28 February 2014 (No. of pages: 4)

Japanese report: 28 Feb 2014

January Industrial Production

Growth high in anticipation of last minute demand, but declines expected in March

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Summary

- January 2014 indices of industrial production was up 4.0% m/m, recording its second consecutive month of growth. Growth was especially high this time around, exceeding market consensus (+2.8%) and bringing further affirmation of the growth trend.

- As for production by industry, eleven out of the total of fifteen industries recorded m/m gains, with production increases seen in a broad range of industries. Of these, transport machinery (+8.0%) and general-purpose/production/business-oriented machinery (+9.6%) won major increases in accordance with business plans and helped to push overall figures up. Last minute demand in anticipation of the upcoming consumption tax hike, as well as attempts on the part of manufacturers to prepare themselves for the reactionary decline expected to occur after the tax hike has gone into effect, were especially notable in the transport machinery industry, as well as the electrical machinery, and info/communications equipment industries.

- METI's production forecast survey projects February up 1.3% m/m according to production plans, while March is expected to see a decline at -3.2%. Production should continue its growth trend in the immediate future, but then run into a slowdown a bit further up the road. The increases in production seen in February, as well as the declines expected in March, are thought to be due to last minute demand in anticipation of the upcoming consumption tax hike, as well as attempts on the part of manufacturers to prepare themselves for the reactionary decline expected to occur after the tax hike has gone into effect. We suggest keeping a close eye on developments in the immediate future.

Industrial Production (m/m %; SA basis) **Chart 1**

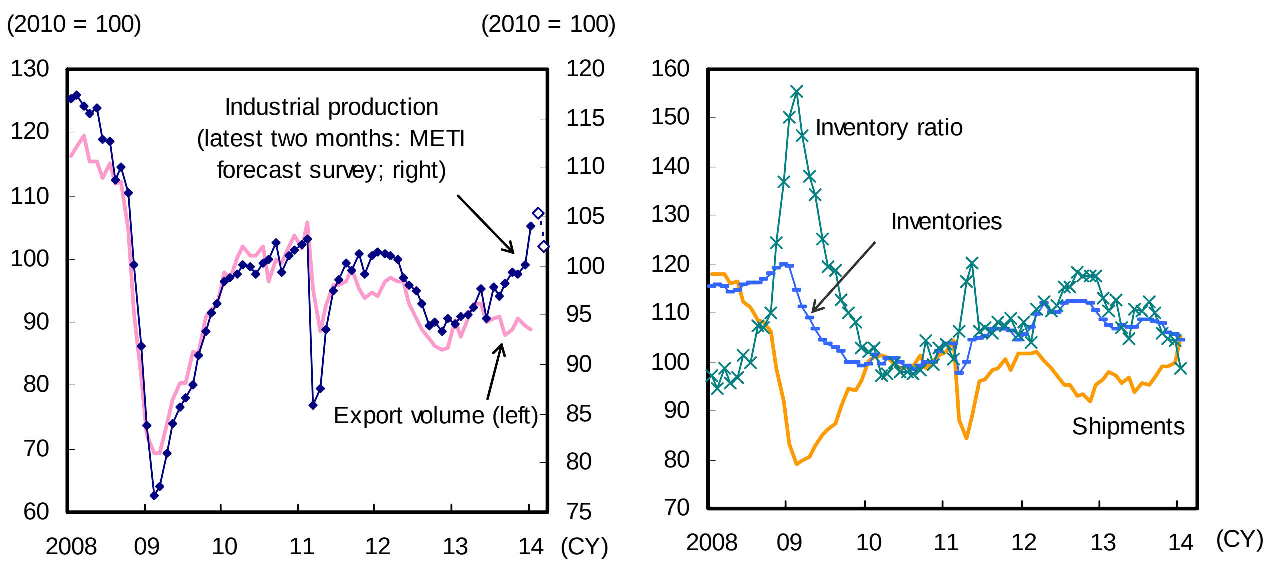
	2013									2014
	Apr	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Jan
Industrial Production	0.9	1.9	-3.1	3.4	-0.9	1.3	1.0	-0.1	0.9	**4.0**
Market consensus (Bloomberg)										2.8
DIR estimate										3.5
Shipments	-1.4	1.0	-3.2	2.0	-0.1	1.5	2.3	0.0	0.8	**5.1**
Inventories	0.8	-0.4	0.0	1.6	-0.2	-0.2	-0.3	-1.8	-0.5	**-0.9**
Inventory ratio	-5.1	-2.1	5.9	-0.5	1.8	-2.1	-3.7	-1.2	-0.1	**-5.6**

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

January 2014 indices of industrial production achieve second consecutive month of growth

January 2014 indices of industrial production was up 4.0% m/m, recording its second consecutive month of growth. Growth was especially high this time around, exceeding market consensus (+2.8%) and bringing further affirmation of the growth trend. The shipment index was also up by 5.1%, showing m/m growth for the second consecutive month, while the inventory index recorded a m/m decline of 0.9%, the sixth consecutive month of declines. Consequently, the index of inventory rate fell by 5.6% m/m, its fifth consecutive month of declines.

