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February Industrial Production

Consensus in a downswing; future likely to see ups and downs

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Summary

- The February 2015 indices of industrial production fell for the first time in three months by -3.4% m/m, while falling below market consensus as well (-1.8%). A broad range of industries reported declines in production, making this report an overall negative one.
- Export volume, which is closely linked to production, experienced major growth in January associated with the Lunar New Year festivals in the Sinosphere. This made the February decline all the more steep, and likely influenced production performance. However, the three-month moving average grew for the sixth consecutive month by +0.3% m/m. Hence we are still of the opinion that industrial production is continuing its growth trend after hitting bottom in August 2014.
- According to METI's production forecast survey, industrial production is expected to decline again in March by -2.0% m/m, but then to bounce back in April 2015 at +3.6%. Production is expected to fall another notch in March, but a major comeback is expected in April, with modest growth seen despite some ups and downs.

Industrial Production (m/m %; SA basis)

Chart 1

	2014								2015	
	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb
Industrial Production	0.7	-3.4	0.4	-1.9	2.9	0.4	-0.5	0.8	3.7	-3.4
Market consensus (Bloomberg)										-1.8
DIR estimate										-1.3
Shipments	-1.0	-1.9	0.7	-2.1	4.4	0.6	-1.4	1.0	5.6	-3.4
Inventories	3.0	2.0	0.9	0.9	-0.7	-0.4	1.1	-0.7	-0.4	0.5
Inventory ratio	4.0	3.4	-2.2	8.6	-6.0	0.8	4.2	-4.3	-3.4	4.3

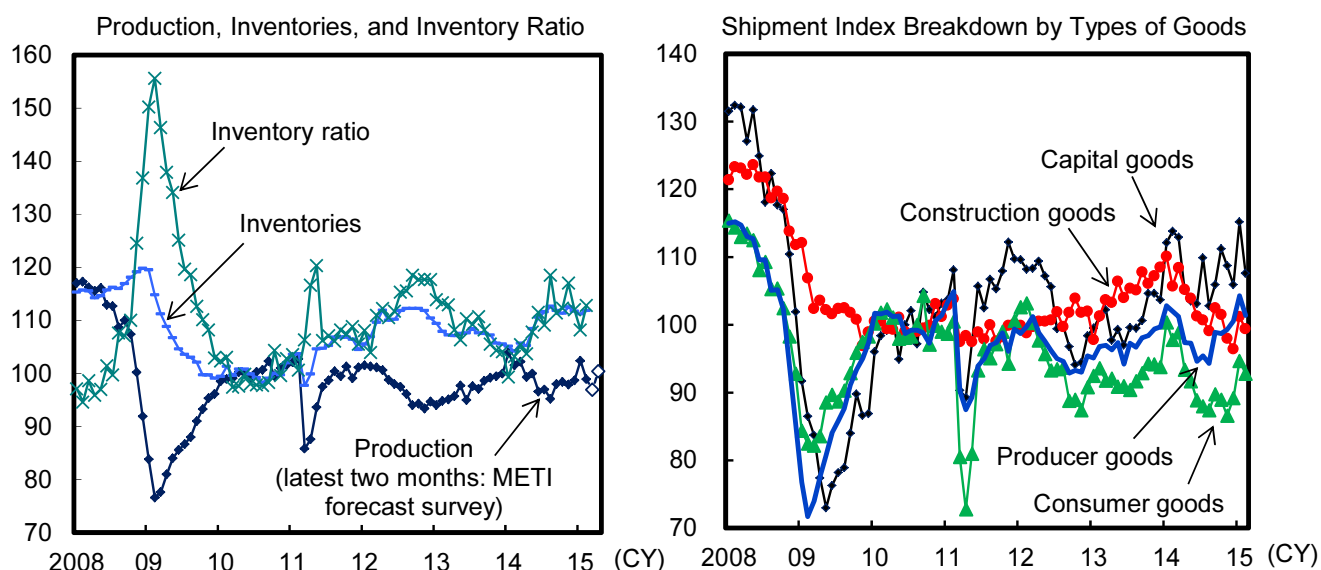
Source: Ministry of Economy, Trade, and Industry; Bloomberg; compiled by DIR.

