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Markit Economics Research

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Global manufacturing prices

Prices fall at sharply reduced pace

Key findings

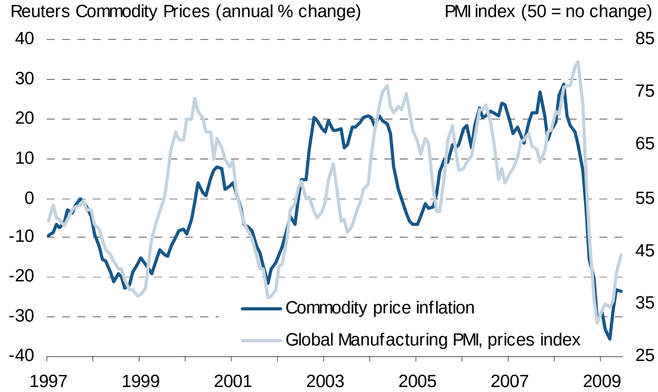
- **Global manufacturing Input Prices Index shows largest rise over a quarter for nearly four years.**
- **Supplier delivery times likely to lengthen, adding further pressure to prices.**

PMI Input Prices Index rises

The Prices Index from the Global PMI, compiled by Markit on behalf of JPMorgan, rose to an eight-month high in June. The Index remained below the 50 level, meaning the number of purchasing managers reporting a fall in their average input prices continued to exceed the number reporting a rise, but the upturn in the Index in June signalled an easing in the rate of decline of input prices for the third month running. The increase in the Index between March and June was the largest over a quarter since Q3 2005.

The upturn in the Input Prices Index in Q2 largely reflects a rebound in commodity prices which, having hit a low last December, also hit an eight-month high in June according to the Reuters commodity price index. Prices still remain well down on a year ago, however. The annual rate of decline has merely eased from a peak of 36% in March to 23% in June.

Chart 1: Global PMI data and commodity prices



The upturns in commodity price and PMI Input Prices indices are both linked to improved demand and supply fundamentals, which are reflected in the PMI Suppliers' Delivery Times Index (see chart 2, in which the Global Suppliers' Delivery Times Index is inverted to show the relationship with prices – sub-50 Delivery Times Index readings signal longer supplier lead-times).

Supplier delivery times are closely correlated with input prices as they reflect supply and demand imbalances (supply chain delays occur when suppliers are busy due to strong demand, meaning they also have more pricing power, and vice versa). The Global Suppliers' Delivery Times Index signalled the smallest improvement in lead-times for eight months in June. Suppliers are increasingly unable to deliver goods promptly as demand from manufacturers recovers and their inventory levels remain low (stock levels having been depleted at record rates in recent months).

Chart 2: Global supplier delivery times and prices

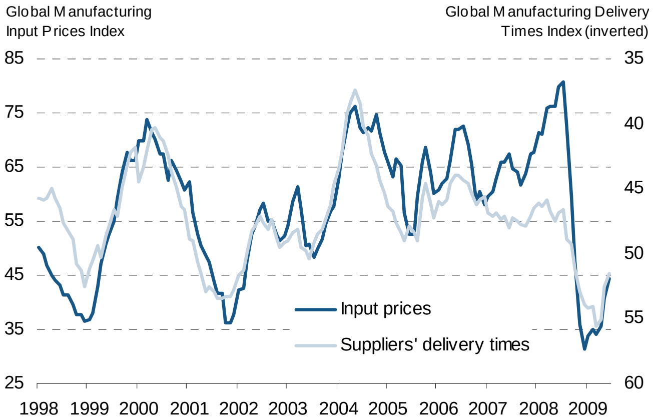


Chart 2 also illustrates how the surge in oil and other commodity prices in 2007-08 was driven primarily by speculative factors rather than industrial demand-pull factors. (See also the oil price charts in the appendix. These show that global output growth was already slowing in late-2007, when oil prices began surging, and production was already contracting when prices peaked last summer).

Upward pressure on prices most evident in US and China

The June PMI data in Chart 3 show that manufacturers' input prices stabilised in the US and China, but continued to decline in the Eurozone, Japan and the UK. These variations can be explained to a large extent by differences in supply chain performance. Chart 4 shows that delivery times again shortened most sharply in the Eurozone, suggesting the region's manufacturers continued to enjoy a buyers' market for inputs on average. In contrast, supply and demand are more in balance in the US, where delivery times lengthened in June (albeit only slightly) for the first time since last September.

