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# May Industrial Production

## Firm in general, ongoing recovery continues

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### Summary

- In *Indices of Industrial Production* (preliminary; Ministry of Economy, Trade and Industry [METI]), industrial production posted the fourth consecutive m/m gain in May (up 2.0%) and substantially overshoot market expectations (up 0.2%), confirming that the underlying recovery continues. Shipments saw the first gain in three months (up 0.8%), while inventories saw the first slide in two months (down 0.3%), resulting in the second consecutive monthly decline (improvement) in the inventory-shipment ratio (down 2.1%).
- The current METI survey projects overall production to decline 2.4% m/m in June but to increase 3.3% in July, meaning industries expect production to grow at a slower pace. Industries project declines across the board in June. In particular, iron/steel and transportation equipment will pull down overall production. Meanwhile, transportation equipment and general-purpose/production/business-oriented machinery project substantial gains in July, firming up overall production.
- We expect production to maintain the uptrend going forward. Export volume is likely to gain momentum as the effects of a weak yen trend that started at end-2012 will likely emerge in full swing with a lag, driving overall production. In addition, public works projects should accelerate with execution of the FY12 supplementary budget. At the same time, domestic demand will probably increase at a growing pace toward end-FY13, reflecting front-loaded demand prior to a consumption tax hike scheduled for April 2014. Such public and private sector factors are anticipated to boost production overall.

**Industrial Production (m/m %; SA basis)**

**Chart 1**

	2012					2013				
	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May
Industrial Production	-1.4	-2.2	0.3	-1.0	1.4	-0.6	0.9	0.1	0.9	<b>2.0</b>
Market consensus (Bloomberg)										0.2
DIR estimate										0.2
Shipments	-0.1	-2.5	0.3	-1.6	3.7	1.2	1.8	-0.8	-1.4	<b>0.8</b>
Inventories	0.4	0.0	0.0	-0.4	-1.3	-1.6	-1.2	-0.7	0.8	<b>-0.3</b>
Inventory ratio	0.2	2.6	-0.7	0.0	0.0	-3.8	-2.6	2.3	-5.1	<b>-2.1</b>

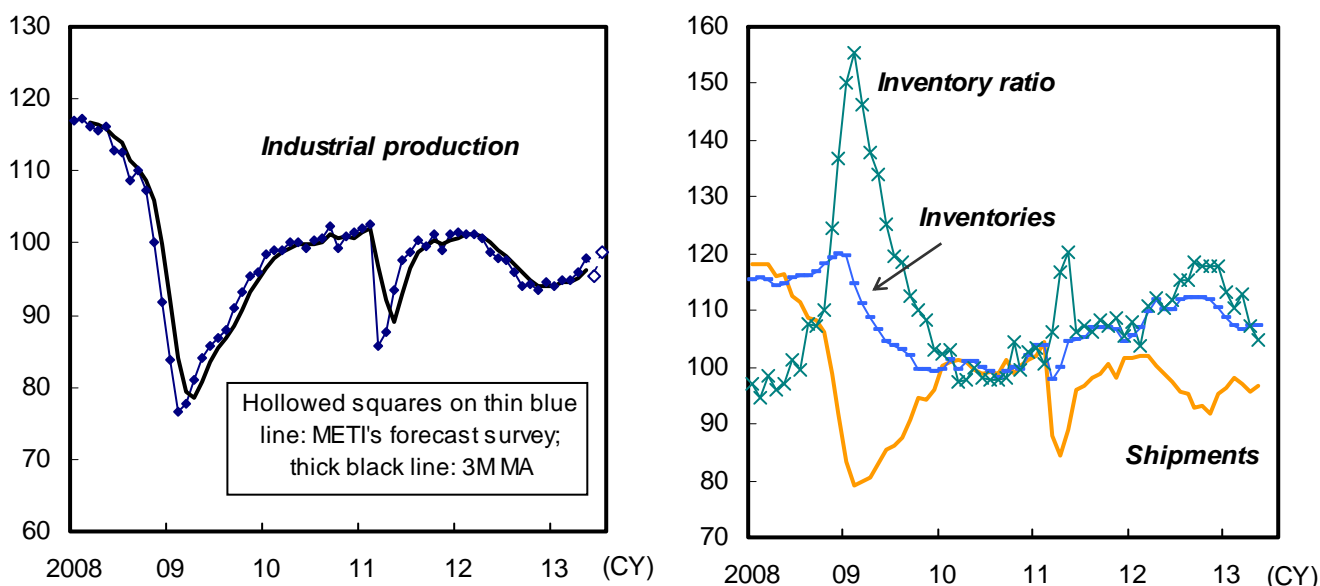
Source: Ministry of Economy, Trade, and Industry; Bloomberg; compiled by DIR.

