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# September Industrial Production

**Capital goods to win major growth in October; effects of halt in automobile production are limited**

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## Summary

- The September indices of industrial production recorded a decline of -1.1% m/m. The METI production forecast survey sees October performance up by +4.7% m/m, and November down by -0.9%.
- Though industrial production declined in September, it is expected to return to positive performance in October due mostly to performance of capital goods. The growth trend is expected to be maintained in the future. Performance of capital goods is especially notable, with general-purpose, production and business oriented machinery centering on exports of semiconductor manufacturing equipment especially favorable. On the other hand, one automobile manufacturer halted production and shipments at its domestic factories, hence declines in production of transport equipment will be a negative factor bringing down overall performance in the short-term. However, the effects are expected to be limited.
- Production is expected to experience moderate growth in December 2017 and beyond. As for capital goods, exports are expected to lead the economy and expand centering on semiconductor manufacturing equipment due to the recovery in the global economy. However, caution is required regarding overseas demand due to possible downside risk. If US interest rates undergo a rapid rise in association with the Fed's exit strategy, this could bring downward pressure on the US economy, while at the same time encouraging capital outflows from the emerging nations.

**Industrial Production (m/m %; SA basis)**

**Chart 1**

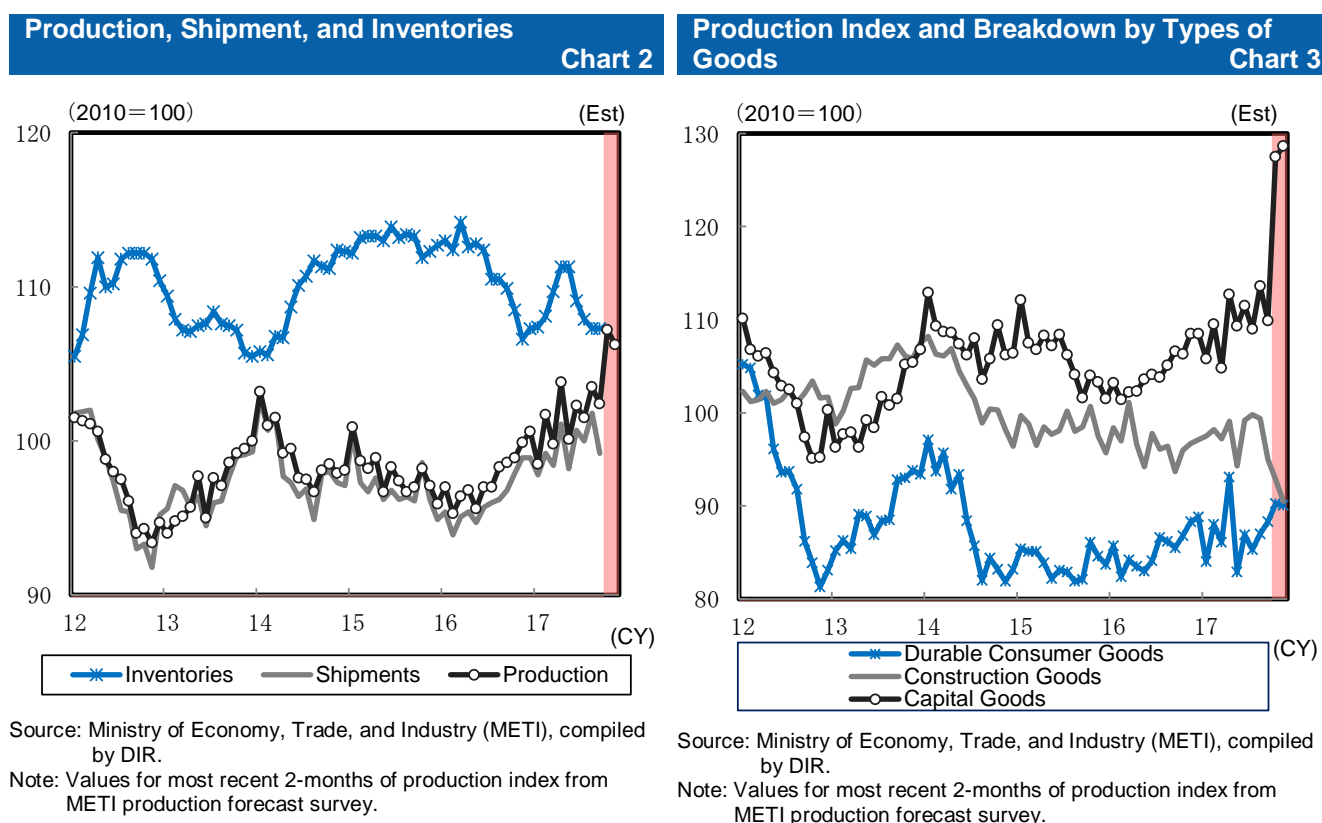
	2016		2017							
	Dec	Jan	Feb	Mar	Apr	May	Jun	Jul	Aug	Sep
Industrial Production	0.7	-2.1	3.2	-1.9	4.0	-3.6	2.2	-0.8	2.0	<b>-1.1</b>
Market consensus (Bloomberg)										-1.6
DIR estimate										-1.0
Shipments	0.0	-1.1	1.4	-0.8	2.7	-2.9	2.5	-0.7	1.8	<b>-2.6</b>
Inventories	0.7	0.1	0.7	1.5	1.5	0.0	-2.0	-1.1	-0.6	<b>0.0</b>
Inventory ratio	0.8	2.5	-0.3	0.2	2.9	-1.9	-1.9	2.6	-4.1	<b>1.6</b>

