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February Industrial Production

Production suffers downturn due to major snowstorms

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Summary

- February 2014 indices of industrial production recorded the first decline in 3 months, down by -2.3% m/m, also falling below market consensus (+0.3% m/m). Growth in production had been expected due to last minute demand associated with the April 1 increase in the consumption tax, but instead production fell despite the positive outlook, adding an especially negative tone to this month's results. However, the decline in production in February was due largely to major snowstorms which brought disorder to the distribution network and caused operations to stop in some areas, hence leaving our assessment unchanged regarding the continuation of the growth trend in production in the long run.
- As for production by industry in February, eleven out of the total of fifteen industries recorded m/m declines, with production slowdowns in a broad range of industries. Transport machinery and general-purpose/production/business-oriented machinery had expected declines in February since the previous month's production forecast survey, but actually suffered worse declines than were expected. In addition, the info/communications equipment industries, which had been expecting major increases in production, were down despite expectations, helping to push overall results further downward.
- METI's production forecast survey projects March results to grow by 0.9% m/m according to production plans, while April is expected to see a decline of -0.6%. March was expected to be down according to the previous month's production forecast survey, but was revised upwards due to the sluggish results reported for February. On the other hand, April expects declines in production for most industries, with info/communications equipment contributing to the overall decline despite its increase in production in March. All in all, production is expected to peak out in March.

Industrial Production (m/m %; SA basis)										Chart 1
	2013								2014	
	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb
Industrial Production	1.9	-3.1	3.4	-0.9	1.3	1.0	-0.1	0.9	3.8	-2.3
Market consensus (Bloomberg)										0.3
DIR estimate										-0.1
Shipments	1.0	-3.2	2.0	-0.1	1.5	2.3	0.0	0.8	5.1	-1.0
Inventories	-0.4	0.0	1.6	-0.2	-0.2	-0.3	-1.8	-0.5	-0.9	-0.8
Inventory ratio	-2.1	5.9	-0.5	1.8	-2.1	-3.7	-1.2	-0.1	-5.4	1.7

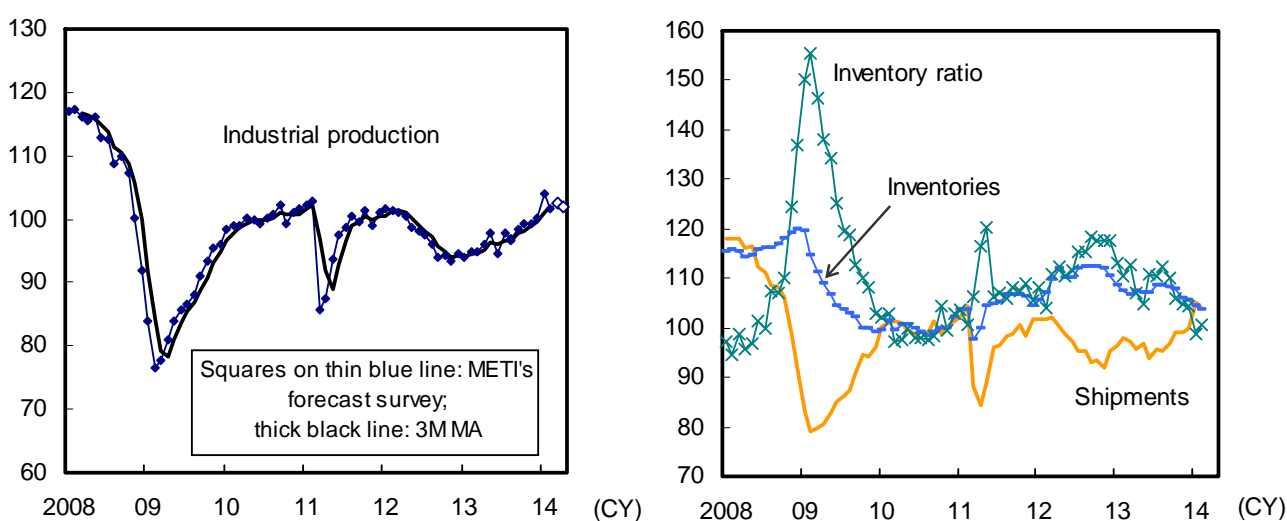
Source: Ministry of Economy, Trade, and Industry; Bloomberg; compiled by DIR.

