

Japan

Policy rewarded as PMIs signal ongoing robust growth and rising price pressures

- All-sector PMI dips in April, but remains consistent with strong growth upturn
- Accelerating growth in manufacturing offset by softer expansion in services
- Input costs rise on weaker yen, with some pass-through to selling prices

The Markit/JMMA Japan PMI surveys point to an ongoing growth spurt in the Japanese economy in April, albeit with growth tapering off slightly compared with March's survey peak, and accompanied by signs of rising price pressures.

The all-sector PMI fell to 51.8 in April, but the decline to a large extent merely reflects some payback from a steep rise to 53.2 in March, which had been the joint-highest since data were first available in late-2007.

The easing was confined to the service sector, where a slowdown compared to March's record high was in part offset by a further acceleration in manufacturing growth, leaving the current reading of the PMI still high by historical standards of the Japanese survey.

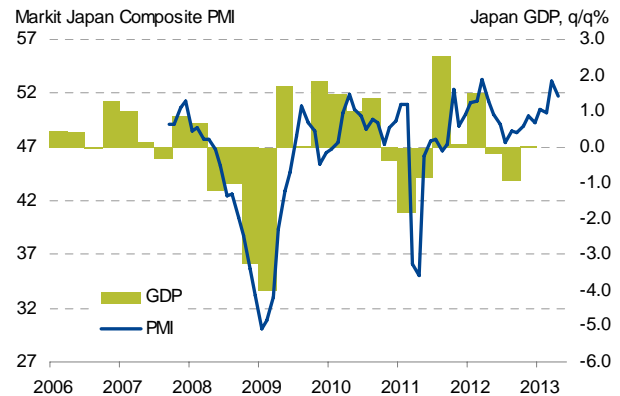
The data not only suggest that the economy returned to growth in the first quarter, but that the pace accelerated to around 1.5% in the three months to April. The comparison with last year is impressive: the economy stagnated in the fourth quarter and shrank by 0.9% in the three months to September.

The PMIs therefore add to evidence that the range of new policy initiatives designed to end two decades of deflation continue to have a positive effect on the real economy, as we had first indicated back in March ([see 'PMIs point to Abenomics-fuelled growth upturn'](#)).

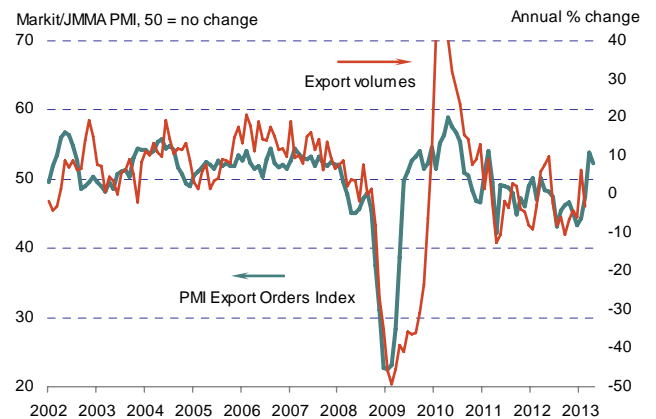
Key to the success of the new policies will be the ability of policymakers to increase prices alongside an upturn in economic activity, and to ensure that short-term price increases do not end up all-too short-lived. In this respect, the PMI surveys also provide encouraging news.

The weakened yen, which has depreciated by approximately one-quarter against the US dollar over

Economic growth



Exports



Sources: Markit, Ministry of Finance.

Sector output trends



the past year, has had a two-fold impact. First, by reducing the price of Japanese goods in overseas markets it has contributed to the fastest growth of exports for almost three years in recent months. Japan's export growth in April was exceeded globally only by the UK and South Korea, [according to the global PMI rankings](#).

Second, the falling yen has increased the cost of imported goods. Manufacturers' input costs rose at the fastest rate for over a year-and-a-half in April, despite a fall in global commodity prices. *The Economist's* commodity price index, quoted in US dollars, fell 4.0% in April.

