

# Global economy

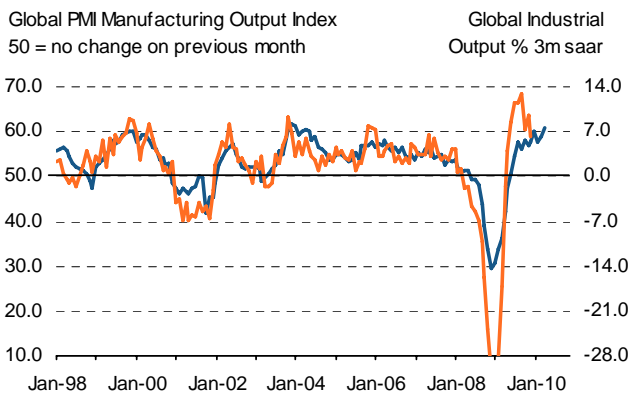
## Manufacturing recovery gains momentum to reach record pace in the developed world, while speed slows in emerging markets

### Global manufacturing growth strongest since 2004

The JPMorgan Global Manufacturing PMI, a composite index derived from survey indices relating to output, order books, employment, inventories and supplier performance, compiled by Markit, rose from 56.8 in March to 57.8 in April – just fractionally below the all-time high seen in May 2004<sup>1</sup>. The latest PMI points to an improvement in global manufacturing business conditions for the tenth month running.

The April PMI data are consistent with global industrial production rising at a quarterly rate of 7%.

### Global manufacturing output



Sources: Markit, ISM, JPMorgan.

Looking into the indices that contribute to the PMI, three important trends are highlighted.

First, although robust output growth was reported in all major developed and emerging nations, rates of expansion accelerated in developed countries such as the US and the Eurozone, but slowed in the emerging powerhouses of China, India and Brazil. However, the slowdown hinted at by the PMI data in the emerging countries is not yet indicative of a definite turning point.

Second, sub-indices suggest that the recovery in the developed world is gaining sustainability, as

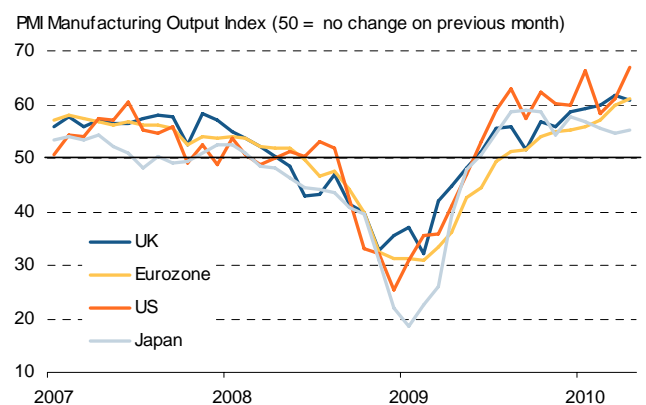
manufacturers seek to expand capacity to meet demand.

However, the third trend is that a side effect of the growth surge is a further increase in inflationary pressures as demand runs ahead of supply.

### Record growth in developed countries contrasts with cooler pace in emerging markets

Output growth in April was the strongest since January 2004 in the US and since June 2000 in the Eurozone (led by Germany and France). Meanwhile, the pace slowed only slightly from March's 15-year peak in the UK. Japan continued to lag but nevertheless reported a slight but encouraging re-acceleration of growth. As a result, a weighted index of manufacturing output growth in the developed countries rose to the highest seen since data were first available in 1998.

### Developed world manufacturing output



Sources: Markit, ISM.

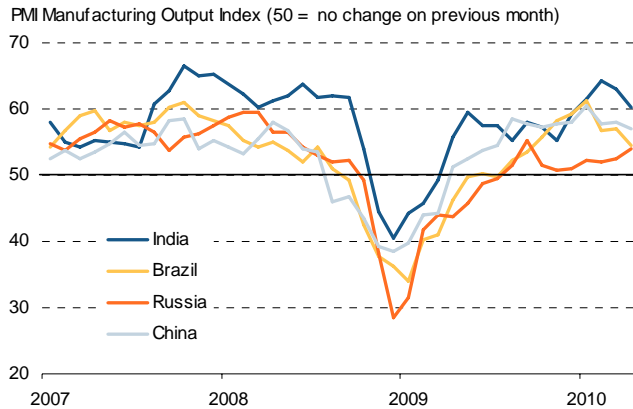
### But pace cools in emerging markets

Emerging nations as a whole also reported very strong manufacturing output growth in April. However, in contrast to the faster growth seen in developed countries, rates of expansion slowed to nine- seven- and four-month lows respectively in China, Brazil and

<sup>1</sup> The manufacturing PMI series began in January 1998.

India. Only Russia saw growth accelerate in April, though its recovery remains lacklustre.

**Emerging market manufacturing output**



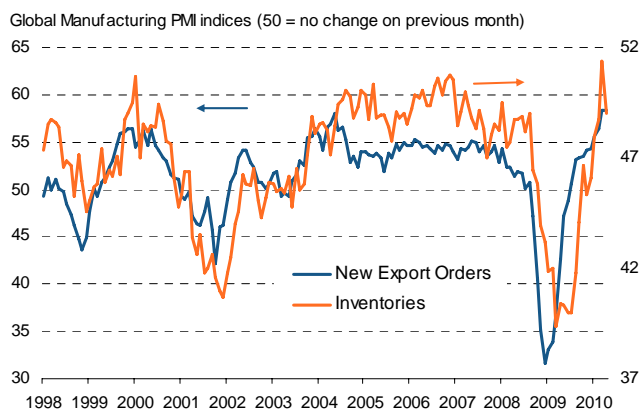
Source: Markit, HSBC, VTB.

