial Production* (preliminary; Ministry of Economy, Trade and Industry [METI]), industrial production posted the fifth consecutive monthly gain in April (up 1.7% m/m) and overshot market expectations (up 0.6%), confirming that the underlying recovery continues. Shipments saw their third gain in a row (up 1.1%), while inventories increased (up 0.6%), resulting in the first rise (worsening) in the inventory-shipment ratio (up 0.5%) in seven months.

Production, Shipments, and Inventories (2005 = 100; SA basis)

Chart 2



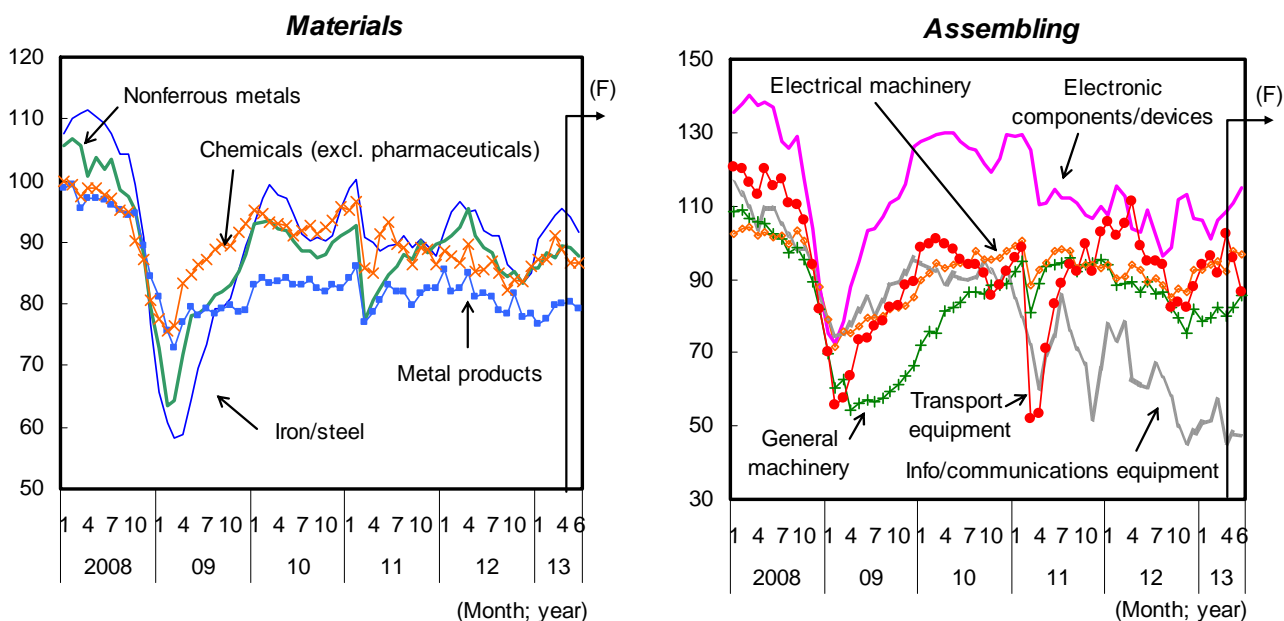
Source: Ministry of Economy, Trade, and Industry (METI); compiled by DIR.
Note: Shaded areas denote economic downturns.

Surge in transportation equipment driving overall production

Looking at April production by industry, thanks to steady domestic sales and exports to the US, transportation equipment jumped (up 11.8% m/m), driving overall production. Reflecting higher production of MOS memory ICs for smartphones, electronic components/devices posted a gain, also contributing to pushing up overall production, although the industry projected a slide in the previous METI report. At the same time, contrary to bearish projections in the previous METI report in general, material industries posted gains across the board, excluding chemicals. Meanwhile, dragged down by lower production of laptop/notebook PCs, info/communications equipment plunged (down 20.5%), pulling down overall production. The industry projected a slide in the previous METI report.