Chart 3: PMI Input Price Indices

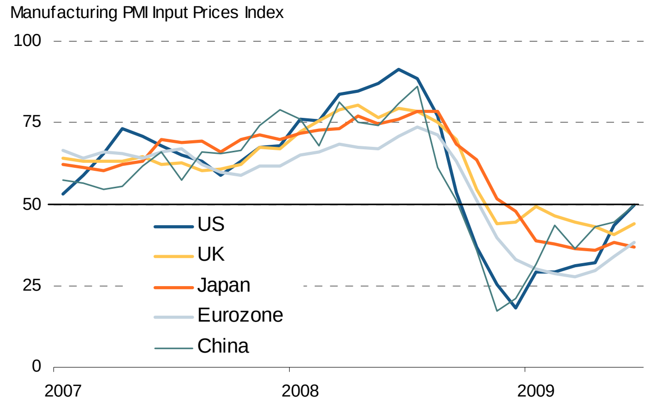
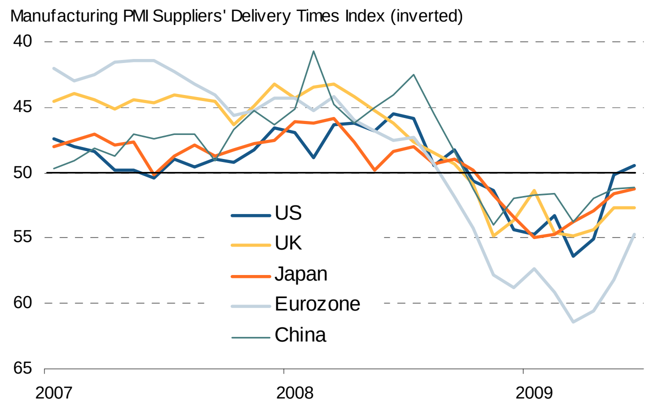


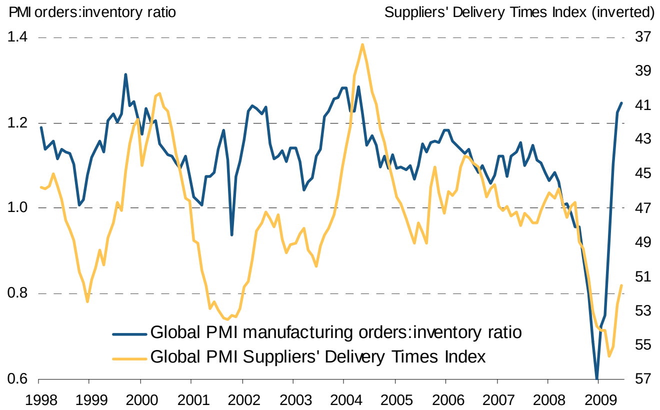
Chart 4: PMI Suppliers' Delivery Times Indices



Orders:inventory ratio suggests further support for commodity prices

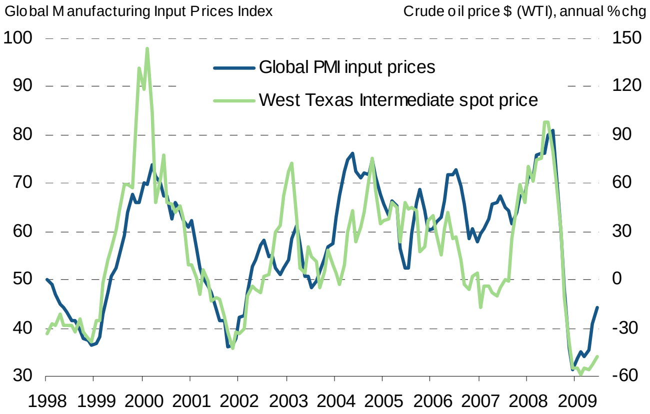
The future course of commodity prices will depend on the recovery path for manufacturing, and in particular what will happen after a rebound in demand for raw materials due to inventory rebuilding. This inventory-led upturn is clearly signalled by the Global PMI's order:inventory ratio, which rose to the highest level for over five years in June. Chart 5 illustrates that significant improvements in the orders:inventory ratio are always followed by a lengthening of suppliers' delivery times. And, as chart 2 shows us, longer delivery times have historically always been accompanied by upward price pressures.

Chart 5: Price pressures and the inventory cycle

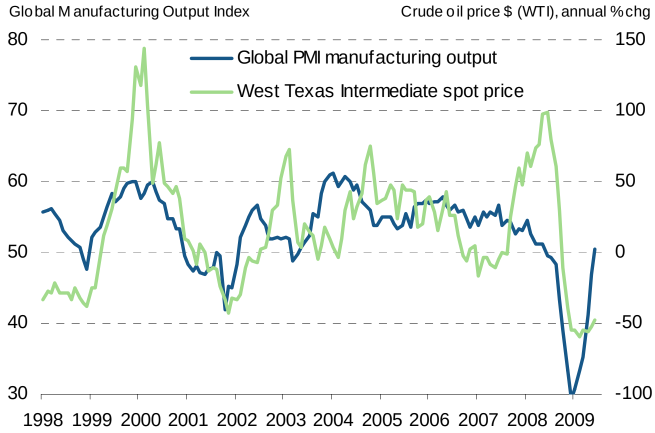


Appendix: Oil prices

Oil price impact on manufacturing costs



Oil prices and manufacturing production



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