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

## September production down, but growth in production seen in October

The September indices of industrial production recorded a decline of -1.1% m/m. The METI production forecast survey sees October performance up by +4.7% m/m, and November down by -0.9%.

Though industrial production declined in September, it is expected to return to positive performance in October due mostly to performance of capital goods. The growth trend is expected to be maintained in the future. Performance of capital goods is especially notable, with general-purpose, production and business oriented machinery centering on exports of semiconductor manufacturing equipment especially favorable. On the other hand, one automobile manufacturer halted production and shipments at its domestic factories, hence declines in production of transport equipment will be a negative factor bringing down overall performance in the short-term. However, the effects are expected to be limited.



## Nine out of fifteen industries suffer declines

As for production index performance by industry in September, nine out of the total of fifteen industries suffered declines. Of these, contribution to decline was especially notable for electronic parts and devices (-5.6% m/m), and general-purpose, production and business oriented machinery (-2.4%).

Overall performance was brought down by electronic parts and devices, but production remains at a high level while inventory is low. Meanwhile, as for general-purpose, production and business oriented machinery, production of manufacturing equipment for flat panel displays declined, but not only do production levels remain high, inventories are maintaining a declining trend. Considering the above, this month's results for these industries needn't be viewed in an overly pessimistic manner.

Meanwhile, in fabricated metals, products such as bridges and steel frames also contributed to the decline. In addition to architectural and construction materials, excavators and cranes in general-

purpose, production and business oriented machinery also suffered declines this month. Behind the weakness experienced by construction and construction related materials is most likely a decline in both housing construction and public works projects.

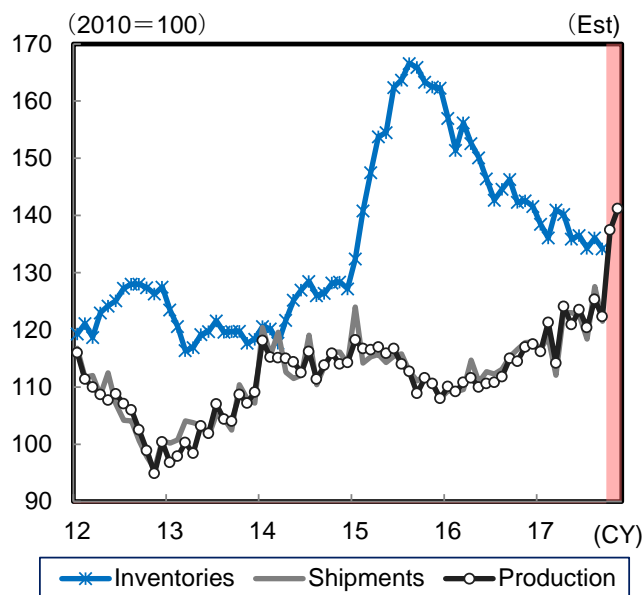
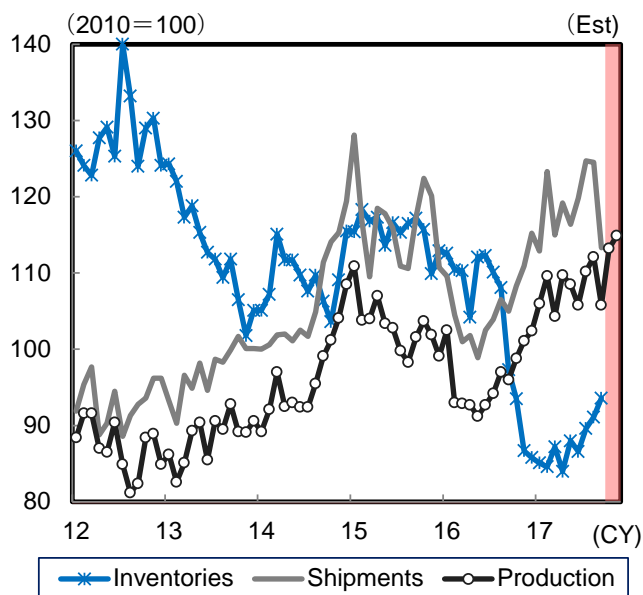
On the other hand, industries reporting growth in production totaled five industries, including chemicals (excluding drugs) at +7.6%. In this industry, production of cosmetics was favorable as a result of brisk consumption on the part of inbound tourists.