February 2014 indices of industrial production fall below market consensus

February 2014 indices of industrial production recorded the first decline in 3 months, down by -2.3% m/m, also falling below market consensus (+0.3% m/m). Growth in production has been expected due to last minute demand associated with the April 1 increase in the consumption tax, but instead production fell despite the positive outlook, adding an especially negative tone to this month's results. However, the decline in production in February was due largely to major snowstorms which brought disorder to the distribution network and caused operations to stop in some areas, hence leaving our assessment unchanged regarding the continuation of the growth trend in production in the long run. However, the inventory index recorded its seventh consecutive month of decline at -0.8% m/m, while the shipment index fell for the first time in six months, recording -1.0%. The index of inventory rate therefore rose for the first time in six months by +1.7% m/m (a negative factor).

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

Chart 2



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

Production falls across broad range of industries.

As for production by industry in February, eleven out of the total of fifteen industries recorded m/m declines, with production slowdowns in a broad range of industries. Transport machinery and general-purpose/production/business-oriented machinery had expected declines in February since the previous month's production forecast survey, but actually suffered worse declines than were expected. In addition, the info/communications equipment industries, which had been expecting major increases in production, were down by m/m despite expectations, helping to push overall results further downward.

The transportation equipment industry experienced a decline in production for the first time in six months at -5.8% m/m. Though domestic auto sales have been maintaining robust sales due to last minute demand prior to the increase in the consumption tax in April, the halt of operations at industrial facilities in some areas due to major snowstorms caused production to drop. Shipments also declined for the first time in two months at -0.6% m/m. In addition to the unusually heavy snowfall, some auto manufacturers announced recalls of certain vehicles, which also cut shipments severely.

General-purpose/production/business-oriented machinery experienced declines in production for the first time in three months at -3.3% m/m. However, considering the major growth of the previous month, the extent of the decline was fairly modest, and high production levels continue. In terms of

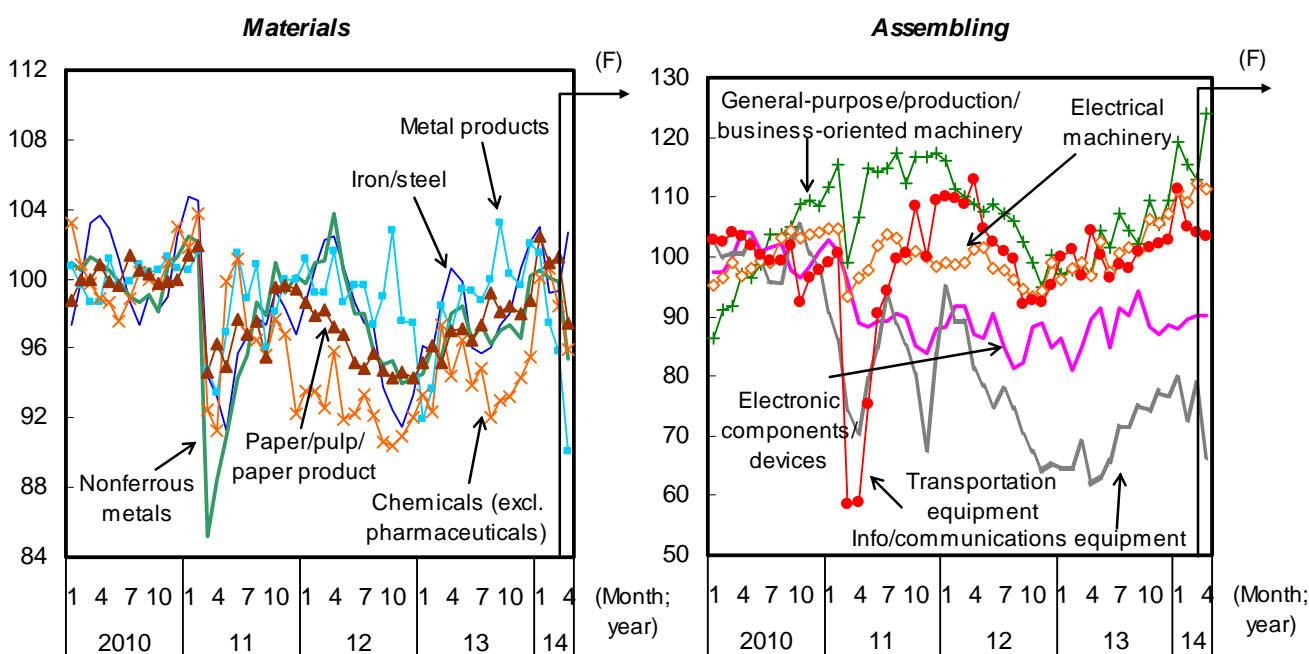
types of goods, the downtrend in boiler parts, which tend to fluctuate quite a bit from month to month, contributed to overall declines. Meanwhile, shipments were down by -5.0 m/m due mainly to declines in production of water-tube boilers and general purpose steam turbines, with grew considerably in January. Meanwhile, production and shipment of capital goods maintains robust performance reflecting the growing willingness of corporations to spend on capex in both the domestic and overseas markets.

