

【Fundamentals Navigator】

Japan industrial production August 2020: Third straight rise, forecast also solid

(original Japanese report issued on September 30, 2020)

Capital goods growth outlook should be discounted, but transport machinery to continue upward

Industrial production grew 1.7% MoM in August for a third successive rise. Continued weakness in capital goods contrasted with robust growth in transportation equipment, steel and electronic parts & devices. The forecast index calls for further gains of 5.7% in September (forward estimate: +2.8%) and 2.9% in October. An increase in September in line with the forward estimate would bring production up 8.8% QoQ for 3Q 2020 (2Q: -16.9%). We are wary of expectations of a dramatic comeback in capital goods, but we do expect transportation machinery growth to come in near the forecast. Electronic parts & devices could experience rush demand and a consequent backlash in connection with US-Chinese trade frictions, but the outlook on average remains steady.

(1) Overview: Industrial production grew 1.7% MoM (preliminary estimate) in August for a third successive rise (July: +8.7%), outperforming market expectations. The production index in August came to 88.7 (2015 average = 100). The July index reading of 87.2 exceeded April's 86.4, but remains some way from March's 95.8.

(2) Production by industry: The biggest boost came again from transportation machinery, whose 8.6% MoM rise (July +30.3%, June +24.1%) lifted production by 1.42 percentage points (ppt). Automobiles were up 8.9% (July: +38.4%) amid the ongoing recovery in passenger cars and trucks. Production materials also remained healthy, with steel up 8.1% (+11.1%, contribution +0.27ppt) and electronic parts & devices up 4.6% (+4.6%, +0.29ppt). At the same time, capital goods trended weak overall. Production machinery was down 9.8% (-4.6%, -0.71ppt), continuing the previous month's slide due to a drop in volatile semiconductor and FPD production equipment.

(3) Shipments, inventory, inventory ratio: Shipments outpaced production with a 2.1% MoM rise (July: +6.6%). Passenger cars and air conditioners fueled a further 5.6% rise in durable goods (+24.7%), and production goods enjoyed a third straight gain at 3.4% (+10.5%). Capital goods were down another 2.2% (-9.1%). Inventories fell a fifth month with a 1.4% drop (-1.5%), and the inventory ratio was down 2.5% (-8.9%) for a third monthly decline.

Results (preliminary)

IIP: +1.7 % MoM
(Bloomberg forecast: +1.4%)

- Shipments: +2.1%
- Inventories: -1.4%
- Inventory ratio: -2.5%

METI Survey of Production Forecast (MoM):

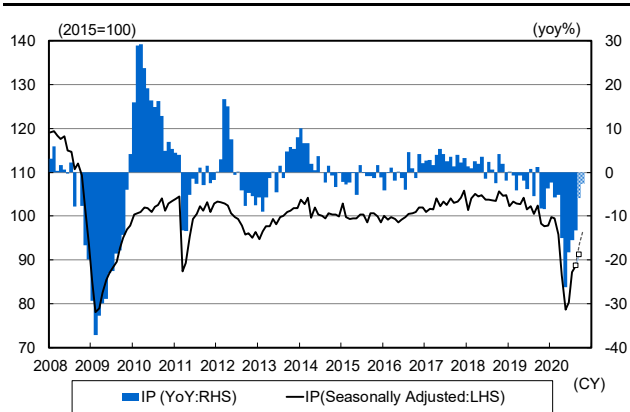
Sep 2020: +5.7% (adjusted to exclude prediction error: +2.8%)