### General-purpose, production and business oriented machinery to register especially strong performance in October

The METI production forecast survey sees October performance up by +4.7% m/m, and November performance down by -0.9%. Meanwhile, METI’s estimated forecast value for the October Indices of Industrial Production indicates growth of +2.4% (mode value).

Looking at the production forecast survey by industry, we see that production plans for general-purpose, production and business oriented machinery (+12.4% m/m in October and +2.7% in November), which contributed to decline this month, are expected to be especially strong, along with electronic parts and devices (+7.0% in October and +1.5% in November). As for general-purpose, production and business oriented machinery, exports are favorable centering on semiconductor manufacturing equipment due to the recovery in the global economy. Meanwhile, electronic parts and devices are expected to see favorable demand for parts used in new model smartphones. With orders seen favorable in the future, these industries are expected to maintain a firm tone. However, these industries tend to experience downturns in production after initial plans have been announced; hence figures should be taken with a certain grain of salt.

**Production, Shipments, and Inventory (Left: Electronic Parts & Devices, Right: General-Purpose, Production and Business Oriented Machinery) Chart 4**



Source: Ministry of Economy, Trade, and Industry (METI), compiled by DIR.  
 Note: Values for most recent 2-months of production index from METI production forecast survey.

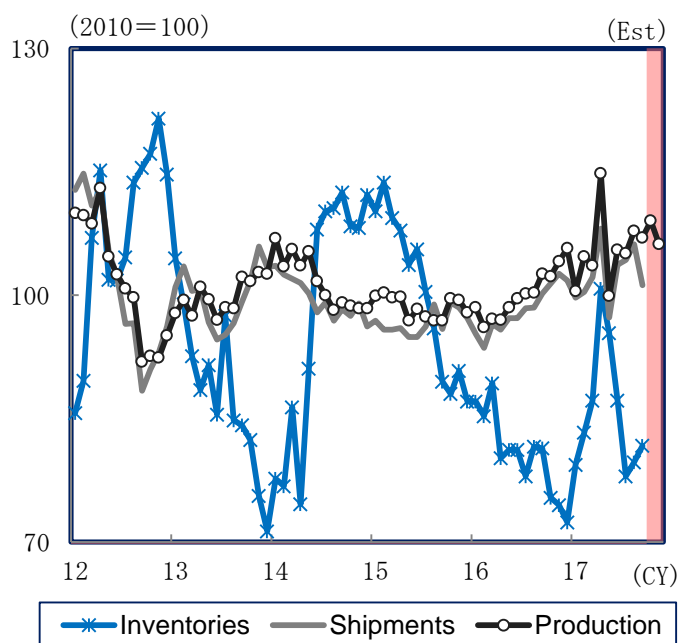
Source: Ministry of Economy, Trade, and Industry (METI), compiled by DIR.  
 Note: Values for most recent 2-months of production index from METI production forecast survey.

## Effects of halt in automobile production are limited

According to the METI production forecast survey, transport equipment up in October by +1.9% m/m and down in November at -2.6%. We have not included the effects of one automobile manufacturer halting production and shipments at its domestic factories in these calculations. The production forecast survey is carried out on the last day of each month and submitted by the 10<sup>th</sup> of the following month (the submission date for the October survey is Oct. 10). The manufacturer mentioned here reported that it was not prepared for an inspection on September 29. The halt of domestic production and shipments of automobiles was not announced until October 19.