February 2015 production index declines for first time in three months

The February 2015 indices of industrial production fell for the first time in three months by -3.4% m/m, while falling below market consensus as well (-1.8%). A broad range of industries reported declines in production, making this report an overall negative one. Export volume, which is closely linked to production, experienced major growth in January associated with the Lunar New Year festivals in the Sinosphere. This made the February decline all the more steep, and likely influenced production performance. However, the three-month moving average grew for the sixth consecutive month by +0.3% m/m. Hence we are still of the opinion that industrial production is continuing its growth trend after hitting bottom in August 2014.

The shipment index declined for the first time in three months at -3.4% m/m due mostly to declines suffered by capital goods (-6.6% m/m) which registered considerable growth during the previous month, and production goods (-2.8%). Meanwhile, the inventory index was up for the first time in three months by +0.5% m/m. As a result, the inventory ratio also grew for the first time in three months by +4.3% m/m.

Production, Inventories, Inventory Ratio, and Shipment Index Breakdown (2010 = 100; SA basis) Chart 2



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

Poor performance in general-purpose, production and business oriented machinery, transport equipment, and electronic parts and devices pushes down overall production

As for production index performance by industry in February, twelve out of the total of fifteen industries recorded declines. Contribution to overall decline was especially noticeable from general-purpose, production and business oriented machinery (-5.6% m/m), transport equipment (-3.6%), and electronic parts and devices (-7.4%), helping to push overall performance down.

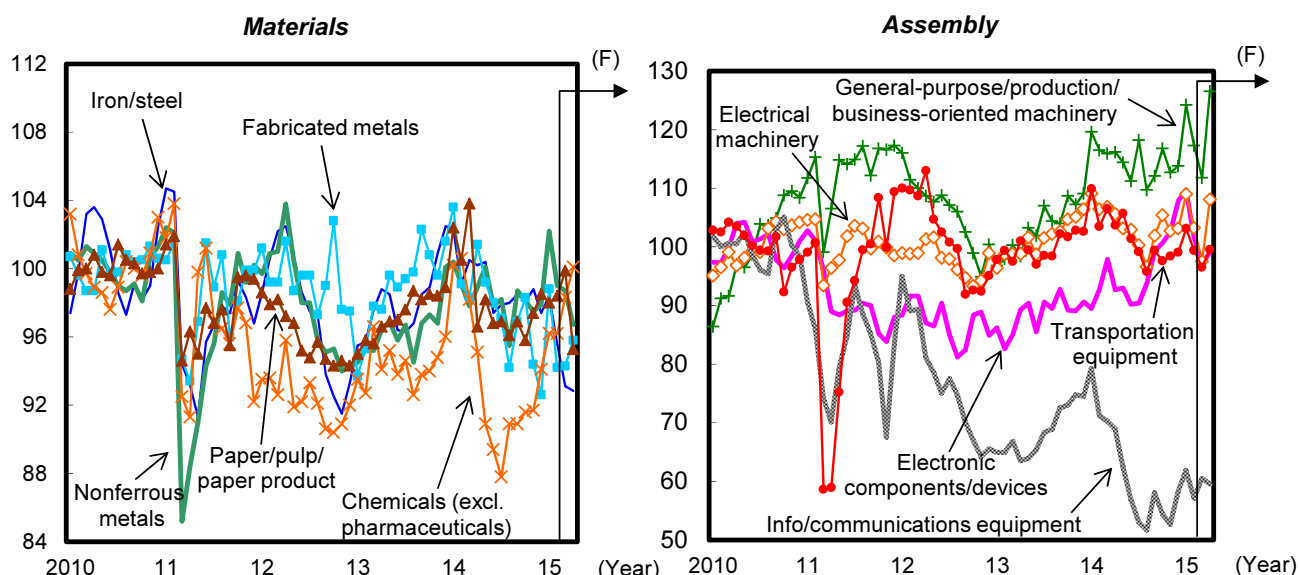
General-purpose, production and business oriented machinery, as well as transport equipment, were expected to experience a decline according to last month's production forecast survey, but the extent of the decline exceeded expectations. Meanwhile, electronic parts and devices suffered a major decline despite last month's prediction that production would be up, producing an especially negative tone. Most industries suffered declines, but the processing industries, which depend heavily on exports, experienced an especially steep fall in shipments and production in comparison to other industries.

Hence the decline in exports due to Lunar New Year celebrations in Asia is thought to have been a major factor in pushing down production.

On the other hand, areas that suffered declines in production during the previous month, such as petroleum and coal products (+1.8%) and pulp, paper, and paper products (+0.4% m/m) recorded growth.

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.

