

29 November 2013 (No. of pages: 4)

Japanese report: 29 Nov 2013

October Industrial Production

Undershot expectations but remained on underlying uptrend

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Summary

- In Indices of Industrial Production (preliminary; Ministry of Economy, Trade, and Industry [METI]), October industrial production saw the second m/m gain in a row (up 0.5%). Although undershooting the consensus expectation (up 2.0%), we maintain our view that production remains on an underlying uptrend. Indeed, METI's forecast survey projects production to increase going forward. Thus, being short of expectations alone does not warrant excessively pessimistic views.
- Production was mixed by industry, up m/m in nine, down in six. Among those that saw advances and pushed up overall production were general-purpose/production/business-oriented machinery, electrical machinery, and plastic products.
- METI's production forecast survey projects gains in overall production in November (up 0.9% m/m) and December (up 2.1%). As for November, gains are posted by general-purpose/production/business-oriented machinery (industry that has persistently posted projections of substantial gains), as well as by iron/steel and chemicals. As for December, gains are projected across the board, regardless of materials or assembling. Thus, the underlying uptrend is projected to continue in general.
- Going forward, we expect production to maintain the uptrend. Considering a likely acceleration in personal consumption centering on durable goods toward end-FY13 prior to the consumption tax hike scheduled for April 2014, and also taking into account public works projects likely maintaining the current high level, domestic demand will lift overall production. Meanwhile, export volume, which tends to move in tandem with industrial production, has slackened, centering on shipments to Asian trading partners. However, reflecting the weak yen and economic growth in the US, export volume is likely to return to an uptrend, driving production.

Industrial Production (m/m %; SA basis)

Chart 1

	2013									
	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	Oct
Industrial Production	-0.6	0.9	0.1	0.9	1.9	-3.1	3.4	-0.9	1.3	0.5
Market consensus (Bloomberg)										2.0
DIR estimate										0.7
Shipments	1.2	1.8	-0.8	-1.4	1.0	-3.2	2.0	-0.1	1.5	1.8
Inventories	-1.6	-1.2	-0.7	0.8	-0.4	0.0	1.6	-0.2	-0.2	-0.5
Inventory ratio	-3.8	-2.6	2.3	-5.1	-2.1	5.9	-0.5	1.8	-2.1	-3.7

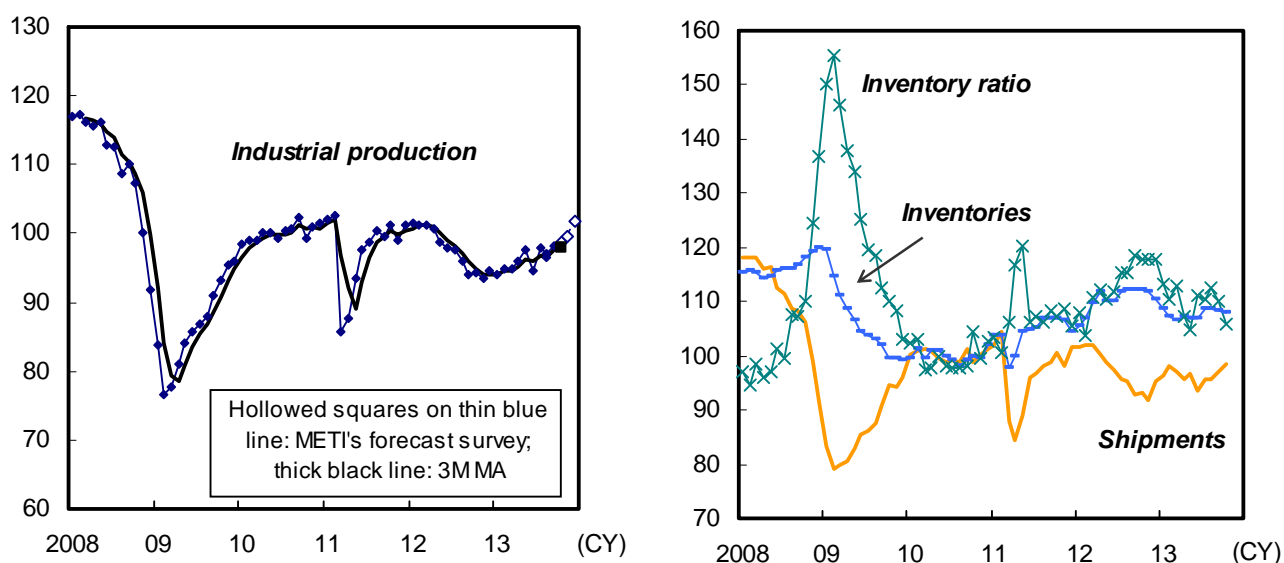
Source: Ministry of Economy, Trade, and Industry; Bloomberg; compiled by DIR.

