Markit Economic Research

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Japan

PMI signals near-stalling of manufacturing sector

- ■ **Manufacturing PMI falls to four-month low**
- ■ **Output barely grows, employment falls, exports grow at weaker rate**
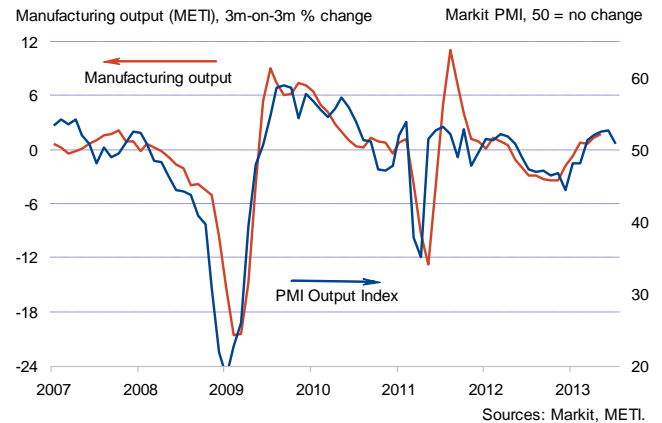- ■ **Price pressures ease**

PMI survey data hinted at a waning impact of Japan's economic stimulus plan, dubbed 'Abenomics', at the start of the third quarter. After strong survey readings pointed to a further strengthening of GDP growth in the second quarter, the third quarter may bring disappointment to policymakers. The manufacturing PMI signalled a near-stalling of growth in the sector in July. Alongside an easing in growth of manufacturing output, new orders and exports, the survey found price pressures to have eased again, and that employment started to fall again as companies cut capacity in line with weak demand.
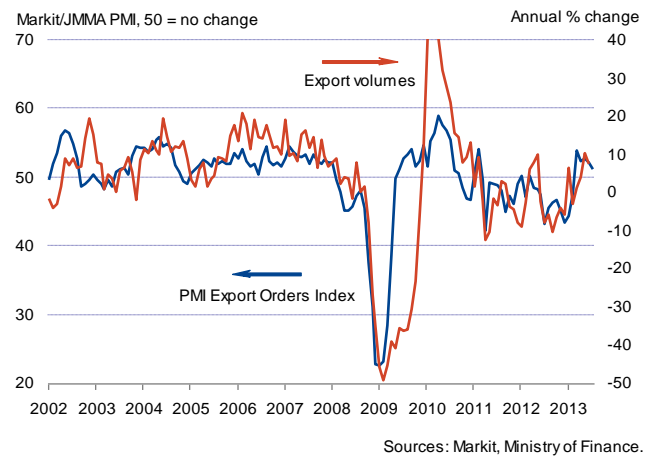
Manufacturing slowdown

Having risen to its highest for over two years in June, rounding off the best quarter of growth for the manufacturing sector for three years, the Markit/JMMA PMI fell in July. Dropping from 52.3 in June to a four-month low of 50.7, the PMI signalled a marked easing in the rate of growth of the goods-producing sector at the start of the third quarter. Output grew at the slowest rate since February, registering only a modest increase after the strong gains seen throughout the second quarter. New order growth also slowed, registering the weakest increase since March.

One of the consequences of the increased aggressiveness of the Japanese stimulus has been to lower the value of the yen. Exporters have benefitted via lower selling prices in overseas markets. However, July's PMI survey showed that, although new export orders rose for the fifth straight month, the latest increase was only modest and the smallest seen over this period. Any increase in competitiveness resulting from the weaker yen is being in part countered by weak economic growth in key export markets, notably China.
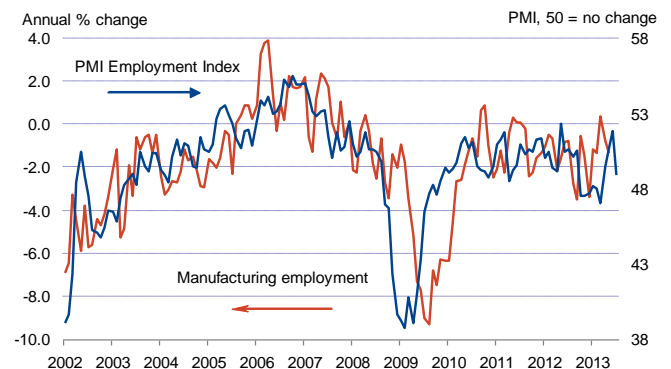
Manufacturing output

Manufacturing output (METI), 3m-on-3m % change

Markit PMI, 50 = no change

Sources: Markit, METI.