According to the previous fiscal year's business performance, the proportion of overall domestic production of four-wheelers accounted for by this manufacturer's domestic production volume of automobiles (domestic automobile production volume – automobile production export volume) is 4.4%. If we calculate based on the production weight of this share in industrial production (proportion of overall industrial production accounted for by four-wheelers including passenger vehicles, buses, and trucks totals 9.1%, and the proportion of transport equipment industry production accounted for by four-wheelers (passenger vehicles, buses, and trucks) totals 47.8%), then if this manufacturer halts its domestic production of automobiles for a period of two weeks, it is expected to have a negative impact on the production index of the transport equipment industry of 1.0%pt, and a negative impact on the overall industrial production indices of 0.2%pt. Considering the possibility of a ripple effect hitting the automobile parts industry and other industries, this phenomenon is thought to have a potentially huge effect, but as long as other industries do not have a direct connection to declines in new car sales, the effect of pushing down overall industrial production will likely be only temporary.

**Production, Shipments, and Inventory (Transport Equipment)**  
Chart 5

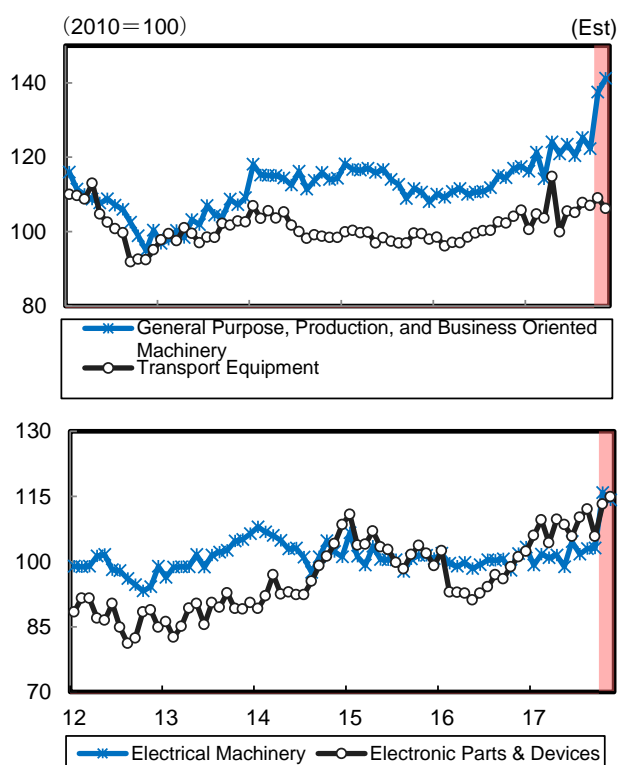


Source: Ministry of Economy, Trade and Industry; compiled by DIR.

Note: Figures for most recent two months of the production index are from the METI production forecast survey.

## Production Indices (Assembly)

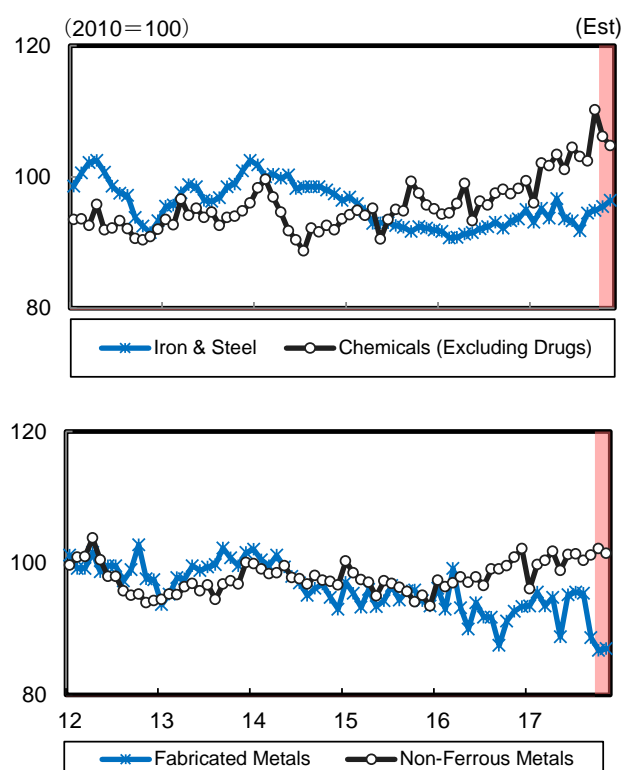
Chart 6



Source: Ministry of Economy, Trade and Industry; compiled by DIR.  
 Notes: 1) Figures for most recent two months of the production index are from the METI production forecast survey.  
 2) The Other Products category on the METI production forecast survey includes ceramics, stone and clay products, petroleum and coal products, and textile products.