March production plans revised upwards due to delayed work being shifted over from previous month

METI's production forecast survey projects March results to grow by 0.9% m/m according to production plans, while April is expected to see a decline of -0.6%. March was expected to be down according to the previous month's production forecast survey, but was revised upwards due to the sluggish results reported for February. March production plans by industry show major growth expected by industries which suffered a downturn in February, with info/communications equipment growing at 8.7% m/m, making up for the previous month's slowness. Meanwhile, growth in the following industries is expected to push overall results up, with electrical machinery growing +2.9% m/m and electronic parts and devices up +1.0%. On the other hand, April expects declines in production for most industries, with info/communications equipment contributing to the overall decline at -16.1% m/m despite its increase in production in March. However, general-purpose/production/business-oriented machinery is expected to record fairly high growth at +9.8% m/m, hence limiting the extent of the declines in overall terms. All in all, production is expected to peak out in March.

Production by Industry (2010 = 100; SA basis)

Chart 3

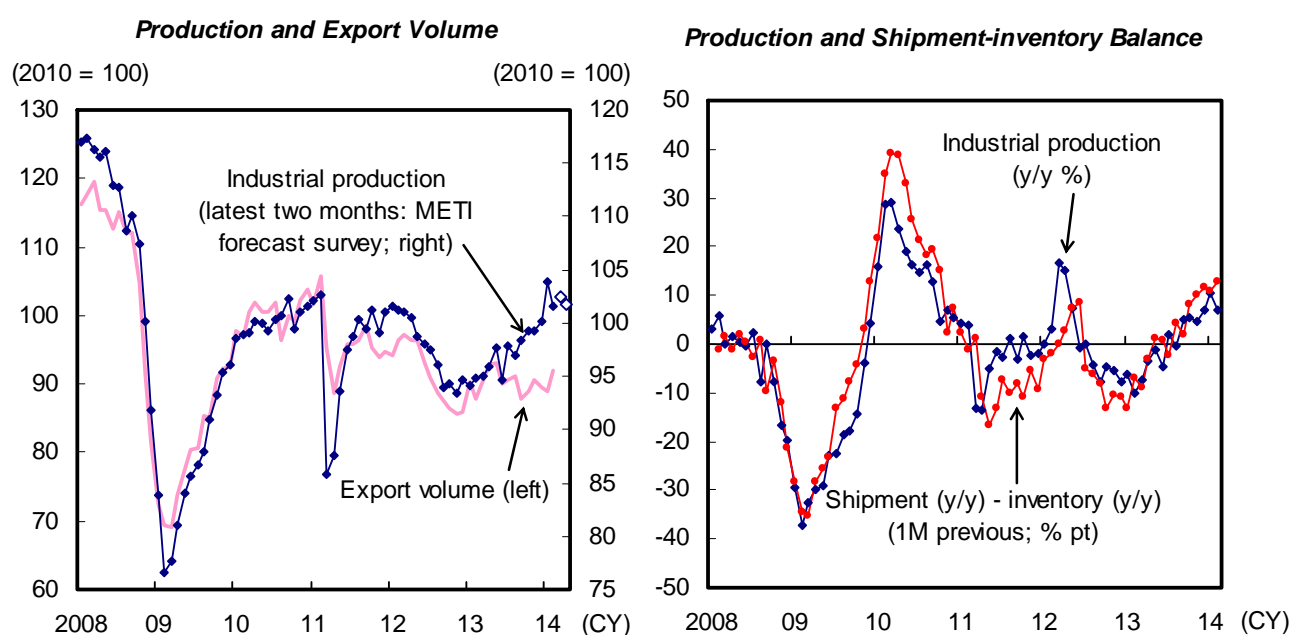


Source: Ministry of Economy, Trade, and Industry (METI); compiled by DIR.
F: METI's forecast survey.

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

Industrial production is expected to continue its growth trend in the coming months despite some minor fluctuations due to the increase in the consumption tax. After the tax hike personal consumption is expected to suffer a reactionary decline and may very well cause a temporary slowdown of production as well. However, exports, which have 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. Meanwhile, increase in exports is expected to provide support for a continuation of the upswing in capex. Public investment is expected to continue at a high level, bringing expectations that growth in production of goods for export and capital 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.