

# Japan

## The shadow of deflation looms heavy over Japan

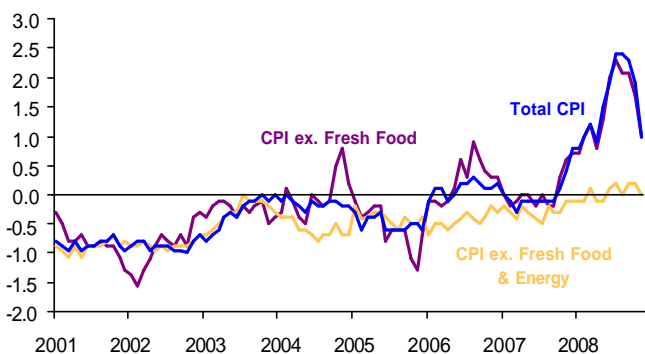
### Key findings

- **The rate of consumer price inflation dropped to 1% in November.**
- **PMI predicted slower inflation.**

### Japan's inflation eased in November

The Japanese Ministry of Internal Affairs indicated that inflation cooled significantly in November, with the annual rate of inflation down from 1.7% in the previous month to 1.0%. Moreover, the index excluding fresh food also declined, from 1.9% to 1.0%. While the core index - excluding fresh food and energy - was at 0.0%, from a 0.2% increase in October. In all three instances the monthly rate of inflation eased (see chart 1).

**Chart 1: Japan Consumer Prices A%C**



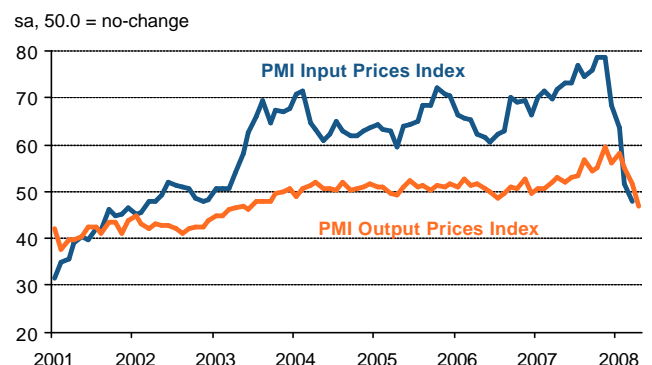
The November inflation numbers for Japan have therefore raised fears that deflationary forces, which crippled its economy for the best part of a decade, remain entrenched. This is highlighted by the fact that core inflation – inflation excluding fresh food and energy – has not once strayed above 0.2% in the current period of inflation. Soaring oil and commodity prices which have fuelled inflation over recent years, merely masking the true extent of Japan's deflation problem temporarily, are now plummeting amid the global economic downturn.

This, combined with a sharp decline in average prices charged by Japanese manufacturers, is a major concern moving into 2009.

### PMI anticipated weaker inflation

In line with official data, November's Nomura/JMMA PMI Input Prices Index signalled that the rate of manufacturers' input price inflation slowed to its weakest in just over four years. The index remained above the 50.0 mark that separates expansion from contraction posting 51.5 from 63.7 in November. Furthermore, November's PMI Output Prices Index fell to a similar level, recording 51.6. The downward trend in the Japanese CPI seen during Q3 and the beginning of Q4 has been broadly captured by PMI data, with both PMI price indexes exhibiting a sharp downward tendency since July. Moreover, PMI data are released approximately a month in advance of the official CPI, indicating that the PMI is a timely indicator of movements in consumer prices.

**Chart 2: PMI Input Prices Index & PMI Output Prices Index**



### Deflation predicted to re-emerge

Japan's deflationary dilemma looks set to return to centre-stage heading into the new calendar year, with both the PMI price indexes indicating a fall in average prices in December.

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The next Japan Manufacturing PMI is released on the 30<sup>th</sup> January 2009. To find out how to receive data from the surveys, or obtain copies of the reports please contact [economics@markit.com](mailto:economics@markit.com)

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