Second m/m gain in a row

In Indices of Industrial Production (preliminary; METI), October industrial production saw the second m/m gain in a row (up 0.5%). Although undershooting the consensus expectation (up 2.0%), we maintain our view that production remains on an underlying uptrend. Indeed, METI's forecast survey projects production to increase going forward. Thus, being short of expectations alone does not warrant excessively pessimistic views. Shipments saw the second monthly gain in a row (up 1.8%), while inventories posted the third monthly slide in a row (down 0.5%), resulting in a decline (improvement) in the inventory-shipment ratio (down 3.7%).

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

Chart 2



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

General-purpose/production/business-oriented machinery, electrical machinery, driving overall production

Production was mixed by industry, up m/m in nine, down in six. Among those that saw advances and pushed up overall production were general-purpose/production/business-oriented machinery, electrical machinery, and plastic products. Gains in the former two were as projected in METI's forecast survey released in the previous month but short of the projections, leading to overall production undershooting expectations.

General-purpose/production/business-oriented machinery posted the first gain in three months (up 7.4% m/m), driven by semiconductor manufacturing equipment, which turned around from a persistent downtrend to a substantial gain (up 46.9%). Electrical machinery saw the first gain in two months (up 5.4%), driven by a surge in separate-type air conditioners (up 15.8%). Separate-type air conditioners have been on an uptrend since the start of 2013, perhaps reflecting a steady housing investment trend. Plastic products saw the second monthly gain in a row (up 2.3%), reflecting a gain in plastic film sheets for flat-TV and smartphone screens.

Among those that saw declines and pulled down overall production were electronic components/devices, metal products, and transportation equipment. Electronic components/devices

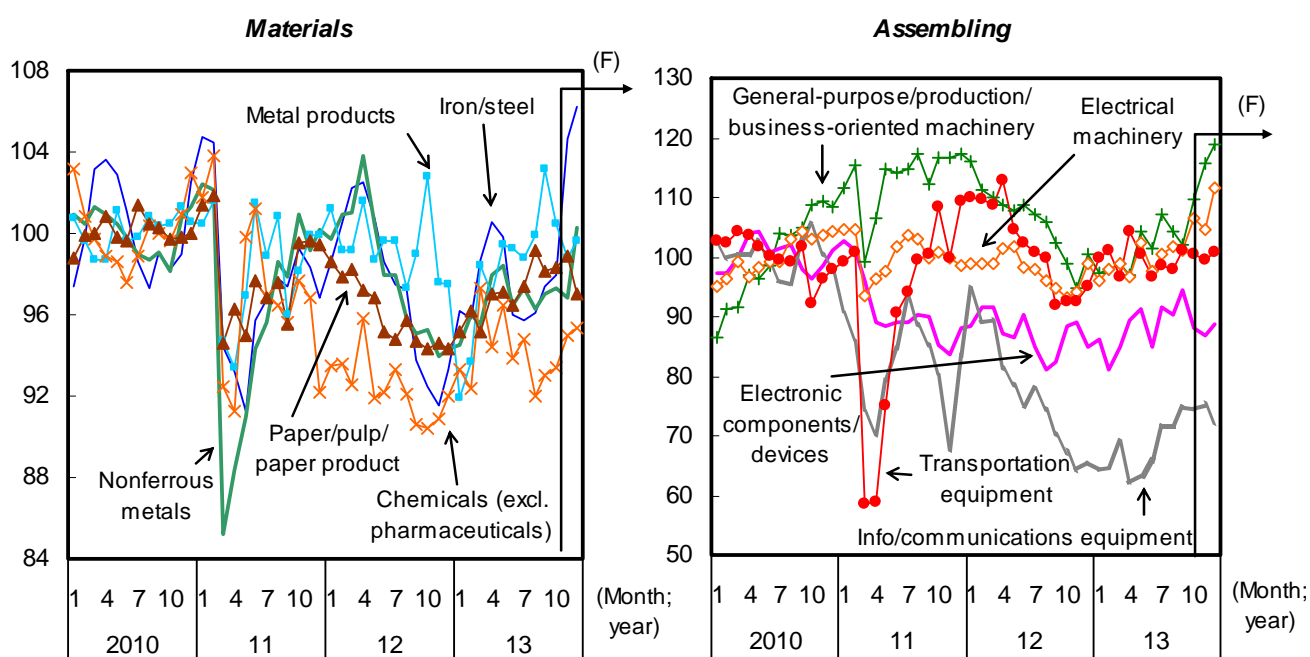
declined (down 6.8%), reflecting a plunge in electronic connectors, as well as a retreat from previous month's gains in active-matrix LCD panels (small, midsize) and MOS ICs, components related to smartphones/tablet devices. Metal products declined (down 2.6%), due to a slide in those for bridges, products that tend to see significant monthly fluctuations. Transportation equipment saw the first slide in two months (down 0.4%), reflecting a decline in mini-vehicles.

