

Global economy

Manufacturing surges, service sector stumbles

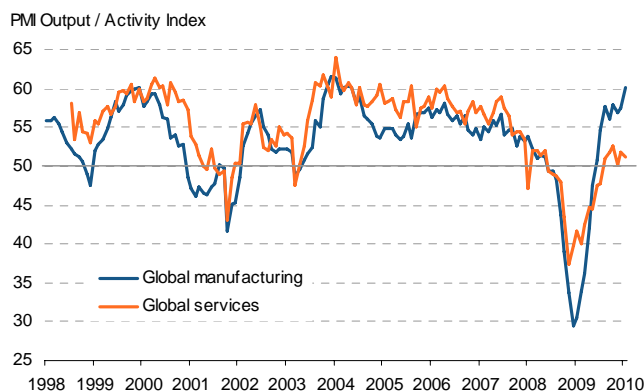
Two-speed world economy

If 2010 was a running race, manufacturing positively flew out of the starting blocks while the service sector stumbled, or perhaps – in the case of Northern Europe at least – slipped on the ice.

The Global Manufacturing PMI Output Index, compiled by Markit for JPMorgan and based on the monthly Purchasing Managers' Index surveys, surged from 57.5 in December to 60.2 in January, signalling the strongest monthly increase in production since April 2004 – a time when worldwide manufacturing output was growing at a pace of nearly 6% per annum.

The equivalent index for services fell from 51.8 to 51.2 in January. By remaining above the 50.0 'no change' level, the service sector index continued to indicate expansion, but only just – and at a slower rate than in December.

Global manufacturing and services



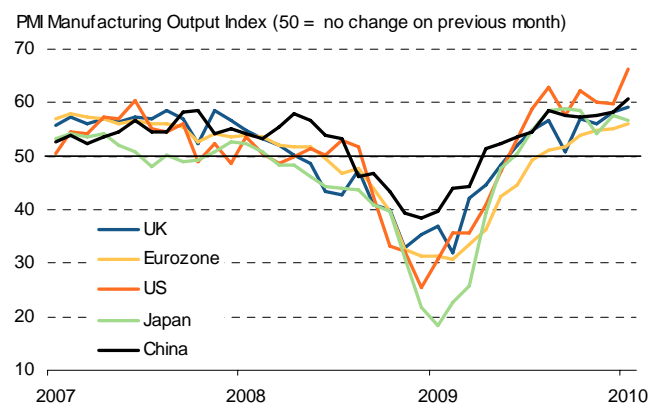
Source: Markit, JPMorgan.

Manufacturing vigour

Manufacturing output rose at the fastest pace for nearly six years in both the US and China, while in the UK a three-and-a-half year high was seen (the composite PMI for the UK – based on five survey variables including orders and employment – hit a 15-year peak). A two-and-a-half year high was meanwhile recorded in the Eurozone, led by France and Germany.

While China led the emerging market recovery, other Asian countries, such as India, Taiwan and South Korea, also saw accelerating rates of manufacturing growth. Even Eastern Europe, which has lagged the global recovery, saw some renewed vigour.

Manufacturing output

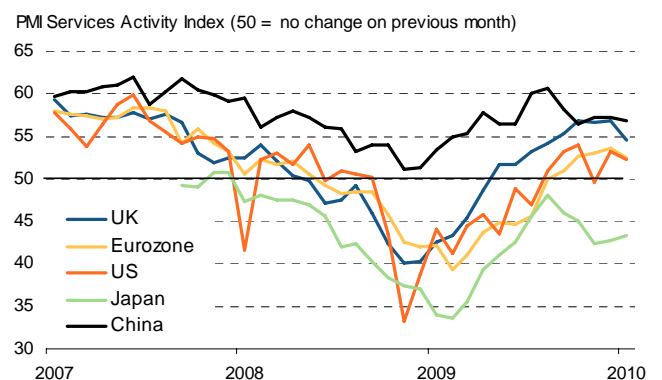


Sources: Markit, ISM.

Service sector doldrums

It was a different story for services, however, where all countries saw considerably slower growth compared to manufacturing in January. In many cases rates of recovery slowed for services.

Service sector business activity



Sources: Markit, ISM.

