HSBC Global Research

4 February 2022

Have supply constraints peaked?

Global PMI wrap-up (Jan)

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Economics - Global

- 2022 started on a rather slower note with the global composite PMI easing from 54.3 to 51.4
- The Omicron variant led to a slowdown in the services PMIs, but the manufacturing sector was more resilient
- Input price indices look to have peaked, and we see signs of supply constraints easing

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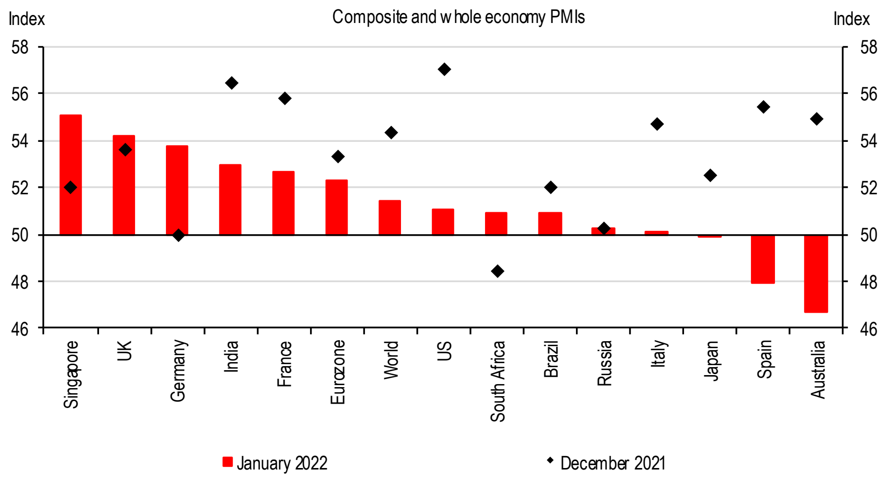
Composite PMIs – World at a glance



Source: IHS Markit, HSBC. Note: No data for mainland China, to be released on 7 February

The global composite PMI slipped from 54.3 to 51.4 in January. That said, overall PMI data still point to growth and highlight the relative resilience of both the manufacturing and service sectors despite the Omicron variant. Businesses have become much more adept at dealing with the pandemic, and with new COVID-19 cases looking like they have peaked in many economies, the future outlook looks relatively bright for 2022.

The manufacturing sector in particular has showed remarkable resilience. That said, the global headline PMI fell by 1.1ppt to 53.2 in January, primarily due to increased numbers of COVID-19 cases in many countries. However, many countries including Germany, Japan, Thailand and Vietnam showed a sharp improvement.

The Omicron effect is more pronounced in the service sector. Rapid transmission of the virus has dampened the global services PMI, which fell to an 18-month low of 51.3.

However, there is a silver lining. While input prices look to have passed the peak, we are seeing early signs of easing supply delivery times. This may precede some cooling of supply constraints that would aid the growth-inflation mix through the course of 2022.

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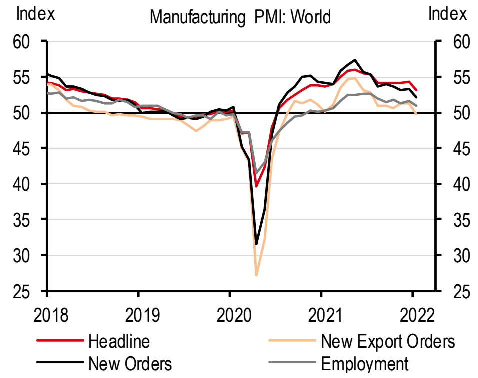
What are the data telling us?

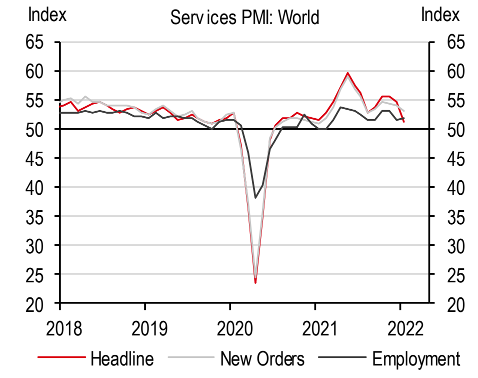
The global PMI data continue to paint a mixed picture. The manufacturing sector continues to remain resilient with the global headline index having been above the 50 watermark level for 19 straight months. That said, 2022 started with global manufacturing PMI easing to the weakest reading in 15 months. The slowdown reflected weaker growth of incoming new work, declining international trade volumes, supply chain disruptions and rising COVID-19 infections primarily due to the Omicron variant. And this trend is more pronounced in the service sector where the global PMI fell to 51.3, an 18-month low.