METI's production forecast survey sees ups and downs

According to METI's production forecast survey, industrial production is expected to decline again in March by -2.0% m/m, but then to bounce back in April 2015 at +3.6%. Production is expected to fall another notch in March, but a major comeback is expected in April, with modest growth seen despite some ups and downs. Most industries will see a decline in production in March, especially notable in the processing industries, including general-purpose, production and business oriented machinery (-4.7% m/m), electronic parts and devices (-4.4%), electrical machinery (-5.5%), and transport equipment (-2.9%). This is expected to push down production overall. However, April expects to see an all-around increase in production in the processing industries, most of which are expecting declines in March, with general-purpose, production and business oriented machinery expecting growth of +13.2% m/m, electronic parts and devices +2.0%, electrical machinery +10.8%, and transport equipment up +3.1%. Furthermore, this is expected to push up overall performance. In contrast, iron and steel, along with non-ferrous metals, is expected to see a continuation of the March declines in April as well, with both of these industries reporting measured production plans.

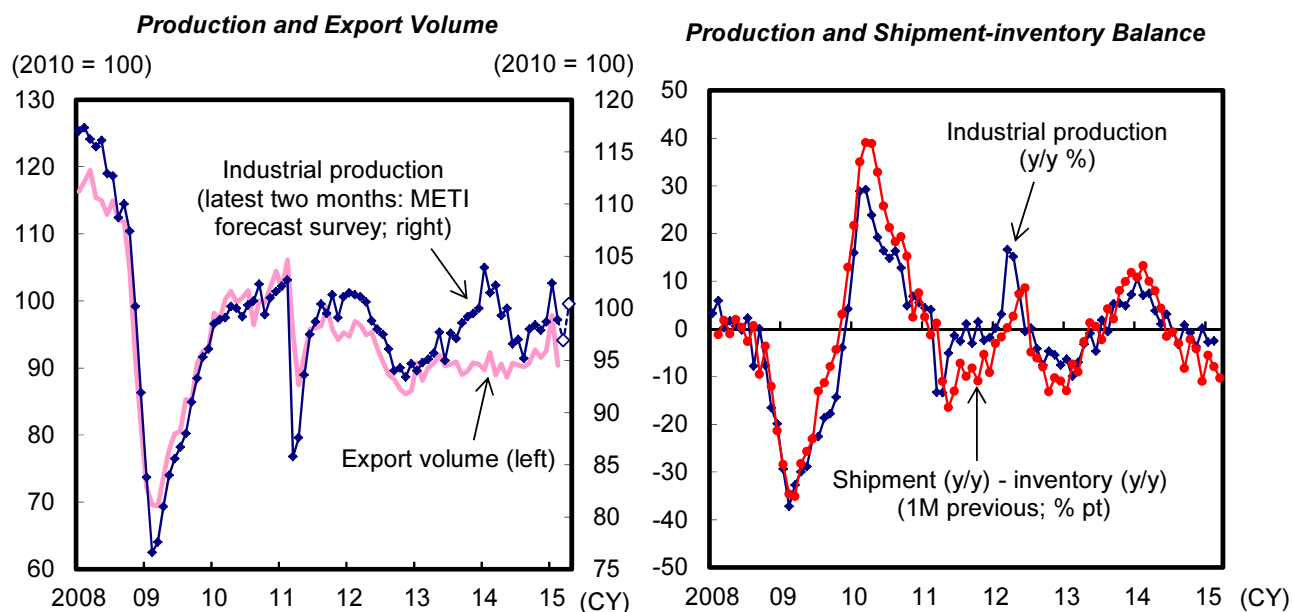
Production expected to continue growth trend in future

We here at DIR predict that production will continue in a growth trend in the future. Increase in export volume is expected to bring with it an increase in industrial production due to expanding overseas economies. The US continues its firm undertone as its economy expands, and the EU economy, which was suffering a continued slowdown recently, is now seeing the light at the end of the tunnel. Growth in production stemming from export growth is then expected to act along with improved corporate earnings in mustering demand associated with domestic capital expenditure, and the ripple effect promises to stimulate demand for capital goods. Meanwhile, the environment for household income is improving and the recent collapse in the price of crude oil promises to provide forward impetus for an

increase in real wages. Therefore demand for consumer goods is expected to continue making a comeback. Finally, with both domestic and overseas demand moving toward a comeback, production is expected to continue its current growth trend.

Production, Export Volume, and Shipment-inventory Balance

Chart 4



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