**Hopes raised of a more sustainable recovery**

The recent growth surge has been driven by soaring global trade flows, which plummeted in the recession but have since recovered strongly. Having sunk to an all-time low in December 2008, the PMI surveys' New Export Orders Index rose to a new high in April.

This volatility of global trade can be in part attributed to the inventory cycle. While companies pared back their stock holdings as much as possible during the downturn, they are now starting to rebuild their inventories to meet rising demand.

**Global manufacturing new export orders and inventories**



Sources: Markit, ISM, JPMorgan.

In many cases, companies report that inventories continued to fall simply because they were unable to purchase sufficient quantities of inputs, linked in turn to a lack of stock at suppliers. This is a short-term

capacity issue: suppliers (and especially companies producing inputs for other manufacturers) need to raise operating capacity to rebuild stock levels and meet demand. This lack of capacity is highlighted by manufacturers reporting that suppliers' delivery times continued to lengthen at a near-record rate in April.

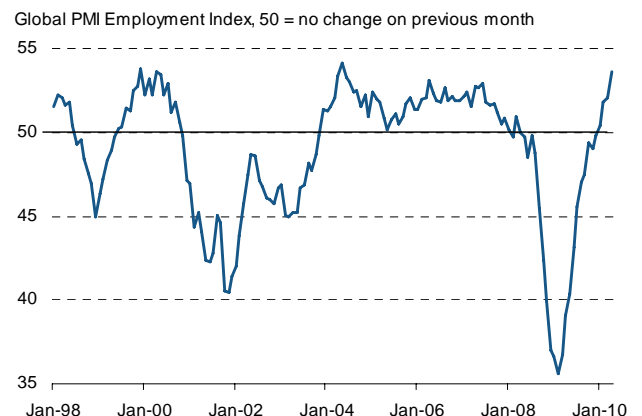
**Global manufacturing PMI supplier delivery times**



Sources: Markit, ISM.

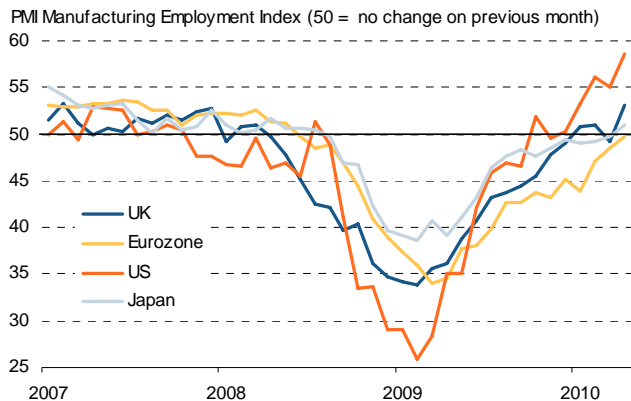
The longer-term, and more positive consequence, of demand exceeding supply is that manufacturers have begun to take on more staff to address the capacity shortfall. Globally, manufacturing employment rose for the fourth month running in April, having declined almost continually over the preceding two years. Moreover, the increase in headcounts in April was the largest since May 2004 and driven to a large degree by recruitment within developed countries. Both German and Japanese manufacturers reported a return to employment growth in April for the first time in these recoveries, US producers reported the best jobs growth since January 2005 and the increase in UK staffing levels was the largest since February 2007.

**Global manufacturing employment**



Sources: Markit, ISM.

### Manufacturing PMI employment indices



Sources: Markit, ISM.

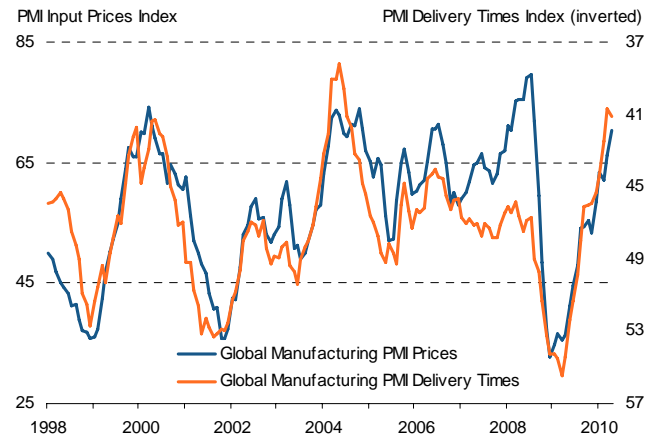
Rising employment is particularly welcome as it points to improved job security, higher incomes, rising consumer confidence and greater consumer spending, which should in turn help bolster economic growth. It also suggests that companies may also be ready to raise capital expenditures as they increase production capacity (and Markit's European PMI indicators relating to capital goods producers' order books support this idea).

### Supply chain price pressures rise

On the other hand, a down-side to the surge in demand for inputs to meet buoyant manufacturing expansion is that suppliers have been increasingly able to charge higher prices. The average increase in

manufacturers' input costs in April was the largest since August 2008, with new recovery-highs recorded in the US, UK and the Eurozone, and a further acceleration in the rate of increase seen in China.

### Manufacturing PMI input prices



Sources: Markit, ISM, JPMorgan.

It is likely that these price pressures will be short-lived to some extent, as ongoing employment growth will help address the shortfall of supply against demand. However, price rises could prove stickier if companies remain cautious about future growth, and prefer to boost margins instead of building extra capacity. Indicators such as the Suppliers' Delivery Times Index should prove useful in tracking these trends.

## Chris Williamson

### Chief Economist

Markit

Tel: +44 20 7260 2329

Email:

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