1. The global manufacturing PMI edged down in January



Source: IHS Markit

2. The global services PMI felt the effects of Omicron in January

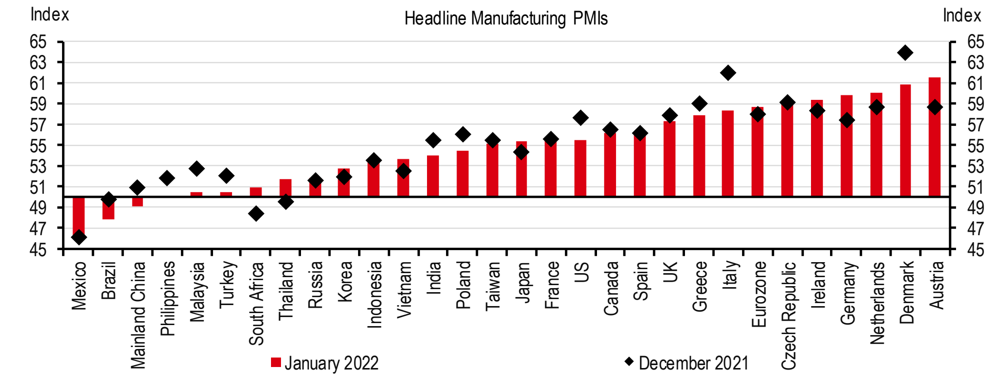


Source: IHS Markit

Manufacturing activity remains steady

Global manufacturing PMIs have been remarkably steady despite COVID-19 related restrictions and uncertainties. That said, the global headline PMI fell by 1.1pt at the beginning of the year, although it remained above 50. Output, new orders and employment all mirror the headline trend. In January we saw a sharp improvement in the manufacturing PMIs in Germany, Thailand, Vietnam and Japan. Meanwhile, mainland China's PMI fell below 50 as rising COVID-19 cases, both domestically and abroad, and seasonal softer demand in preparation for the Chinese New Year resulted in a slowdown in activity. Brazil, India and Mexico's manufacturing PMIs also deteriorated in January.

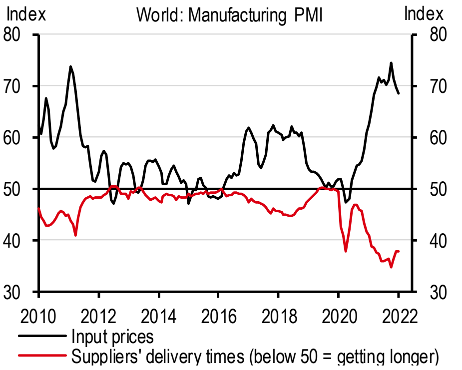
3. Even though the global index edged down, the global picture is diverse



Source: IHS Markit

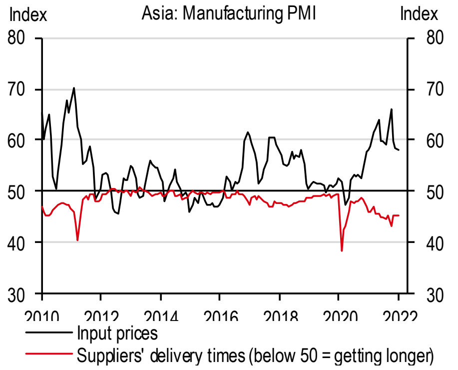
On the prices front, input prices look to have peaked in the majority of economies. Some exceptions include mainland China, Russia, Thailand, and Vietnam which are still experiencing rising input prices. Chart 4 shows that globally, input prices have started falling. However, manufacturers have transferred some of the increased cost pressures to output prices. The global manufacturing PMI output prices index increased by 1.1ppt which is in line with increasing consumer prices across the globe.

