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February Industrial Production

Chances increase for negative growth in Jan-Mar 2016 period, but there are signs of improvement in the future

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Summary

- The February 2016 indices of industrial production was down by -6.2% m/m, suffering a decline for the first time in two months, while falling below market consensus at -5.9%. The shipment index was down considerably at -4.6% m/m. Meanwhile, inventories were down just slightly at -0.1%, with inventory ratio up by +0.5% m/m, for the first time in two months. Due to these results, the Jan-Mar period is likely to register negative growth, and may influence future fiscal policy. On the other hand, the METI forecast indicates that there are signs of gradual improvement in the future.
- Production is expected to return to a gradual growth trend in the future. First of all, domestic demand is expected to improve as consumption bottoms out reflecting improvement in real income for both working households and pensioners. Meanwhile, corporations have not lost their willingness to invest in domestic capex, and this should provide underlying support for demand in the area of capital goods. As for overseas demand, a gradual recovery is seen though there will be ups and downs. The US economy continues to expand helped along by the steady undertone in the household sector, and this is expected to bring continued growth in Japan's exports of durables. As for exports to the EU, the European economy is making a comeback thanks to the effects of falling crude oil prices and the ECB's quantitative monetary easing, and the recovery trend is expected to continue. Meanwhile, in regard to the Asian economy, China's real economy is showing signs of bottoming out due to the lowering of the ratio of cash reserves to deposits as well as interest rates, and it is very possible that further declines in demand can be avoided, centering on consumer goods.

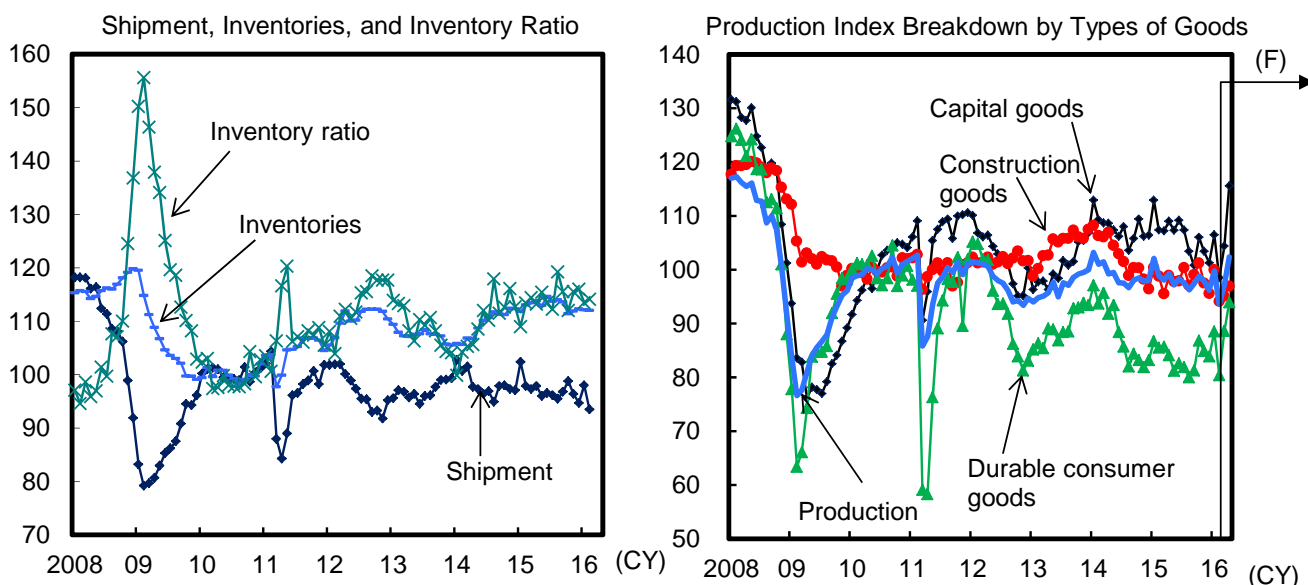
Industrial Production (m/m %; SA basis)										Chart 1	
	2015									2016	
	May	Jun	Jul	Aug	Sep	Oct	Nov	Dec	Jan	Feb	
Industrial Production	-2.1	1.1	-0.8	-1.2	1.1	1.4	-0.9	-1.7	3.7	-6.2	
Market consensus (Bloomberg)										-5.9	
DIR estimate										-6.3	
Shipments	-1.9	0.6	-0.4	-0.7	1.4	2.1	-2.4	-1.8	3.5	-4.6	
Inventories	-0.8	1.5	-0.8	0.3	-0.4	-1.9	0.4	0.4	-0.2	-0.1	
Inventory ratio	1.9	-1.6	-1.1	6.2	-3.1	-3.0	3.1	0.4	-2.2	0.5	