Production, Export Volume, Shipments, and Inventories (2010 = 100; SA basis) **Chart 2**



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

Production grows across broad range of industries. Last minute demand pushes numbers up in some areas

As for production by industry, eleven out of the total of fifteen industries recorded m/m gains, with production increases seen in a broad range of industries. Of these, transport machinery (+8.0%) and general-purpose/production/business-oriented machinery (+9.6%) won major increases in accordance with business plans and helped to push overall figures up.

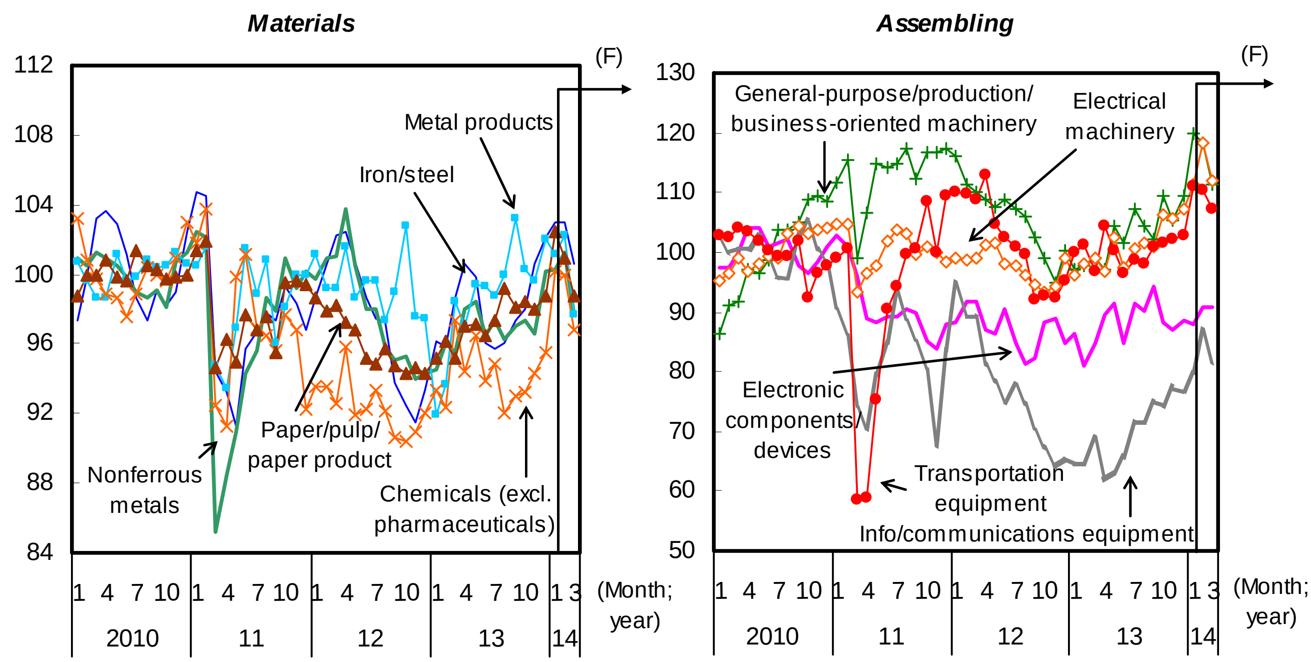
Transport machinery grew for the fifth consecutive month at +8.0% m/m, while last minute demand in anticipation of the April 2014 consumption tax hike was already noticeable in January auto industry performance where favorable domestic sales pushed production up. Shipments saw major growth in January at +6.1% though they fell below the numbers for production. Consequently, the inventory index was up 3.4%. It is assumed that this was for the purpose of beefing up inventories in expectation of last minute demand intensifying prior to April. Meanwhile, the electrical machinery industry (+4.1%) and the info/communications equipment industry (+4.2%) also exhibited the effects of last minute demand. Here also production was pushed up due to preparations for an increase in activity just before the tax hike comes into effect.