4. Supply issues and price pressures look to have peaked…



Source: IHS Markit

5. …but some countries in Asia still have longer supply delivery times



Source: IHS Markit

Supply issues have been a key part of the global economics story over the course of the past year. Panellists cited lack of availability of raw materials & components in the market and pressure on transport capacity as primary reasons. Although the global suppliers' delivery times index is still below 50, it rose to its highest reading last March, suggesting that some of the pressures have started to lessen. And this also contributed to a mild deceleration in input cost inflation to a ten-month low.

These issues appear to be greatest in the US and Europe, but this is where the bulk of the improvements have been seen in recent months. However Asian economies such as Thailand, New Zealand, Hong Kong, Indonesia and Philippines are still experiencing notable pressures when it comes to delivery times, and there is less sign of improvement for now.

6. Supplier deliveries are very slow in most of the world

Source: IHS Markit. Note: Some economies don't have manufacturing PMIs; whole economy PMIs are used. All economies with a supplier deliveries component shown.

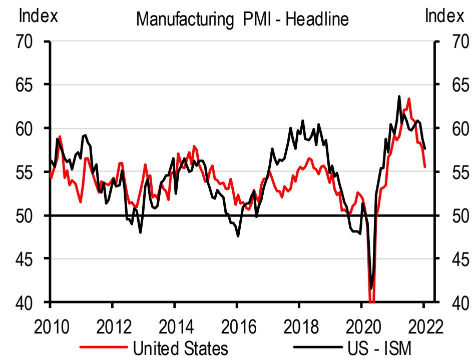
The combination of expectations of future growth along with the ongoing catch-up on backlogs continues to result in increased job creation. Manufacturing employment rose for the fifteenth consecutive month in January, although the rate of growth slipped to an 11-month low. Staffing plans increased in the US, the eurozone and Japan, with the pace of growth improving in the latter two. China and India were among the nations where firms are shedding workers according to the PMIs.

In the US, Markit's manufacturing PMI dropped to the lowest level since October 2020 amid more subdued demand conditions and labour shortages. The recent Omicron outbreak in the US hit the manufacturing sector hard in both the ISM and Markit PMI surveys. Staff shortages and supply chain issues resulted in only a marginal rise in output at the start of the year. That said, the overall impact on the supply chain has been less marked than prior COVID-19 waves and input prices also look to have peaked. As a result, manufacturers are much more upbeat about the future outlook.

In mainland China, the recent uptick in COVID-19 cases resulted in a fall in manufacturing activity as some cities re-imposed restrictions to curb the virus. Likewise, new orders also fell reflecting subdued demand conditions. Given relatively subdued manufacturing activity generally in Asia, and declining new export orders, it is no surprise that employment remains soft in most markets.

The notable exceptions are Japan, Taiwan, and Indonesia, reflecting the respective strength of their exports: capex goods, electronics, and commodities. That said, Lunar New Year holidays make the underlying trend hard to assess.

7. The manufacturing sector continues to lose momentum in the US…



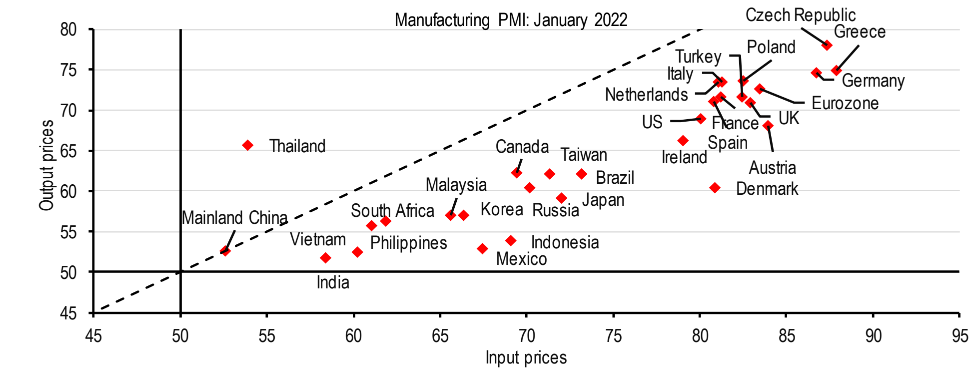
Source: IHS Markit, Institute for Supply Management

8. …but the fall in China's manufacturing PMI is more concerning

Source: IHS Markit

On the prices front, globally, input price indices remain high but they seem to have already peaked. Across Asia, input price indices are still much lower than in the developed world but they remain elevated by historical standards. Only in Thailand is the output price index rising more quickly than input price equivalents, suggesting that at least for now firms are absorbing some of their higher costs.