## Production Indices (Materials)

Chart 7



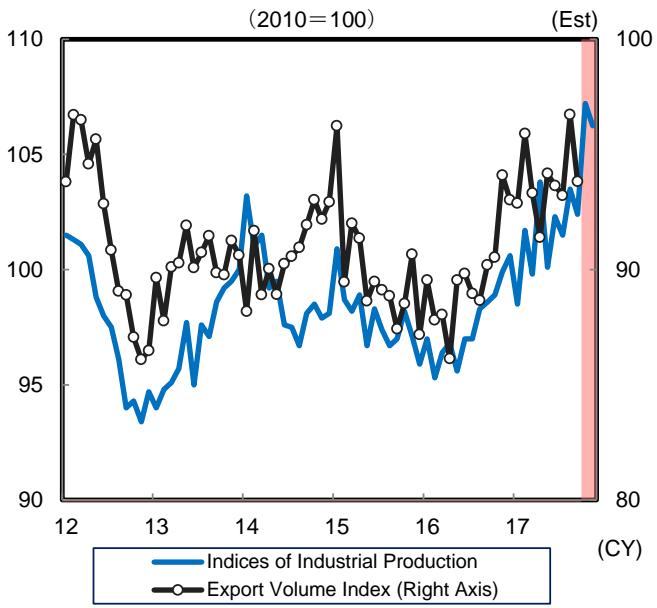
Source: Ministry of Economy, Trade and Industry; compiled by DIR.  
 Notes: 1) Figures for most recent two months of the production index are from the METI production forecast survey.  
 2) The Other Products category on the METI production forecast survey includes ceramics, stone and clay products, petroleum and coal products, and textile products.

## Moderate growth in production seen in future

Production is expected to experience moderate growth in December 2017 and beyond. As for capital goods, exports are expected to lead the economy and expand centering on semiconductor manufacturing equipment due to the recovery in the global economy. As for the domestic scene, capex spending in the area of maintenance & repair remains promising throughout FY2017, but caution is required as it is unknown whether the growth trend in operating rate can be maintained.

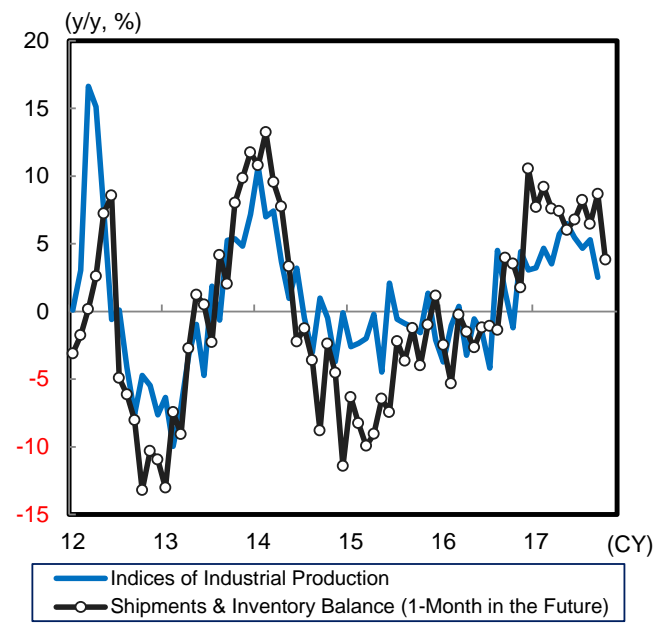
However, caution is required regarding overseas demand due to possible downside risk. If US interest rates undergo a rapid rise in association with the Fed's exit strategy, this could bring downward pressure on the US economy, while at the same time encouraging capital outflows from the emerging nations. Meanwhile, the ECB has decided to begin reducing its quantitative easing activities in January 2018, hence we advise caution regarding the possibility that this could bring downward pressure on the EU economy. While our main scenario sees a continuation of moderate growth for the global economy, if uncertainty regarding the future grows, it could lead to a slowdown in exports and risks bringing downward pressure on the Japanese economy.

**Industrial Production & Export Volume**  
Chart 8



Source: Ministry of Economy, Trade, and Industry (METI), compiled by DIR.  
Note: Values for most recent 2-months of production index from METI production forecast survey.

**Shipments, Inventory Balance & Production**  
Chart 9



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