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September Industrial Production

Positive results exceed market consensus; hopes high for a comeback

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Summary

- The September 2014 indices of industrial production achieved growth for the first time in two months at +2.7% m/m, while at the same time exceeding market consensus (+2.2%) – all in all positive results. Although it is a bit early to declare that production has hit bottom, these results bring hope that industrial production will make a comeback in the near future. METI's production forecast survey sees the index reflecting a steady undertone in October and November.
- As for production by industry in September, thirteen out of the total of fifteen industries experienced growth. Fabricated metals remained flat in comparison to the previous month, and the only industry which reported declines was the chemical industry at -0.1% m/m. Besides the general strength of overall production, the extent of industries reporting growth was quite wide-ranging, and individual industry performance showed very positive results.
- According to METI's production forecast survey, a comeback is expected in industrial production after some initial ups and downs, with a slight decline seen in October (-0.1%) and growth of +1.0% expected in November. As for October production plans by industry, those industries which contributed to considerable growth in September (electronic components and devices, information & communications equipment, and the transport equipment industry) are expected to pull overall performance down. In November, general purpose, production & business oriented machinery is expected to see a decline in production, while all other industries are expected to see production increases.

Industrial Production (m/m %; SA basis)											Chart 1
	2013	2014									
	Dec	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep	
Industrial Production	0.5	3.9	-2.3	0.7	-2.8	0.7	-3.4	0.4	-1.9	2.7	
Market consensus (Bloomberg)										2.2	
DIR estimate										2.2	
Shipments	0.2	5.1	-1.0	-0.2	-5.0	-1.0	-1.9	0.7	-2.1	4.3	
Inventories	-0.2	-0.4	-0.9	1.4	-0.5	3.0	2.0	0.9	0.9	-0.8	
Inventory ratio	-0.2	-4.6	3.9	2.1	-1.6	4.0	3.4	-2.2	8.6	-5.7	

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

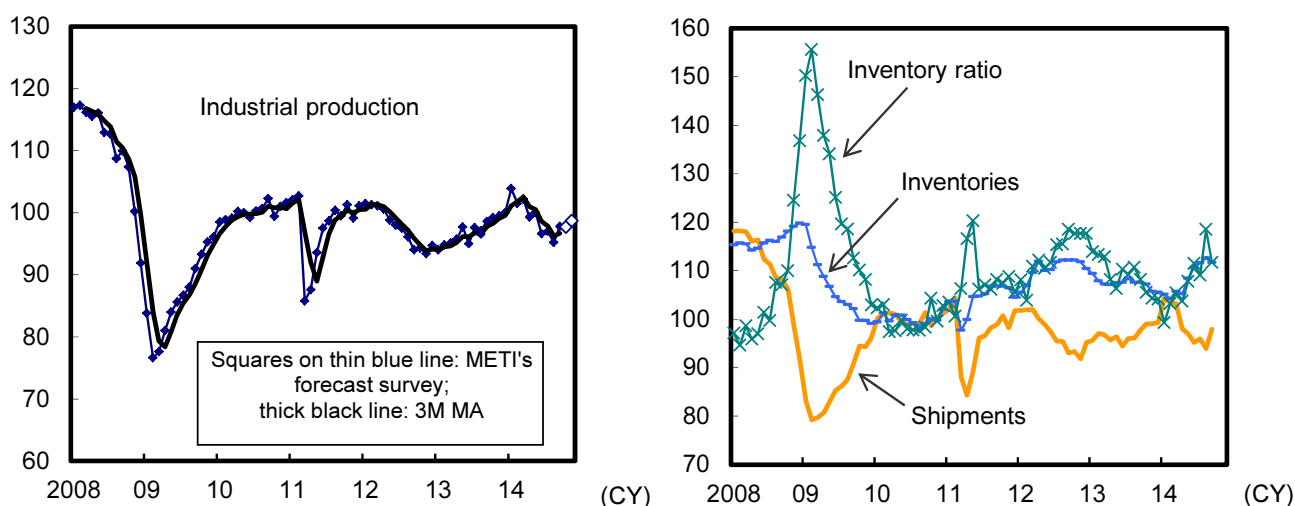
September 2014 industrial production exceeds market consensus

The September 2014 indices of industrial production achieved growth for the first time in two months at +2.7% m/m, while at the same time exceeding market consensus (+2.2%) – all in all positive results. Although it is a bit early to declare that production has hit bottom, these results bring hope that industrial production will make a comeback in the near future. METI's production forecast survey sees the index reflecting a steady undertone in October and November.

