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# June Industrial Production

Production grows for first time in two months; future production plans show strength

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## Summary

- The June 2016 indices of industrial production grew for the first time in two months by +1.9% m/m. Rebound from the previous month's major decline is a large part of positive results, but considering strength in comparison to market consensus (+0.5%) results are considered to be extremely good. Meanwhile, the METI production forecast survey sees growth continuing in July (+2.4%) and August (+2.3%). Even if we ignore the strength of production plans in areas which are often revised downwards at a later date, such as general-purpose, production and business related machinery and information communication & electronics equipment, we can conclude that growth in production will continue to a certain extent in the future. This is encouraged by the especially strong production plans of the electronic parts and devices industry where exports of ICs are in a growth trend.
- Production is expected to experience ups and downs in the future. Personal consumption is expected to mark time due to sluggish growth in disposable income for working families and household income for pensioners. In addition, the earnings environment for corporations is worsening due to the progressively strong yen, and this will very likely narrow the focus of domestic capex to labor-saving as a means of handling the shortage in manpower, research and development, and energy-saving. As for overseas demand, though some goods are expected to maintain a firm undertone, overall demand is expected to mark time.

Industrial Production (m/m %; SA basis)										Chart 1
	2015				2016					
	Sep	Oct	Nov	Dec	Jan	Feb	Mar	Apr	May	Jun
Industrial Production	0.3	1.2	-1.1	-1.2	2.5	-5.2	3.8	0.5	-2.6	<b>1.9</b>
Market consensus (Bloomberg)										0.5
DIR estimate										0.2
Shipments	-0.3	2.6	-2.4	-1.4	2.0	-4.1	1.8	1.6	-2.6	<b>1.2</b>
Inventories	-0.1	-1.2	0.4	0.4	-0.3	-0.2	2.9	-1.7	0.4	<b>0.0</b>
Inventory ratio	-1.0	-1.8	2.2	0.7	-0.1	-1.5	3.3	-2.2	1.8	<b>-1.4</b>

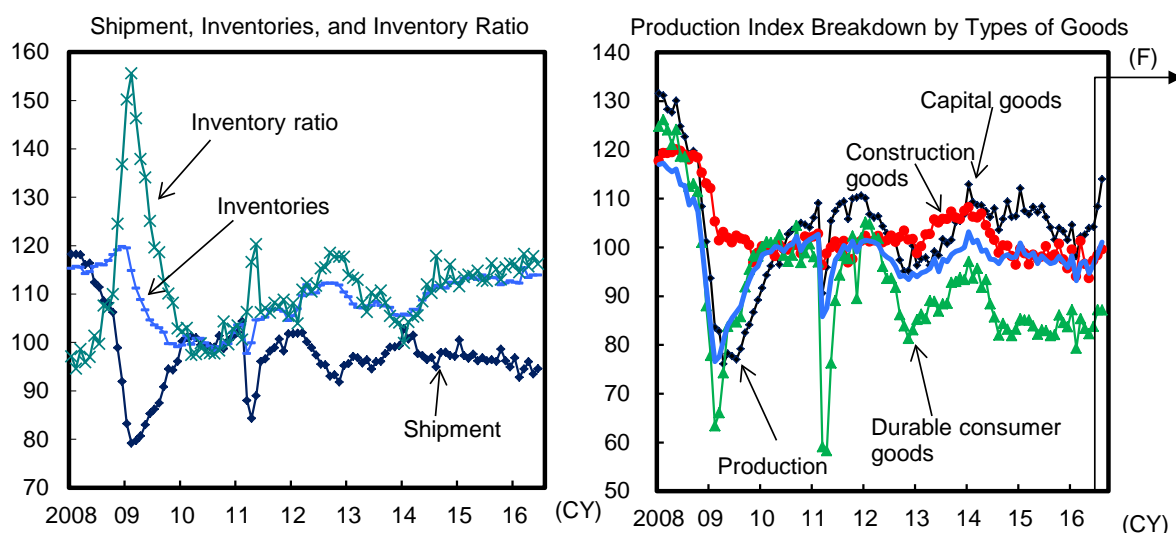
Source: Ministry of Economy, Trade, and Industry; Bloomberg; compiled by DIR.