Broad-based gains projected

METI's production forecast survey projects gains in overall production in November (up 0.9% m/m) and December (up 2.1%). As for November, gains are posted by general-purpose/production/business-oriented machinery (up 5.3%)—an industry that has persistently posted projections of substantial gains—as well as by iron/steel (up 6.8%) and chemicals (up 1.7%). As for December, excluding projections of declines by info/communications equipment (down 3.9%) and paper/pulp products (down 1.9%), gains are projected across the board, regardless of materials or assembling. Thus, the underlying uptrend is projected to continue in general.

Production by Industry (2010 = 100; SA basis)

Chart 3



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

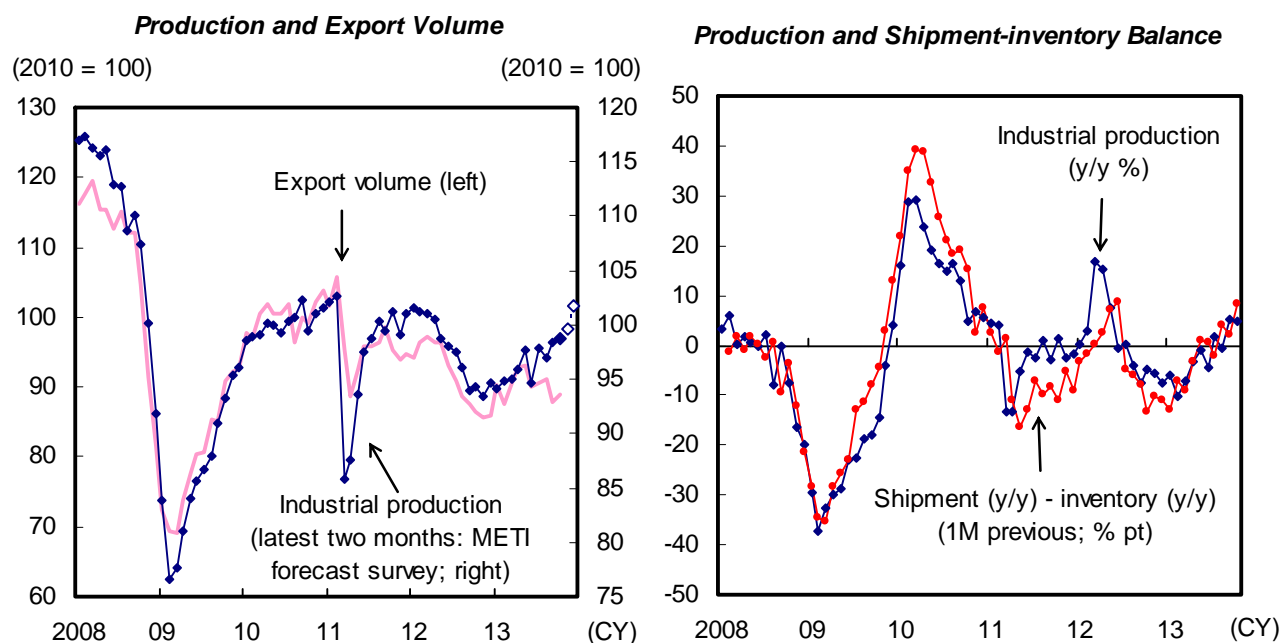
F: METI's forecast survey.

Domestic demand to accelerate toward end-FY13 and to drive production

Going forward, we expect production to maintain the uptrend. Considering a likely acceleration in personal consumption centering on durable goods toward end-FY13 prior to the consumption tax hike scheduled for April 2014, and also taking into account public works projects likely maintaining the current high level, domestic demand will lift overall production. Meanwhile, export volume, which tends to move in tandem with industrial production, has slackened, centering on shipments to Asian trading partners. However, reflecting the weak yen and economic growth in the US, export volume is likely to return to an uptrend, driving production.

Production, Export Volume, and Shipment-inventory Balance

Chart 4



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