The shipment index grew for the first time in two months at +4.3% due mainly to shipments of durables, which were up by +7.7% m/m, the first time they achieved growth since January this year. Meanwhile, shipments of construction materials grew for the first time in six months at +1.5% m/m, in addition to capital goods (+2.8%) and production goods (+4.8%). The comeback in these areas contributed to the overall growth in production. Inventory and inventory ratio levels have been on the rise up to now, but September results show the inventory index to be down for the first time in five months at -0.8% m/m and the inventory ratio down for the first time in two months at -5.7% m/m. It may not be much, but we do see some progress in inventory adjustment.

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

Chart 2



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

Production grows in a broad range of industries

As for production by industry in September, thirteen out of the total of fifteen industries experienced growth. Fabricated metals remained flat in comparison to the previous month, and the only industry which reported declines was the chemical industry at -0.1% m/m. Besides the general strength of overall production, the extent of industries reporting growth was quite wide-ranging, and individual industry performance showed very positive results.

As for extent of contribution to overall production, the transport equipment industry (+4.7% m/m), electronic components and devices (+5.8%), the electrical machinery industry (+5.4%), and information & communications equipment (+12.4%) helped push overall performance up. Each of these industries had forecast growth in September on last month's production forecast survey, so performance was according to the original plan. However, the fact that actual performance did not fall below those aggressive plans for any of these industries is in itself a positive factor. (The production forecast survey realization rate for each of these industries was in other words on the plus side.) On the other hand, results for the general purpose, production & business oriented machinery industry have

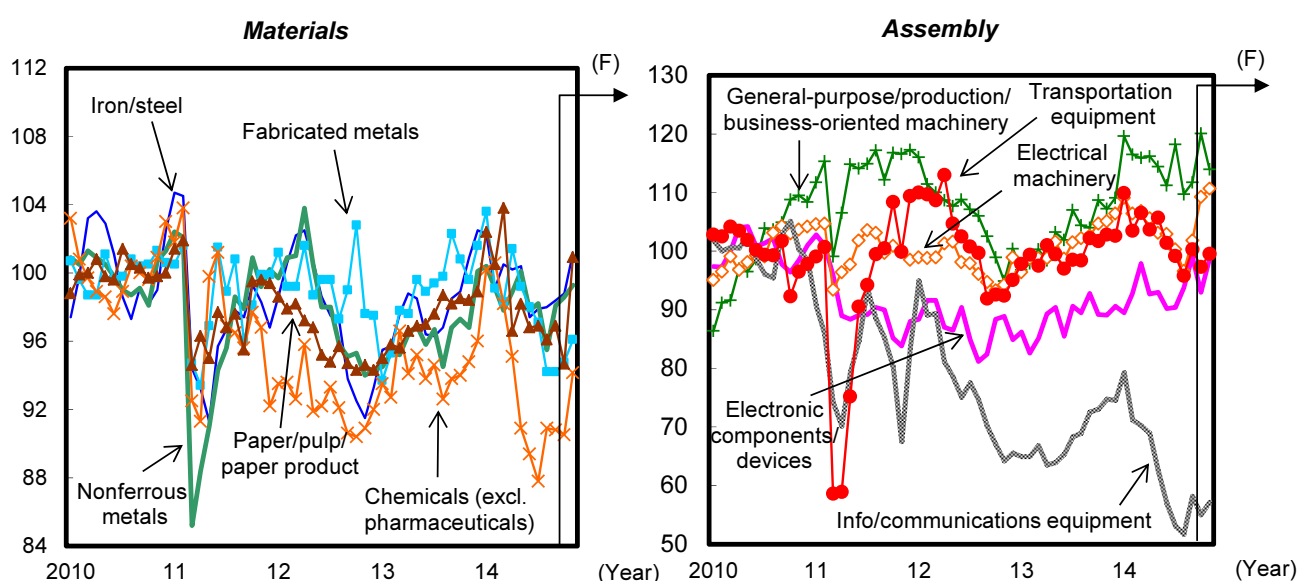
tended to fall below the production forecasts and the current month was no exception, with growth fairly limited at +1.8% m/m.

Production of transport equipment achieved growth for the first time in four months. Exports continue at a sluggish pace, while domestic auto sales grew causing a +3.6% m/m jump in shipments. It appears that the comeback in demand contributed to an increase in production.

In the area of electronic components & devices, active-matrix liquid-crystal display panels (both middle-size and small), which were in a downtrend in July and August, won major growth both in terms of shipments (+38.5% m/m) and production (+39.9%), thereby providing a major contribution to overall growth. Production in most industries developed a weak tone since the beginning of the year, but production in the electronic components & devices industry has maintained a growth trend.

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 forecast survey sees a comeback in the future

According to METI's production forecast survey, a comeback is expected in industrial production after some initial ups and downs, with a slight decline seen in October (-0.1%) and growth of +1.0% expected in November.