## Production grows for first time in two months; future production plans show strength

The June 2016 indices of industrial production grew for the first time in two months by +1.9% m/m. Rebound from the previous month's major decline is a large part of positive results, but considering strength in comparison to market consensus (+0.5%) results are considered to be extremely good. Meanwhile, the METI production forecast survey sees growth continuing in July (+2.4%) and August (+2.3%). Even if we ignore the strength of production plans in areas which are often revised downwards at a later date, such as general-purpose, production and business related machinery and information communication & electronics equipment, we can conclude that growth in production will continue to a certain extent in the future. This is encouraged by the especially strong production plans of the electronic parts and devices industry where exports of ICs are in a growth trend.

The shipment index in June also grew for the first time in two months by +1.2% m/m, while the inventory index marked time at +0.0%. The inventory ratio declined for the first time in two months by -1.4%. Strong results were seen for production in June and production plans in July and August, but the level of inventory remains high, and we must remain aware of the possibility that production could weaken at some point in the future due to inventory adjustment.

**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.

## Materials, which declined during the previous month, and industries recording favorable exports show strength. Capex related production remains weak.

As for production index performance by industry in June, thirteen out of the total of fifteen industries recorded production growth. A rebound was seen in the materials industries in response to the previous month's declines, with chemicals (minus pharmaceuticals) at +4.0% m/m and fabricated metals at +5.0%. Meanwhile, industries showing a firm undertone during the previous month showed strength in June, including transport equipment (+1.6% m/m) and electronic parts and devices (+1.6%).

Looking at June production index performance by types of goods, we see production growth in a broad range of areas, including production goods (+1.9%), durable consumer goods (+1.8%), and non-durable consumer goods (+1.2%). Capital goods also gained though just slightly at +0.2%. Meanwhile, considering the fact that general-purpose, production and business related machinery was on the weak side, capex related production is also expected to continue in a weak tone.

## Production plans robust in July and August

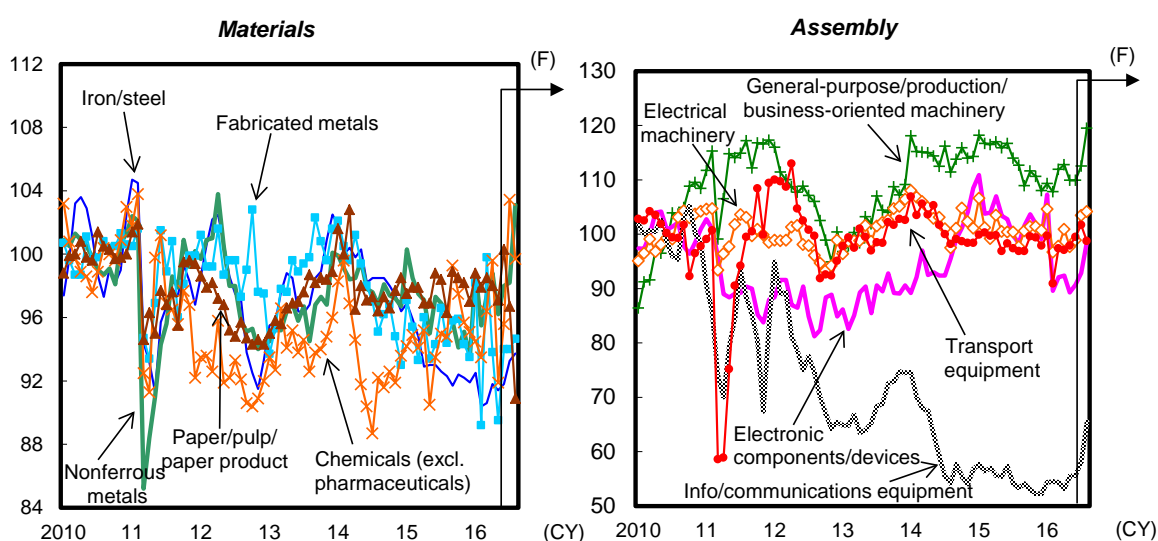
The METI production forecast survey sees both July and August registering month-to-month growth of +2.4% and +2.3% respectively. Even after adjustments are made for prediction errors, growth of +0.9% m/m is seen in July. And even considering that a downward revision could occur based on past trends, these are still strong numbers.