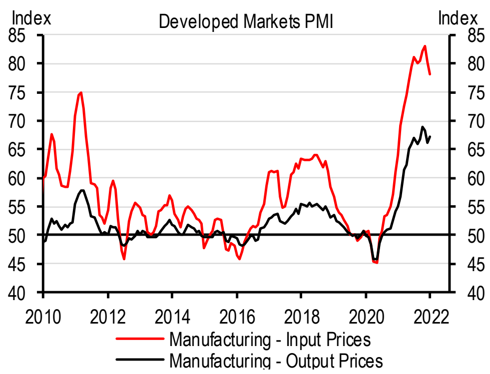
9. Price pressures continue to remain high in the developed markets



Source: IHS Markit

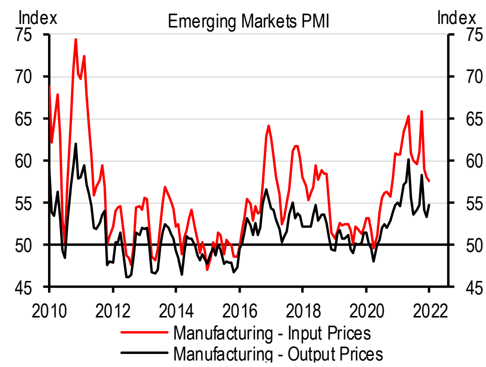
But we do see more signs of output prices increasing across the board. The trend is clearer for countries like France, Germany, mainland China, Thailand and Japan.

10. Developed market price pressures may have rolled over…



Source: IHS Markit

11. …and the trend is clearer in the emerging world

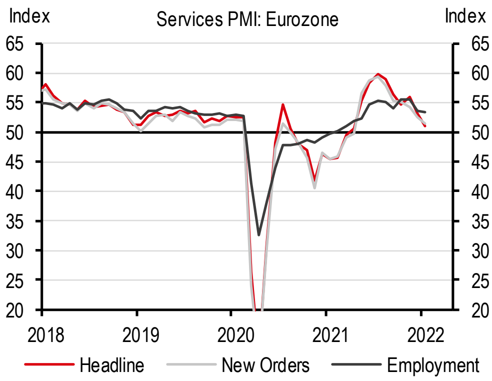


Source: IHS Markit

Services feel the impact of Omicron

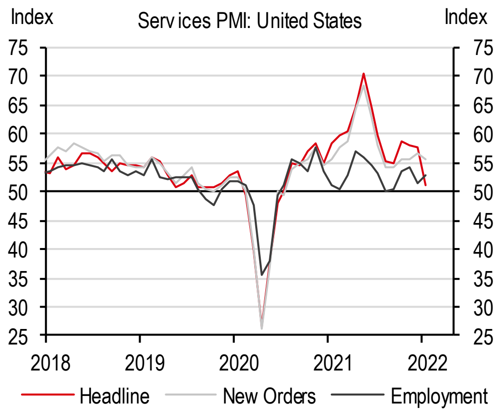
The impact of Omicron is more pronounced in the service sector. The global services PMI fell further to 51.3 at the start of the year from 54.7 in December 2021, although that global indicator doesn't include mainland China. We saw a fall in service PMI in most economies with the exception of Germany, UK and South Africa. The eurozone services PMI fell by 2ppt for the second consecutive month and the same trend followed for its components, namely new orders and employment. The US Markit services PMI fell sharply, from 57.6 to 51.2, but job creation picked up to 53.0 in January from 51.3 in the previous month. The impact was felt as a result of shortages of staff limiting output, something reflected in the ISM services (which fell from 62.3 to 59.9) where one respondent was quoted as saying: "*Labor constraints are presenting problems throughout all areas of the business*".