As for October production plans by industry, those industries which contributed to considerable growth in September (electronic components and devices, information & communications equipment, and the transport equipment industry) are expected to pull overall performance down. On the other hand, general purpose, production & business oriented machinery, which performed poorly in September, is expected to experience considerable growth, while in addition, the electrical machinery industry is expected to continue its production increases. Production was stopped temporarily at some factories producing transport equipment in October due to a typhoon with superstorm status, and this event is expected to bring production results down. Some of the effects of the typhoon can already be seen in the current month's results, but it should be noted that this will likely cause a downturn in results next month.

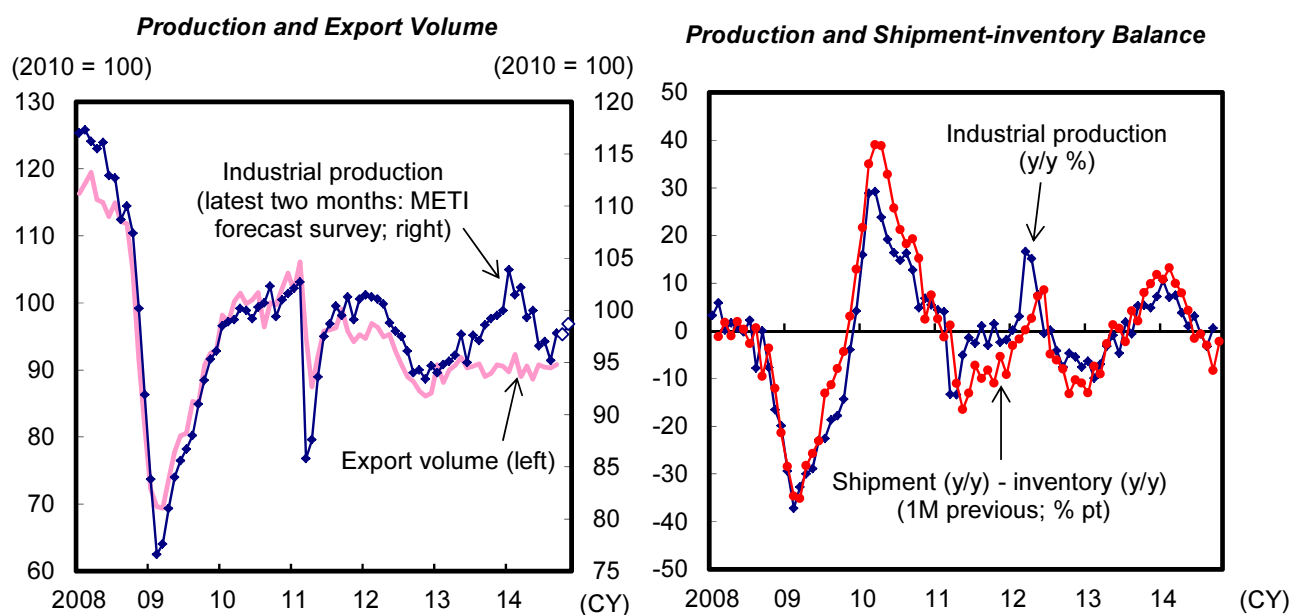
In November, general purpose, production & business oriented machinery, which expects major growth in October, is expected to see a decline in production, while all other industries are expected to see production increases. Many industries expect to see ups and downs in October, but chemicals and

paper & pulp are expected to experience major growth, while iron & steel, non-ferrous metals and fabricated metals expect to see their second consecutive month of growth. Meanwhile, the materials industry should be moving toward an unambiguous comeback.

Future to see comeback in production

As for the future, production is expected to move toward a comeback. The decline in personal consumption due to reactionary decline is expected to move closer to resolution, and factors bringing downward pressure on production are expected to recede. For the time being non-durable consumer goods, which have pretty much completed their recovery from the recent reactionary decline, and production of durables, which had been at a low for some time, are expected to experience a comeback as demand gradually recovers. Meanwhile, various capex surveys, such as the BOJ Tankan, have all issued positive stances toward the future of corporate capex, and an increase in capex related demand is expected to push up results centering on production of capital goods. Meanwhile, exports continue to mark time due to the economic slowdown in the EU and Asian emerging nations. However, overseas economies are expected to move toward recovery led by a robust US economy, which will gradually lead to a growth trend in Japanese exports. Inventory and inventory ratio levels remain on the high side, meaning that continued monitoring of factors which could bring downward pressure on production is required, but there is still a high possibility that production will move into a growth trend as both domestic and overseas demand head toward a comeback.

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



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