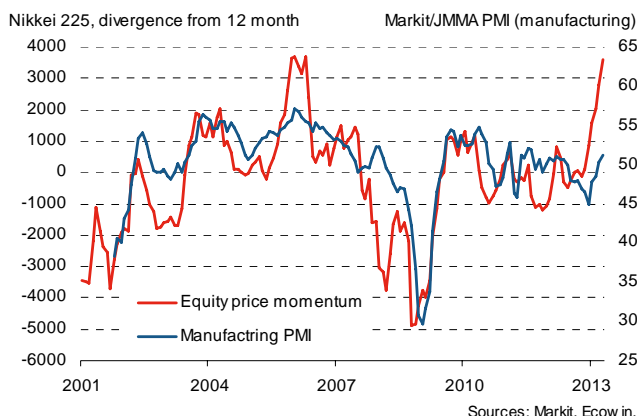
Service sector costs are meanwhile showing the strongest upturn since late-2008, reflecting a combination of higher fuel prices but also upward pressure on staff costs. Rising salaries will be crucial to ensure deflation is conquered.

Higher cost pressures are yet to feed through to higher selling prices at Japanese manufacturers and service providers, both of which fell again in April. However, the rates of decline were marginal, suggesting that the deflationary trend is moving in the right direction.

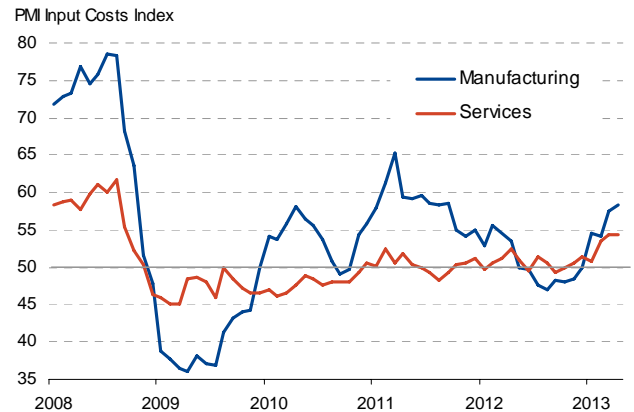
Equity exuberance?

A concern is that recent trends in share prices and the PMI have diverged to the greatest extent seen in the history of the manufacturing PMI survey (see chart). The divergence of the Nikkei 225 from its 12-month average hit its highest since April 2006. The hope is that the rally in share prices will help drive a further improvement in confidence and real economy growth. On the other hand, unless the economic data pick up further in coming months, as the impact of Japanese policies is perhaps limited by a fight against a tide of [slowing global economic growth](#), it will start to look like prices have risen far more than is currently justified.

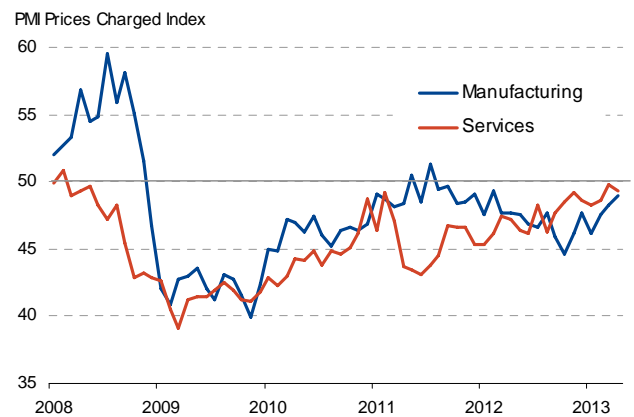
Japanese PMI and share prices



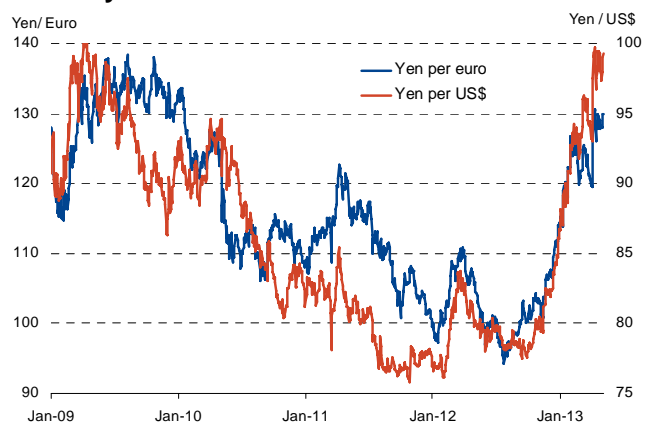
Input costs



Prices charged



Weaker yen



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