In Northern Europe, particularly in the UK, France and Germany, slower service sector growth was linked to heavy snow falls and freezing temperatures. While

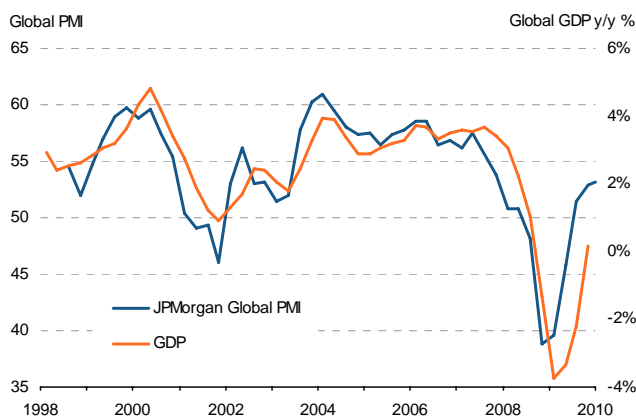
manufacturers were often able to make up for lost days resulting from bad weather, owners of hotels, restaurants and other consumer-oriented services simply found that customers stayed at home, in many cases representing a permanent loss of business. Japan meanwhile continued to suffer an ongoing contraction of its service sector and in the US the rate of expansion disappointed, slowing from December's already-subdued pace.

It is, of course, not possible to precisely quantify the impact that the bad weather had on service sector business levels, which is all the more frustrating as it comes at a time when signs of stronger growth outside of the manufacturing economy are being eagerly watched for as a key element of a more sustainable recovery.

Global GDP growth lacks upward momentum

The divergent trends of manufacturing and services left the 'all sector' Global PMI marginally higher than December, at 53.2 in January compared to 53.1, but down on the recent peak of 53.7 seen last October. The latest numbers point to worldwide GDP rising at an annual rate of around 2%. So while the global recovery continued, led by emerging markets and the US, followed by Europe, it is not clear how much underlying momentum – if any – has really been lost. The pace nonetheless remains well below that seen prior to the financial crisis.

Global GDP



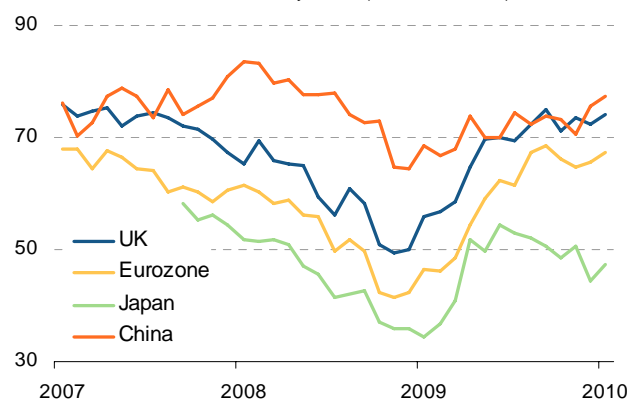
Sources: Markit, JPMorgan, EcoWin

In this respect, some of the PMI 'sub-indices' provide reassuring signs. Notably, growth of global service sector incoming new business improved in January to the fastest since 2007, although it must be said that it

remained disappointingly lacklustre. Service sector expectations about the year ahead also generally improved, reassuringly so in the snow-bound areas of Northern Europe (with service providers perhaps hoping that consumers will have saved some unspent cash during the poor weather for more luxuries later in the year). The overall rate of worldwide job losses also slowed marginally, showing the weakest decline since August 2008, suggesting that private sector employers are at least less pessimistic and cost-conscious.

Service sector confidence

Services PMI future business activity index (12 month outlook)

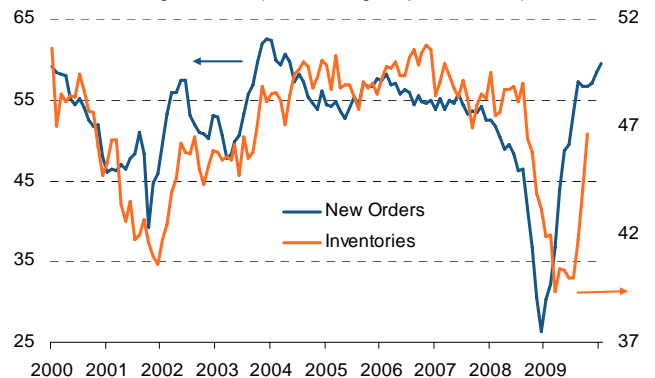


Source: Markit.

However, irrespective of the growth momentum in the service sector, it is evident from the PMI surveys that the global recovery continued to be very dependent on the rebound in world trade and the manufacturing inventory cycle. New orders growth is set to slow when client inventories return to normal. Signs of stronger 'final demand' in future months will be crucial in determining the sustainability of the recovery.

Manufacturing inventory cycle

Global Manufacturing PMI indices (50 = no change on previous month)



Sources: Markit.

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