The current METI survey projects overall production to remain flat 0.0% m/m in May and to decline 1.4% in June, meaning industries expect production to decelerate going forward. Industries projecting slides for both months are iron/steel and nonferrous metals, exhibiting a cautious attitude on the part of materials industries in general. Assembling industries project recoveries in general, although seesawing on a monthly basis. Meanwhile, although production has been firm in transportation equipment, the industry projects slides for both months, likely dragging down overall production. Nevertheless, if May and June projections are fulfilled, industrial production would mark the second consecutive quarterly gain in Apr-Jun (up 2.0% q/q).

Production by Industry (2005 = 100; SA basis) Chart 3



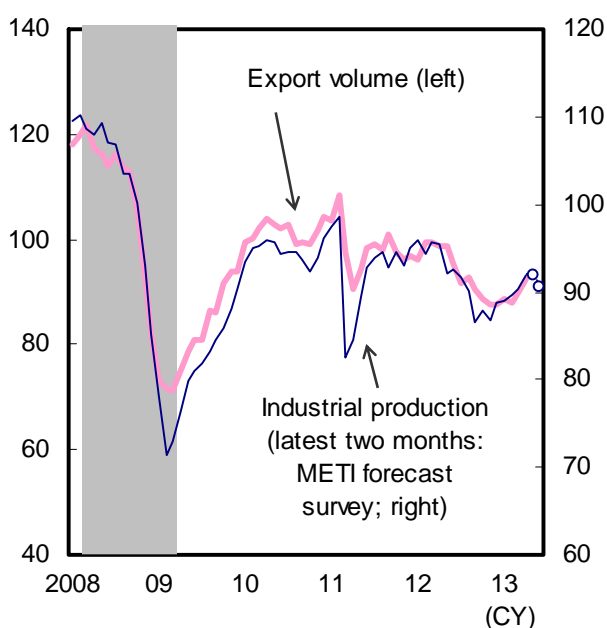
Source: Ministry of Economy, Trade, and Industry (METI); compiled by DIR.
 Note: Latest two months based on METI's forecast survey.

Production to grow driven by higher exports

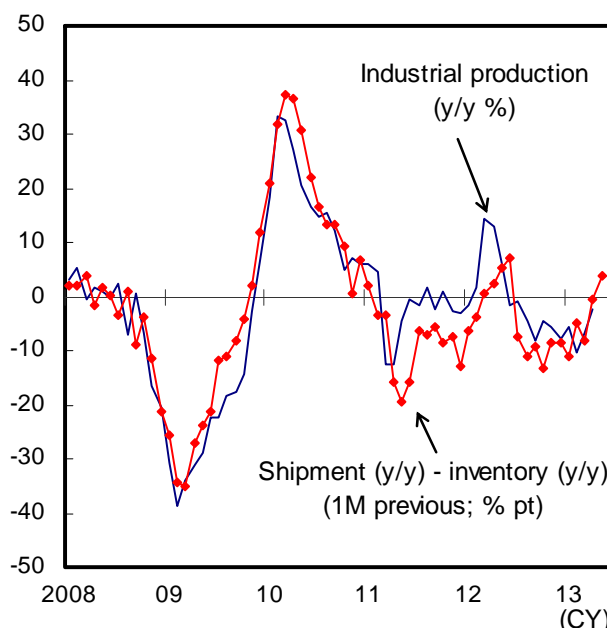
The current METI projection was bearish, raising concerns that production could decelerate going forward. However, we believe production should continue to increase. Whether production sees a stable recovery will depend on the export volume trend, which is expected to gain momentum as effects of a weaker yen since end-2012 are likely to emerge in full swing with a lag. Another positive factor is the ongoing improvement in the inventory-shipment balance, meaning downward pressure arising from inventory adjustments has gradually weakened.

Shipment-inventory Balance and Outlook for Industrial Production Chart 4

Production and Export Volume (2005 = 100)



Production and Shipment-inventory Balance



Source: Ministry of Economy, Trade, and Industry (METI); Cabinet Office; compiled by DIR.
 Note: Shaded area denotes economic downturn.