## Fourth consecutive monthly gain in production

In *Indices of Industrial Production* (preliminary; METI), industrial production posted the fourth consecutive m/m gain in May (up 2.0%) and substantially overshoot market expectations (up 0.2%), confirming that the underlying recovery continues. Shipments saw the first gain in three months (up 0.8%), while inventories saw the first slide in two months (down 0.3%), resulting in the second consecutive monthly decline (improvement) in the inventory-shipment ratio (down 2.1%).

Production, Shipments, and Inventories (2010 = 100; SA basis)

Chart 2



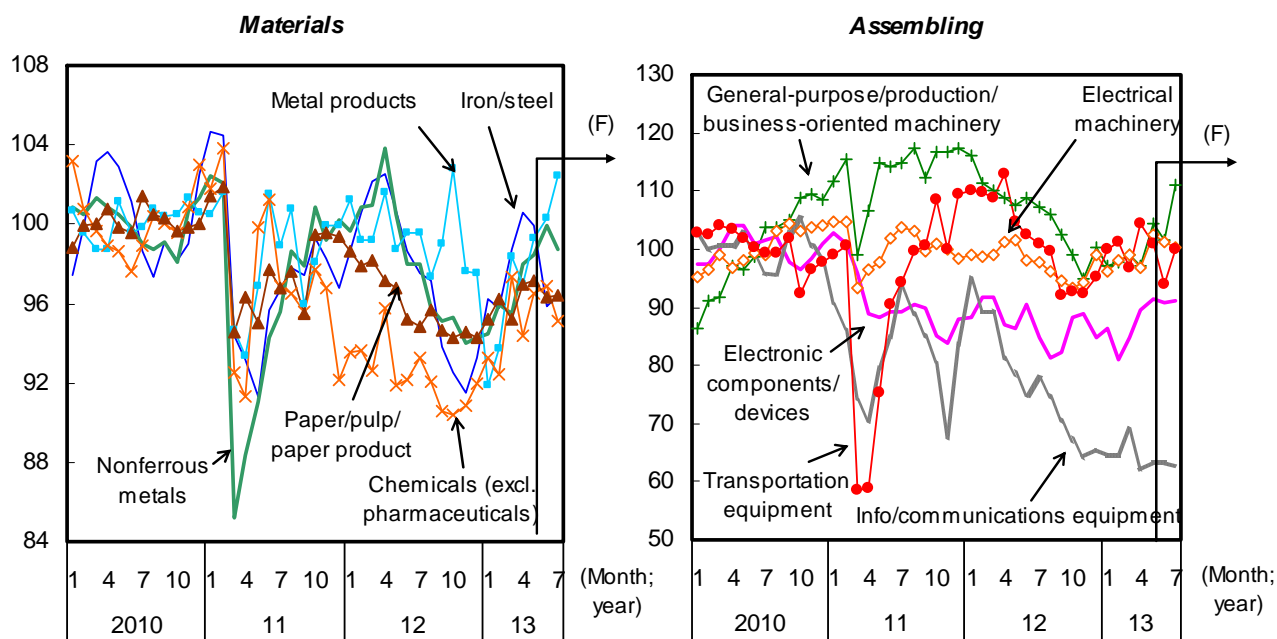
Source: Ministry of Economy, Trade, and Industry (METI); compiled by DIR.

## Wide ranging advance

Production increased m/m in May for 12 industries out of 15 for which data is available on a preliminary estimate basis, exhibiting a steady result as a whole. Prominent increases were seen in assembling industries, driving overall production. General-purpose/production/business-oriented machinery increased 7.6% m/m, reflecting advances in steam turbines and boiler components for electricity generation, and electrical machinery advanced 6.1%, supported by a gain in solar cell modules. However, as projected in the May preliminary report, transportation equipment declined, reflecting a fall in domestic automobile sales and lower exports to China and Europe, posting a slide of 3.4%. Meanwhile, materials industries continued to firm up in general, posting m/m gains across the board, albeit not so substantial. The iron/steel industry stood out, posting a slide of 3.4%.

