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May Industrial Production

Growth achieved for first time in two months, but production headed for slowdown

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Summary

- The May 2014 indices of industrial production achieved growth for the first time in two months, up 0.5% m/m, while at the same time falling below market consensus, which recorded +0.9%. In light of the April downturn, growth in May is considered to have been modest, leading to a sense that production has entered a slowdown. The shipment index fell for the fourth consecutive month at -1.2% m/m, while the inventory index rose for the first time in two months by +2.9% m/m, hence accompanied by an increase in the index of inventory rate for the first time in two months at +3.5%.
- As for production by industry in May, eight out of the total of fifteen industries recorded month-to-month growth. Of those reporting growth, transport equipment, textiles, and electronic components/devices helped push up overall results.
- According to METI's production forecast survey, June production schedules are expected to suffer a decline of -0.7% m/m, while July is seen regaining some ground at +1.5% m/m. The result of this fluctuation is that on the whole, production is expected to mark time in the near future. As for June production plans by industry, information communication electronics equipment is expected to continue the declines experienced in May with a further decline of -5.7% seen. Meanwhile, transport equipment is expected to be down by -4.1%, helping to push down overall industry performance. There are also signs of a turnaround in July, the major factor being the general purpose production and business oriented machinery industry, which expects major growth of +8.0% m/m. But all in all, production is expected to falter in the near term, with the information communication electronics equipment industry expected to fall even more deeply into the downtrend at -10.3% m/m. we suggest keeping a sharp eye on future trends.

Industrial Production (m/m %; SA basis)

Chart 1

	2013					2014				
	Aug	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May
Industrial Production	-0.5	1.5	0.6	0.3	0.5	3.9	-2.3	0.7	-2.8	0.5
Market consensus (Bloomberg)										0.9
DIR estimate										1.3
Shipments	0.1	1.7	1.3	0.1	0.2	5.1	-1.0	-0.2	-5.0	-1.2
Inventories	-0.7	-0.1	-0.3	-1.4	-0.2	-0.4	-0.9	1.4	-0.5	2.9
Inventory ratio	1.4	-2.3	-2.5	-1.1	-0.2	-4.6	3.9	2.1	-1.6	3.5

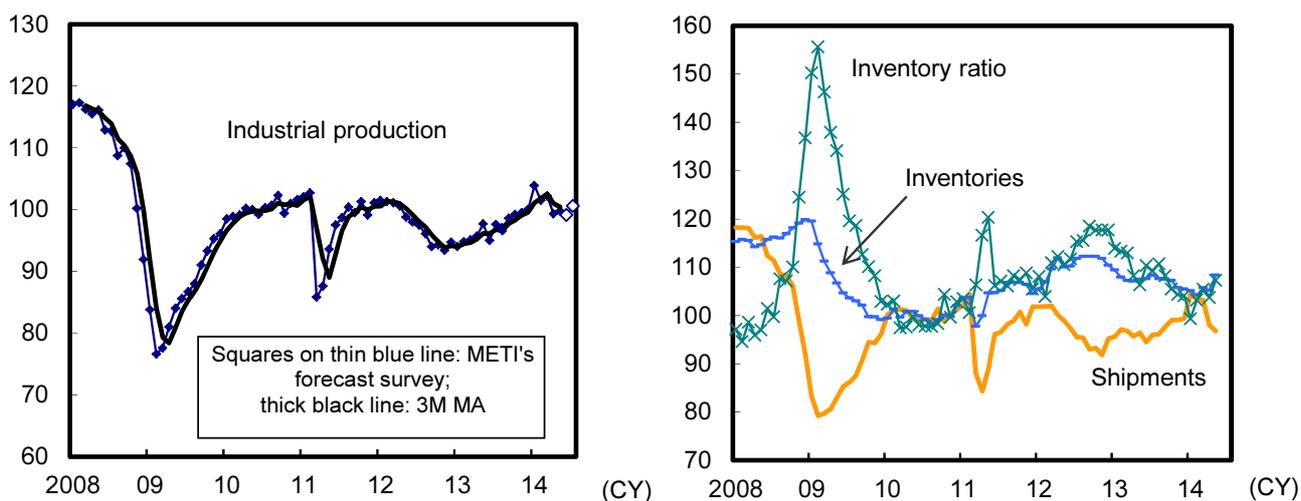
Source: Ministry of Economy, Trade, and Industry; Bloomberg; compiled by DIR.