12. The eurozone services PMI continues to fall amid high numbers of COVID-19 cases…



Source: IHS Markit

13. …while Markit's US services PMI fell sharply

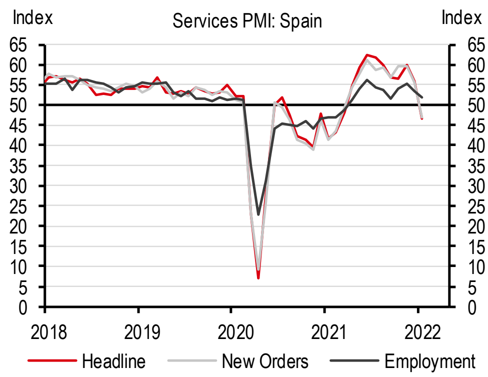


Source: IHS Markit

Europe became the epicentre of the pandemic in January and this was clear in the service PMI data. The worst performing countries were Spain and Italy where the service sector registered a noticeable drop in activity. Spain's services PMI fell to 46.6 in January from 55.8 in December – contracting for the first time since last March. Underlying the headline number was a similar decline in new business as demand slowed amid rising infection numbers.

Likewise, in Italy the services PMI fell to 48.5 in January from 53.0 in December as output fell for the first time since April last year. Panellists responded that weak demand conditions were the primary reason for contraction in January. France also recorded a fall in its services PMI, albeit the headline print remained above 50.

14. Spain's services PMI fell by the most anywhere in the world



Source: IHS Markit

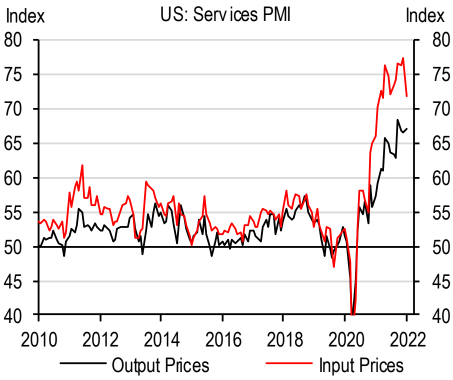
15. Germany's services PMI rose after a sharp fall in December

Source: IHS Markit

The story is a little different for Germany and the UK. January's services PMI rose in both countries after a fall in December 2021. In Germany, the headline index rebounded to 52.2 in January after a contraction in December. Service providers reported slightly improved inflow of new business at the start of the year which in turn contributed to a pick-up in the pace of job creation. Likewise, the recovery in the UK service sector output gained momentum during January as constraints from the Omicron variant began to ease and customer demand rebounded.

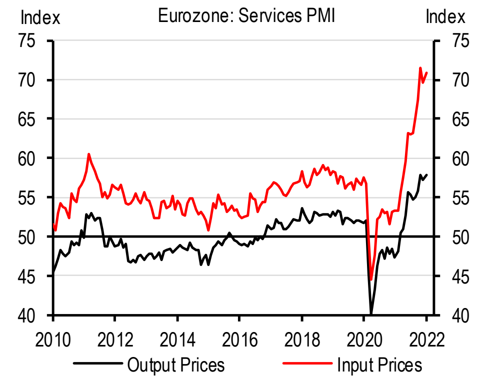
But January data pointed to a rapid increase in business expenses in the UK, with the overall rate of input cost inflation accelerating to its second-highest since the survey began. In fact, price pressures persist in the eurozone, with both the input and output prices indices rising. On the other hand, services input prices seem to have peaked in the US, while output prices continue to rise.

16. Input prices seem to have peaked in the US service sector while output prices are still on the rise…



Source: IHS Markit

17. …and price pressures continue to rise in the Eurozone



Source: IHS Markit

Summary

2022 started on a slower note, but we think future expectations remain bright. The manufacturing sector remains resilient despite the increased number of COVID-19 cases across the globe as businesses better adjust to the pandemic. But services activity waned as demand for high-touch services and restaurants deteriorated as cases increased. Fortunately, input prices in the manufacturing sector look to have already peaked and there are early signs of the easing of supply constraints as well. Data in the coming months will provide a better picture of how these supply related constraints are evolving.

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