Oct 2020: +2.9%

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- (4) Forecast index:** The production forecast index of early September (deadline for response: 10 September) calls for added gains of 5.7% MoM in September and 2.9% in October. METI's forward estimate for September, which adjusts the index for prediction error, is a 2.8% increase. The forward estimate previously tended to significantly underperform the forecast index, but that trend has gradually weakened. If the forecast index proves correct, the result would be a 9.9% QoQ rise in 3Q 2020 (2Q: -16.9%) and a 7.3% gain in October over the 3Q average. A rise equivalent to the forward estimate would mean an 8.8% QoQ increase in 3Q.
- (5) Forecast index by industry:** Production plans for general, production and business machinery call for increases of 6.9% in September and 6.0% in October. However, we should note that the forecast index in this sector tends to be bullish. In contrast, transportation machinery production usually proves close to the forecast (+11.4%, +2.9%), and we believe the upcoming results should be roughly as predicted. Electronic parts & devices (+6.3%, -1.1%) were revised up significantly (forecast index +10.2%) for September. We suspect that this incorporates anticipated rush demand from Chinese telecom equipment makers prior to the tightening of US sanctions as well as an expected backlash in October. Still, the outlook for the sector on average remains steady.

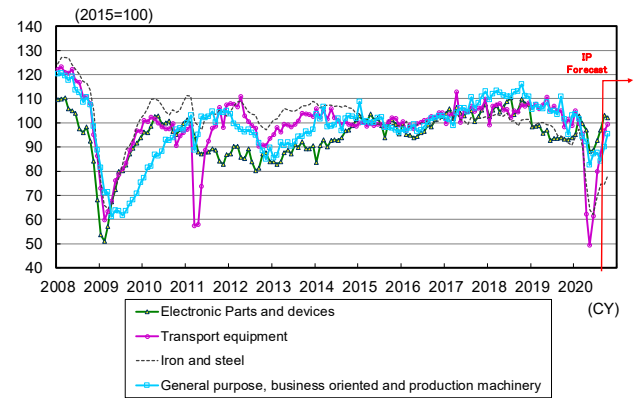
Figure 1. Industrial production (monthly)



Note: Seasonally adjusted figures for Sep -Oct 2020; dotted lines indicate MoM change in the forecast index; squares indicate estimates adjusted for prediction error. YoY changes are for the forecast index.

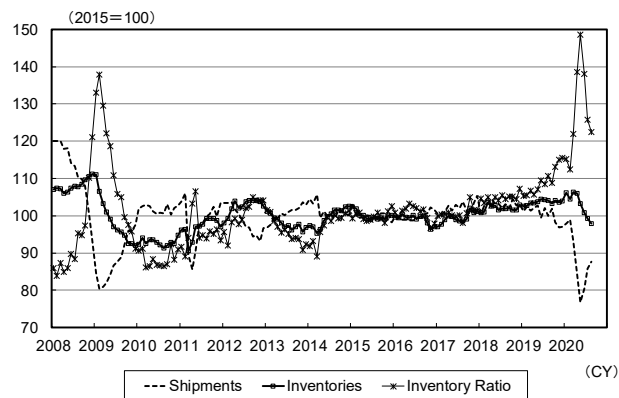
Source: MUMSS, from METI "Indices of Industrial Production" and "Indices of Industrial Production Forecast"

Figure 2. Industrial production by industry (monthly, SA, 2015=100)



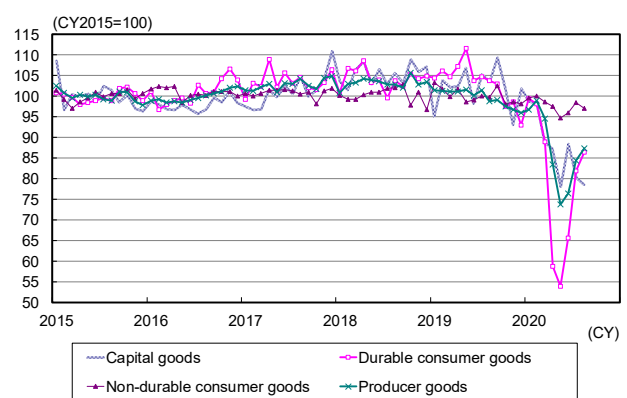
Source: MUMSS, from METI "Indices of Industrial Production" and "Indices of Industrial Production Forecast"

Figure 3. Shipments, inventories and inventory ratio



Source: MUMSS, from METI "Indices of Industrial Production Forecast"

Figure 4. Shipments by product category



Source: MUMSS, from METI "Indices of Industrial Production"

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Appendix A

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