The current METI survey projects overall production to decline 2.4% m/m in June but to increase 3.3% in July, meaning industries expect production to grow at a slower pace. Industries project declines across the board in June. In particular, iron/steel and transportation equipment will pull down overall production. Meanwhile, transportation equipment and general-purpose/production/business-oriented machinery project substantial gains in July, firming up overall production. As a whole, production will retreat and advance on a monthly basis. However, electrical machinery and info/communications equipment project slides for both months, exhibiting a cautious attitude. Nevertheless, if June projections are fulfilled, industrial production would mark the second consecutive q/q gain in Apr-Jun (up 1.8%).

**Production by Industry (2010 = 100; SA basis) Chart 3**

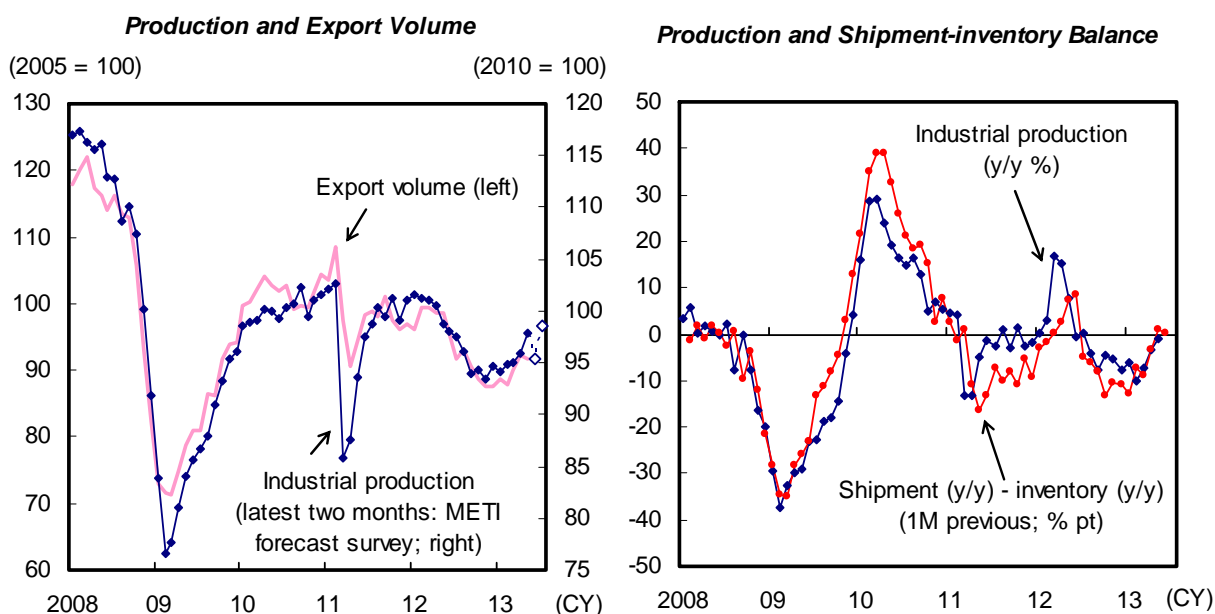


Source: Ministry of Economy, Trade, and Industry (METI); compiled by DIR. F: METI's forecast survey.

**Production to grow driven by higher exports**

We expect production to maintain the uptrend going forward. Whether production will steadily advance or not will depend on export volume, which is likely to gain momentum as the effects of a weak yen trend that started at end-2012 will likely emerge in full swing with a lag. In addition, public works projects should accelerate with execution of the FY12 supplementary budget. At the same time, domestic demand will probably increase at a growing pace toward end-FY13, reflecting front-loaded demand prior to a consumption tax hike scheduled for April 2014. Such public and private sector factors are anticipated to boost production overall. Another positive factor is the ongoing improvement in the inventory-shipment balance, meaning downward pressure arising from inventory adjustments has gradually weakened.

**Production, Export Volume, and Shipment-inventory Balance Chart 4**



Source: Ministry of Economy, Trade, and Industry (METI); Cabinet Office; compiled by DIR.