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

Major declines in production increase possibility of negative growth in Jan-Mar period

The February 2016 indices of industrial production was down by -6.2% m/m, suffering a decline for the first time in two months, while falling below market consensus at -5.9%. The shipment index was down considerably at -4.6% m/m. Meanwhile, inventories were down just slightly at -0.1%, with inventory ratio up by +0.5% m/m, for the first time in two months. Due to these results, the Jan-Mar period is likely to register negative growth, and may influence future fiscal policy. On the other hand, the METI forecast indicates that there are signs of gradual improvement in the future.

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



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

Reactionary decline after last year's production in advance and Chinese Lunar New Year brings major declines in production of durable consumer goods and capital goods

As for production index performance by industry in February, thirteen out of the total of fifteen industries recorded production declines. Sectors which recorded major growth in January suffered notable reactionary declines due partly to the effects of the Lunar New Year holiday in Asia. These included transport equipment (-10.2% m/m), electronic parts & devices (-14.7%), general-purpose, production and business oriented machinery (-7.3%), electrical machinery (-6.0%), and fabricated metals (-9.5%). Transport equipment and electronic parts & devices suffered not only from the reactionary decline following the production in advance carried out at the end of last year, but further declines suffered throughout the Jan-Mar period.

Looking at February production index performance by types of goods, we see that production declines were considerable in areas which gained major growth in January, including durable consumer goods (-9.2%), capital goods (-7.5%), and construction goods (-5.9%). Other areas experienced moderate growth, including non-durable consumer goods (+0.7%) and production goods (+2.0%). Durable consumer goods and capital goods have recorded fairly large declines throughout January and February.

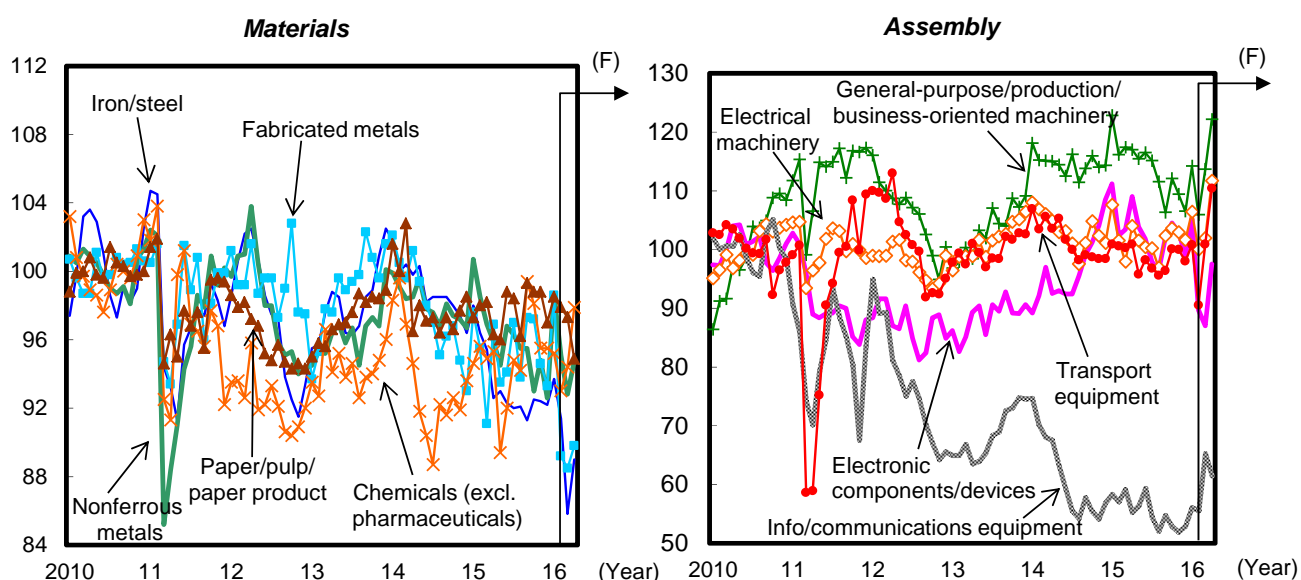
Growth trend for production seen in future

As can be seen in METI's production forecast survey, production is expected to return to a growth trend in the future, the production index in March and April 2016 expecting +3.9% m/m and +5.3% m/m respectively. Looking at the METI forecast by industry, we see the processing industry, which is especially susceptible to economic ups and downs, recording major growth in production. This includes transport equipment (+11.5% in March and +9.4% in April), general-purpose, production and business oriented machinery (+7.3% in March and +7.5% in April), information communication & electronics equipment (+17.5% in March and -5.8% in April), electrical machinery (+1.9% in March and +9.6% in April), and electronic parts & devices (-3.0% in March and +12.1% in April).