General-purpose/production/business-oriented machinery (+9.6%) grew for the second consecutive month, with semiconductor manufacturing equipment recording a major increase of 23.6% m/m, helping to push the overall production figures for the industry up. Meanwhile, shipments also achieved major gains at +16.7% m/m, where growth was mainly in the areas of general purpose steam turbines and water tube boilers for use in electrical power, and semiconductor manufacturing equipment. As for capital goods, there are few possibilities that this area will be affected by last minute demand associated with the tax hike. Therefore it is thought to be most likely that growth in production and shipments of general-purpose/production/business-oriented machinery reflects increased capex in both the domestic and overseas markets.

Production forecast survey sees a decline in March

METI's production forecast survey projects February up 1.3% m/m according to production plans, while March is expected to see a decline at -3.2%. Production should continue its growth trend in the immediate future, but then run into a slowdown a bit further up the road. February expects to see overall figures improve thanks to positive performance in the electronic parts and devices industry (+3.2%), electrical machinery (+6.0%), and the info/communications equipment industry (+9.0%). On the other hand, all industries are projecting declines for the month of March. The increases in production seen in February, as well as the declines expected in March, are thought to be due to last minute demand in anticipation of the upcoming consumption tax hike, as well as attempts on the part of manufacturers to prepare themselves for the reactionary decline expected to occur after the tax hike has gone into effect. We suggest keeping a close eye on developments in the immediate future.

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

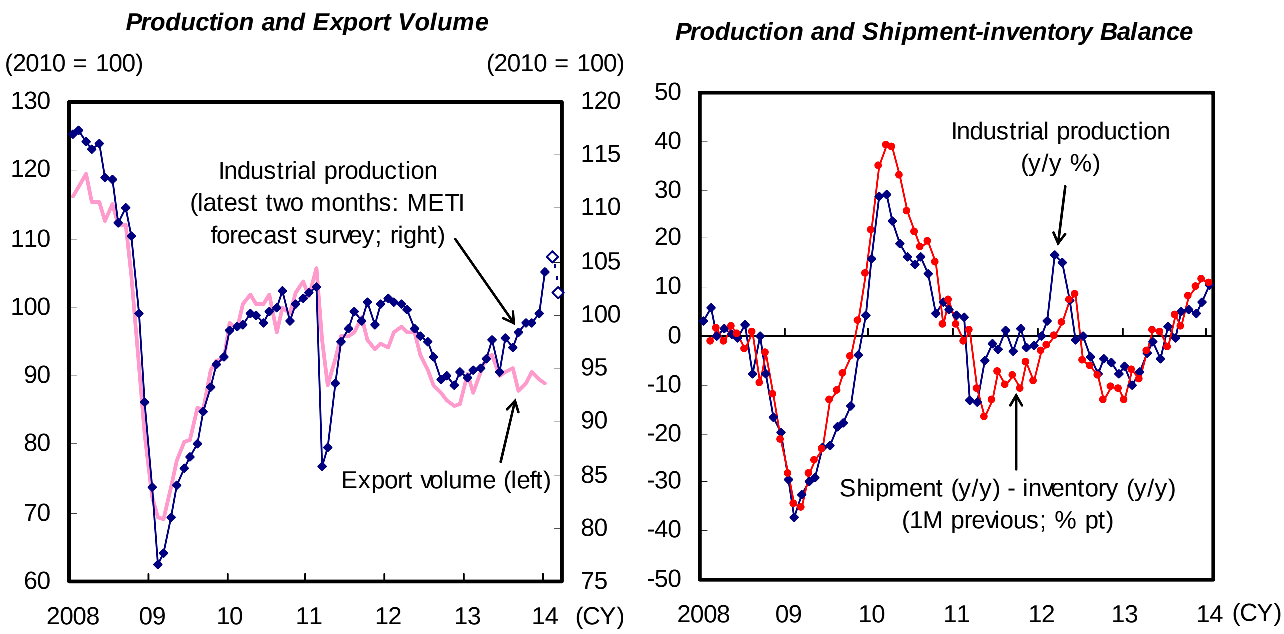


Source: Ministry of Economy, Trade, and Industry (METI); compiled by DIR.
F: METI's forecast survey.

Goods for export and investment goods to drive growth after tax hike

Industrial production is expected to continue its growth trend in the coming months. As was seen in the production forecast survey, a reactionary decline is expected in personal consumption after the tax hike goes into effect in April, and possibilities are high that this will also temporarily effect production. However, exports, which had been improving gradually up till now, are expected to strengthen their momentum in the near future due to the effects of the weak yen and overseas economic expansion centering on the U.S. Increase in exports is expected to provide support for a continuation of the upswing in capex. Meanwhile, public investment is expected to continue at a high level, bringing expectations that growth in production of goods for export and investment goods will drive further gains in production in the near future.

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



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