Exports

Markit/JMMA PMI, 50 = no change

Annual % change

Sources: Markit, Ministry of Finance.

Employment

Annual % change

PMI, 50 = no change

Price pressures abate

Policymakers are seeking to generate inflation of 2% in two years' time. Inflation rose to 0.4% in June, but the surveys suggest that any impact of policy beyond the immediate impact of higher import costs due to the yen's depreciation were difficult to find. On one hand, input prices continued to rise, up for the seventh successive month, linked in part to rising import prices. Although the rate of growth in input costs eased, higher input costs in Japan sit in contrast to falling prices in many other countries, in turn associated with lower global commodity prices.

However, prices charged barely rose during the month, suggesting little feed-though of rising costs to final prices. In many cases, this could be attributable to the need for companies to offer discounts to stimulate sales amid weak demand.

It's worth noting, however, that the marginal increases in selling prices seen over the last three months contrast markedly with the continual fall in prices seen over much of the previous two years.

The fight against deflation is only likely to work if initial price pressures translate into higher wages, generating a wage-price spiral that will keep prices rising over a sustained period. However, higher wages require an improving labour market (alongside labour market reforms). With the PMI's employment index dropping below 50.0 for the first time in three months in July, companies are once again shedding staff. Job cuts were commonly related to an excess of capacity against disappointing order book growth. Backlogs of work fell at the steepest rate since January, suggesting a further net loss of jobs is likely in August.

Producer prices
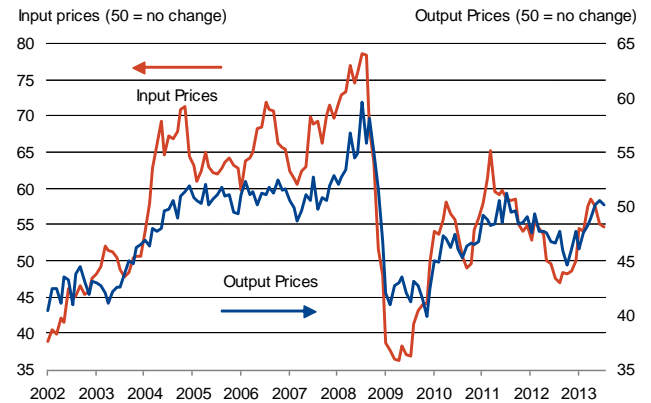
Yen
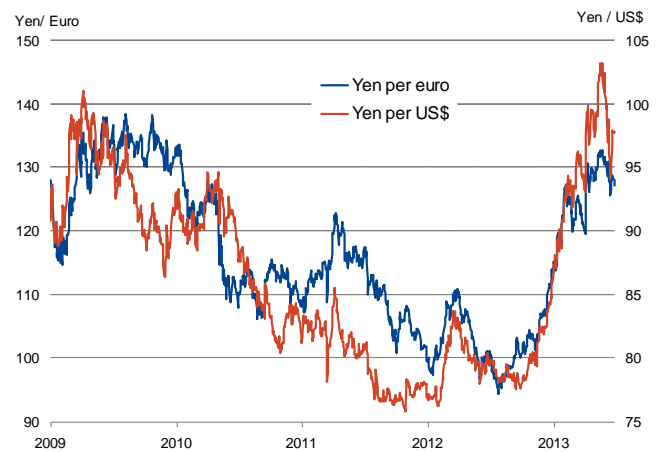
Chris Williamson

Chief Economist

Markit

Tel: +44 207 260 2329

Email: chris.williamson@markit.com

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