Looking at the forecast survey by types of goods, we see strong performance for production of capital goods (minus transport equipment) (+6.0% m/m in March and +10.7% in April) and durable consumer goods (+10.2% in March and +6.0% in April), while performance in other areas is expected to be somewhat weak, including non-durables (-4.4% in March and +0.5% in April) and construction goods (+1.0% in March and +2.0% in April).

Production by Industry (2010 = 100; SA basis)

Chart 3

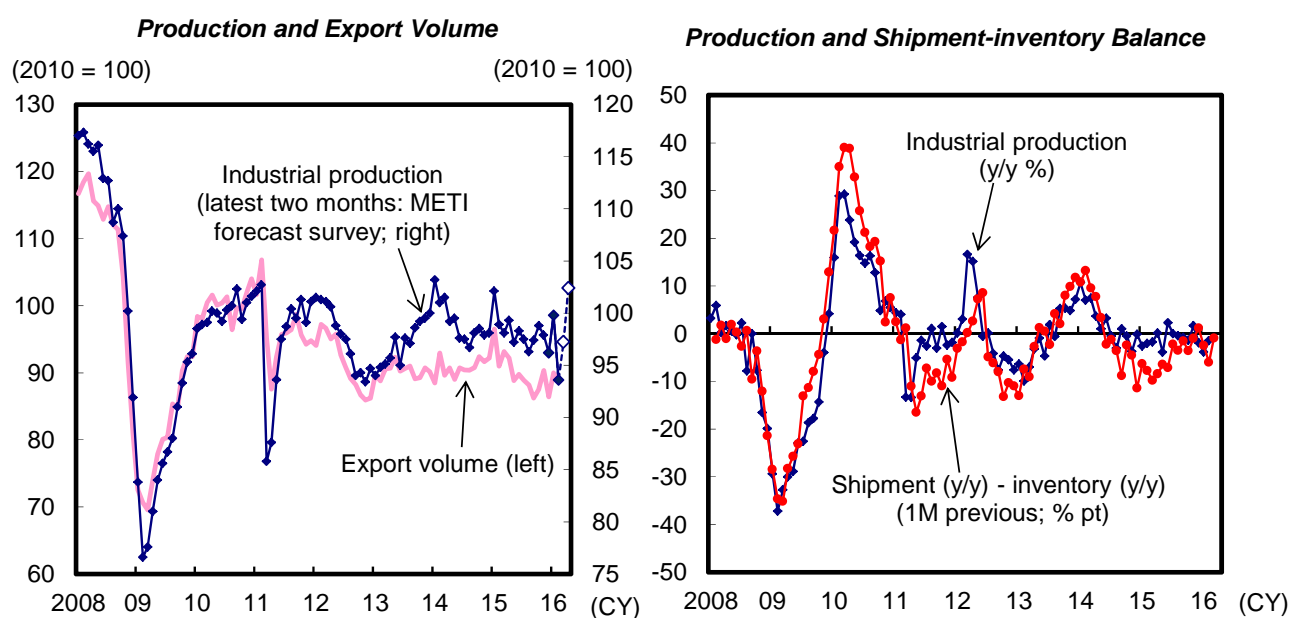


Source: Ministry of Economy, Trade, and Industry (METI); compiled by DIR.
F: METI's forecast survey.

Signs of shaking lull in production

As is indicated in this month's METI forecast, production is expected to return to a gradual growth trend. First of all, domestic demand is expected to improve as consumption bottoms out reflecting improvement in real income for both working households and pensioners. Meanwhile, corporations have not lost their willingness to invest in domestic capex, and this should provide underlying support for demand in the area of capital goods. As for overseas demand, a gradual recovery is seen though there will be ups and downs. The US economy continues to expand helped along by the steady undertone in the household sector, and this is expected to bring continued growth in Japan's exports of durables. As for exports to the EU, the European economy is making a comeback thanks to the effects of falling crude oil prices and the ECB's quantitative monetary easing, and the recovery trend is expected to continue. Meanwhile, in regard to the Asian economy, China's real economy is showing signs of bottoming out due to the lowering of the ratio of cash reserves to deposits as well as interest rates, and it is very possible that further declines in demand can be avoided, centering on consumer goods.

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



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