May Industrial Production Falls Below Market Consensus

The May 2014 indices of industrial production achieved growth for the first time in two months, up 0.5% m/m, while at the same time falling below market consensus, which recorded +0.9%. In light of the April downturn, growth in May is considered to have been modest, leading to a sense that production has entered a slowdown. The shipment index fell for the fourth consecutive month at -1.2% m/m, while the inventory index rose for the first time in two months by +2.9% m/m, hence accompanied by an increase in the index of inventory rate for the first time in two months at +3.5%.

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

Chart 2



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

Transport equipment, textiles, and electronic components/devices report growth in production

As for performance by source of demand, eight out of the total of fifteen industries recorded month-to-month growth. Of those reporting growth, transport equipment, textiles, and electronic components/devices helped push up overall results.

Transport related equipment reported growth in production for the first time in two months at +1.9% m/m, while the domestic market for new car sales continued to suffer declines in volume. The shipment index was down for the third month in a row at -4.8% m/m, while production of transport related machinery maintained a steady undertone supported by movement toward recovery of inventories after the declines experienced as a result of last minute demand prior to the increase in consumption tax. Electronic parts and devices reported growth in production for the first time in two months at +0.4% m/m, due mainly to growth in active matrix liquid crystal displays used in smart phones, and tablet devices. Meanwhile, despite industry overall reporting declines in production, electronic components/devices is maintaining an overall growth trend, and continues to gain robust performance.

Industries reporting declines included chemicals (excluding pharmaceuticals), information & communications equipment, and general purpose production and business oriented machinery.

Results are actually going according to plan when it comes to the chemical industry, which was reported to be expecting declines in production in May on the previous month's production forecast survey as reported by METI. The major downturn in production of synthetic detergent in April, its second month in a row of decline, was a major factor in pushing down overall performance. Now, as

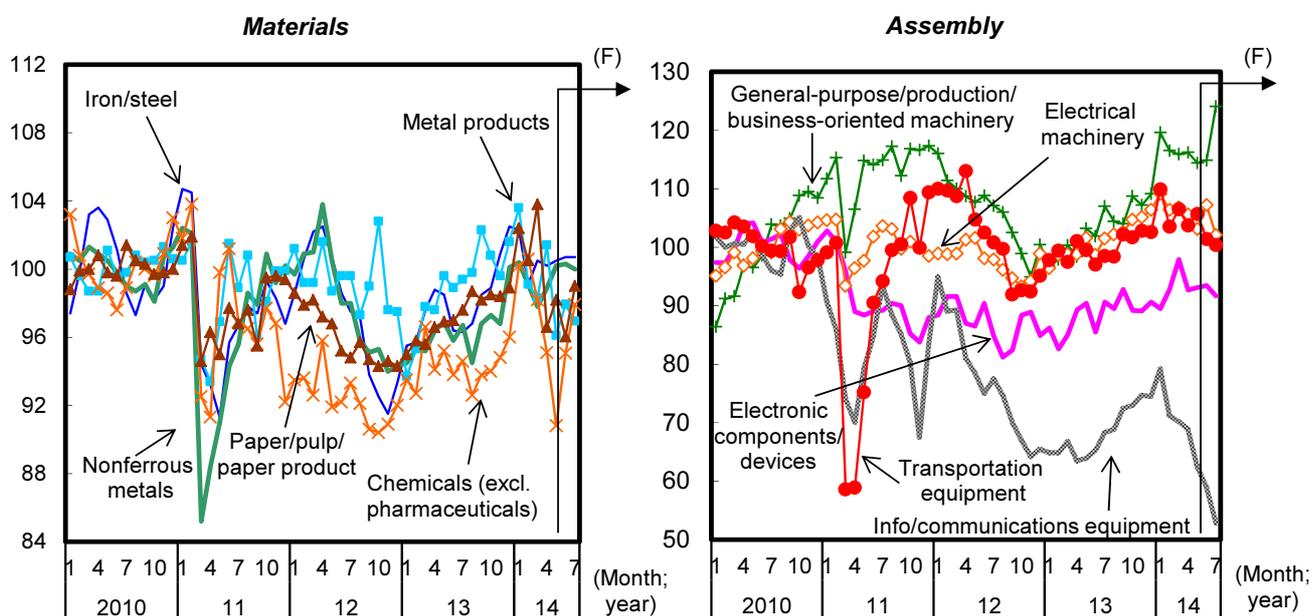
this downward trend continues for the chemical industry, it becomes a factor in bringing down production results for industry overall. Meanwhile, the information & communications equipment industry reported declines in production despite the announcement of plans as of the previous month to increase production. Performance was down by -9.3% m/m, the fourth consecutive month of decline. The major factor in the downturn was slow performance for both desktop and notebook computers. In addition to the reactionary decline occurring after the increase in consumption tax went into effect in April, there was also the effect of a last minute rush to buy new computers before Microsoft halted support for Windows XP, meaning that this industry actually experienced a kind of “double reactionary decline.”