Looking at the METI forecast by industry, we see confidence in future production plans for information communication & electronics equipment (+4.5% in July and 12.6% in August), and general-purpose, production and business related machinery (+2.4% in July and +6.2% in August). However, these industries tend to have realization rates deeply in the negative numbers, and hence these figures should be taken with a certain grain of salt. On the other hand, favorable production plans are also seen for electronic parts and devices (+0.7% in July and +6.9% in August), and electrical machinery (+4.6% in July and +0.7% in August), which may very well lead overall industrial production toward further growth. Transport equipment is seen continuing to experience ups and downs (+2.2% in July and -2.9% in August).

Looking at the METI forecast by types of goods, production plans show strength in capital goods (+4.0% in June and +5.2% in July), and production goods in the area of mining and manufacturing (+1.7% in June and +2.5% in July).

Production by Industry (2010 = 100; SA basis)

Chart 3



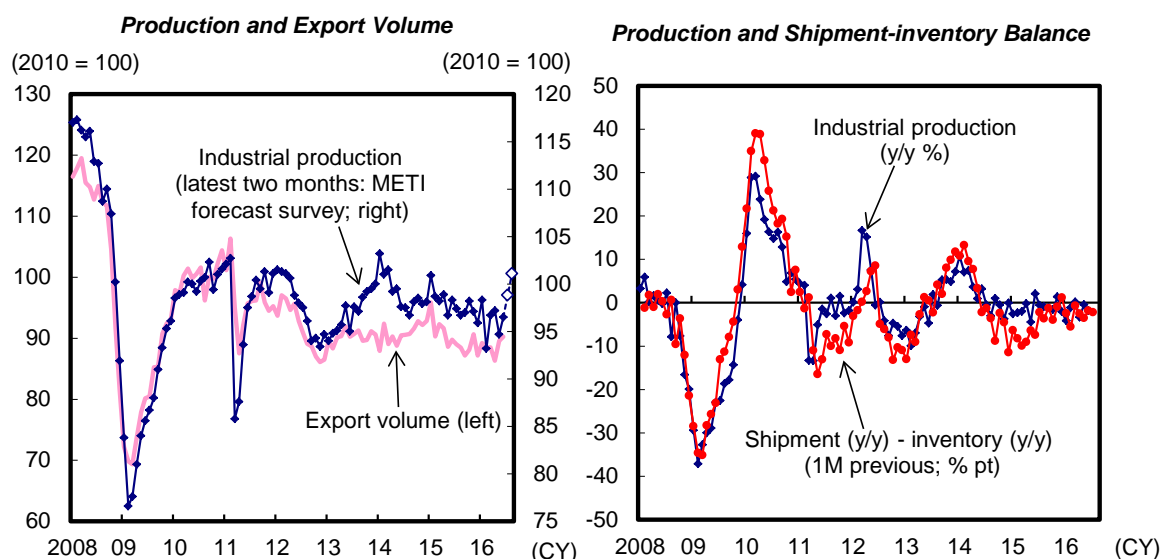
Source: Ministry of Economy, Trade, and Industry (METI); compiled by DIR.  
F: METI's forecast survey.

## Ups and downs seen in future

Production is expected to experience ups and downs in the future. Personal consumption is expected to mark time due to sluggish growth in disposable income for working families and household income for pensioners. In addition, the earnings environment for corporations is worsening due to the progressively strong yen, and this will very likely narrow the focus of domestic capex to labor-saving as a means of handling the shortage in manpower, research and development, and energy-saving. As for overseas demand, though some goods are expected to maintain a firm undertone, overall demand is expected to mark time. As for exports to Europe, the collapse in the price of oil and quantitative easing implemented by the ECB had been encouraging a comeback until now, but the recent decision of the UK to withdraw from the EU could cause the economy to weaken. The US economy continues to show a steady undertone especially in the household sector, but this does not mean that exports of capital goods will increase. Meanwhile, in regard to the Asian economy, fears associated with the tightening of US monetary policy are on the wane, and the negative influence of capital outflows in association with this factor are gradually abating. However, caution is required regarding the possibility that demand could decline further due to turmoil in the financial markets stemming from the situation in the EU.

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

**Chart 4**



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