Production Schedules Mark Time in June and July

According to METI’s production forecast survey, June production schedules are expected to suffer a decline of -0.7% m/m, while July is seen regaining some ground at +1.5% m/m. The result of this fluctuation is that on the whole, production is expected to mark time in the near future.

As for June production plans by industry, information & communications equipment is expected to continue the declines experienced in May with a further decline of -5.7% seen. Meanwhile, transport equipment is expected to be down by -4.1%, helping to push down overall industry performance. There are also signs of a turnaround in July, the major factor being the general purpose production and business oriented machinery industry, which expects major growth of +8.0% m/m. But all in all, production is expected to falter in the near term, with the information & communications industry expected to fall even more deeply into the downtrend at -10.3% m/m. we suggest keeping a sharp eye on future trends.

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



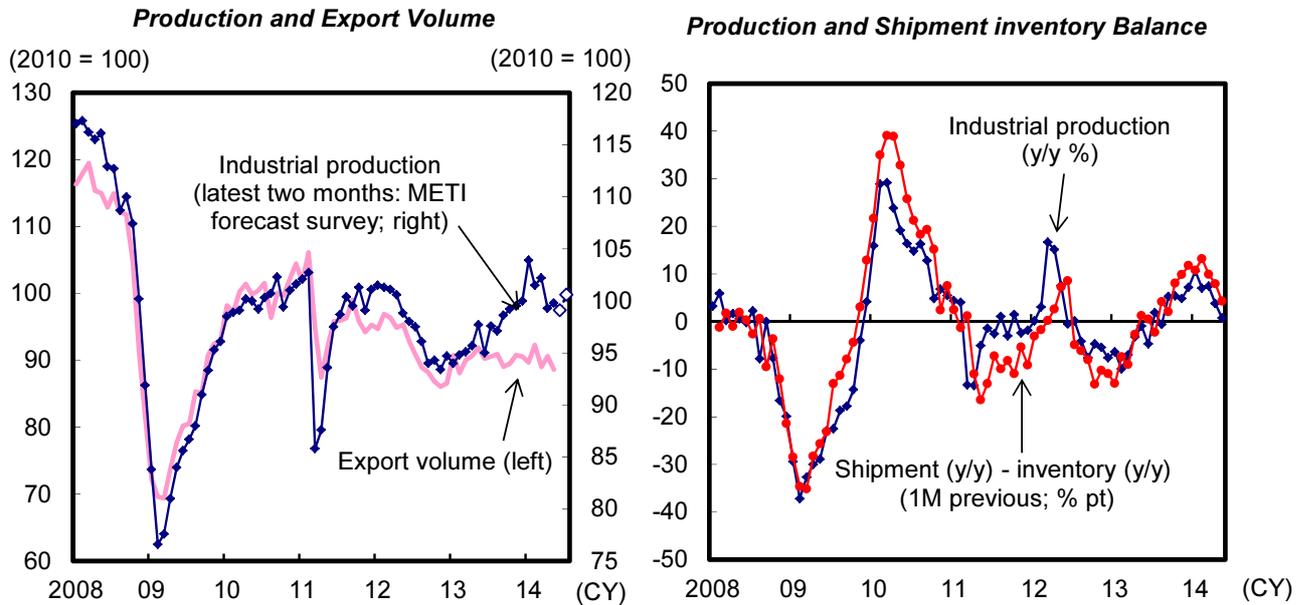
Source: Ministry of Economy, Trade, and Industry (METI); compiled by DIR.
F: METI's forecast survey.

Production Expected to Maintain Steady Undertone

As for the future, the downturn due mostly to a decline in personal consumption after the increase in the consumption tax in April is expected to be short-term, and production is expected to maintain a strong undertone. The reactionary decline in personal consumption is seen as having hit bottom in April and is expected to ease up with time. Factors bringing downward pressure on production are

expected to gradually recede. Meanwhile, increases in exports are expected to bring further support to industrial production in the future. The effect of the weakening yen, as well as economic expansion in overseas economies led by the US, are also expected to bring support for a future growth trend. Capex is already in a growth trend and is expected to expand further if exports continue to grow. Increasing production of domestic oriented investment goods is also expected to help drive industrial production in the future.

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



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