# Supply chains and prices

## Will easing bottlenecks help to lower goods inflation?

**Free to View**
Economics - Global

- Supply chain issues are easing up, very quickly…
- …and inventories are high, just as demand softens…
- …potentially putting downward pressure on goods prices

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Global supply chain problems have played a substantial role in many of the economic developments in recent years – from shortages of various goods to the surge in shipping costs – and these issues have held back growth and lifted inflation.

Some estimates, such as those from Adam Shapiro at the San Francisco Fed, suggest that supply chain issues account for roughly half of the PCE inflation currently being seen in the US, and based on a similar methodology the same applies in Europe.

The major supply chain issues appear to be over, at least for now. With collapses in shipping rates, soaring inventory levels and sliding consumer goods demand, the question is what happens to these supply-led surges in inflation – notably within the goods side of the basket – as demand slows.

Having been evident for some time, the speed of the improvement in global supply chains has caught many by surprise. The drop in freight rates, a clear way of seeing this in real time, has seen the cost of sending a container from Asia to the US collapse by nearly 90% in 2022, far more than even the most ardent optimist could have ever predicted. Many logistics experts believe that these prices may drop below pre-pandemic levels in the coming months, and firms are reporting fewer problems obtaining stock as the backlogs of shipments have subsided.

But, of course, shipping and supply chain issues haven't been the only costs firms have faced in recent years – high energy prices (particularly in Europe) and wage costs have also pushed up input costs for firms. However, easing supply chain constraints don't just lower costs, they increase competitive pressures among goods retailers now that inventories have been built up again.

As demand starts to soften, particularly for goods, more data, surveys and company guidance point to a greater likelihood of discounting to come in the months ahead, while prices are already starting to correct lower for some products, such as used vehicles.

For those looking for good news on inflation in 2023, dropping goods prices could prove to be a source of comfort, particularly if prices correct sharply. Of course, other factors may keep inflation rates elevated over the course of the next year – from food and energy prices to services demand and rental increases. This near-term shift also doesn't tell us anything about some of the more recent structural changes which may result in inflation settling at a higher rate than pre-pandemic, but in the near term downside surprises in goods inflation should make for better headlines.

*This is a Free to View version of a report with the same title published on 14-Nov-22. Please contact your HSBC representative or email AskResearch@hsbc.com for more information.*

# Supply chains easing up

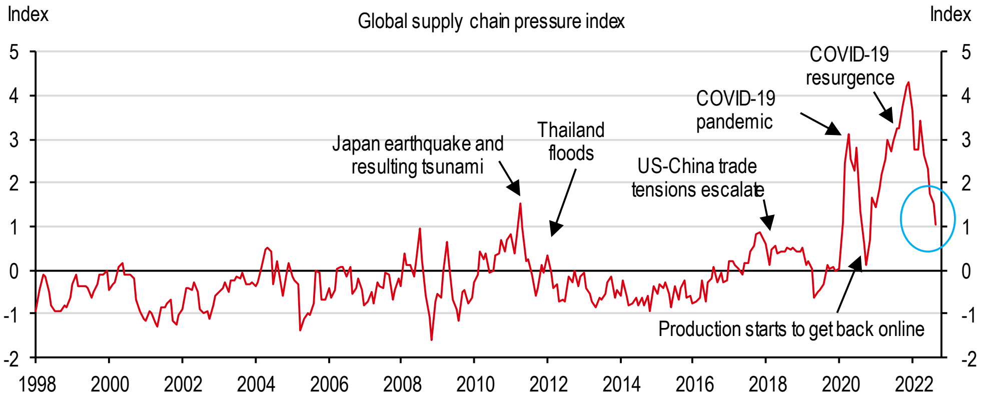
- The worst of the pandemic-related supply chain pressures look to be over…
- …with congestion at ports abating, container backlogs declining and freight rates tumbling…
- …while input shortages also seem to be easing, notwithstanding another big trade shock

## Pressures unwinding

**Logistics and demand**

After more than two years of unprecedented global supply chain disruption, it appears as though the worst of the pandemic-driven logistics challenges and input shortages are behind us. Already, global supply chain pressures – as measured by the Federal Reserve's index – have eased significantly, reaching a 22-month low in September 2022 (Chart 1).

**1. Global supply chain pressures have eased significantly**




Source: Federal Reserve. Note: Latest data point for September 2022.

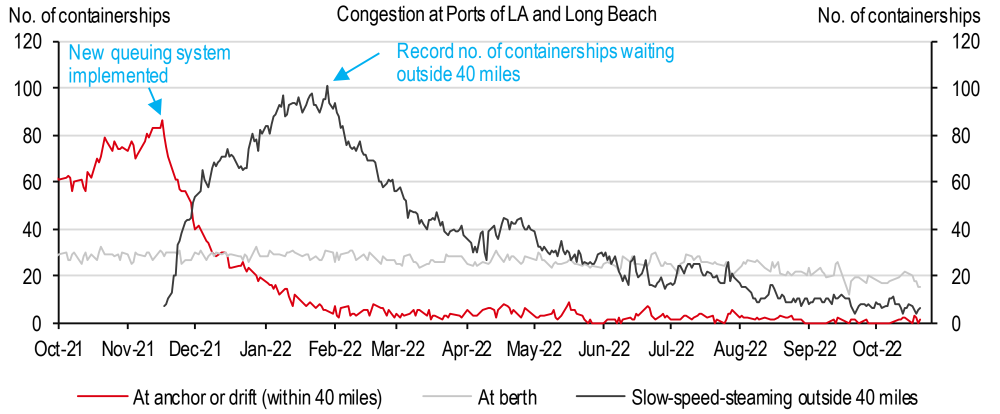
**Global trade is slowing down after a pandemic boom**

And, for the most part, this is to be expected. Global trade boomed over the past couple of years, supported in part by fiscal stimulus measures in Western economies that buoyed consumer demand. In fact, world trade volumes are still about 9% above pre-pandemic levels. But that demand is now starting to normalise and, along with stocked up inventories and slowing consumer demand as inflationary pressures and recessionary fears start to bite, could lead to the further unwinding of supply chain pressures in the coming months.

The improvement in logistics constraints has been notable. Congestion has eased markedly at US West Coast ports, where much of the container backlog was concentrated during the pandemic, mainly due to issues with landside logistics (e.g. labour and warehousing shortages). For example, the average vessel waiting time currently stands at around 0-5 days at the Port of Long Beach, down from 23 days as recently as April 2022, according to data from Hamburg-Sud. Onshore dwell times at that port have also improved, from over 30,000 containers waiting nine days or longer to be cleared at the beginning of November 2021 to around 8,300 containers on 25 October 2022.

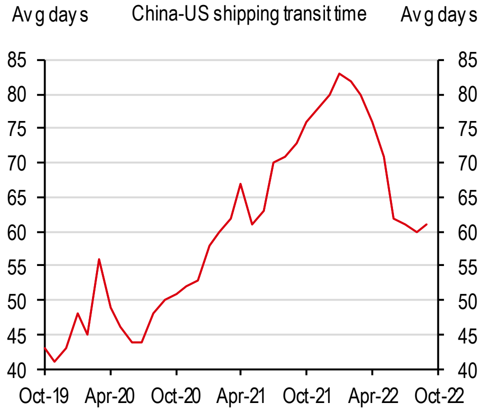
**Congestion is easing and transport costs are down as a result**

**2. Congestion at US West Coast ports is abating…**



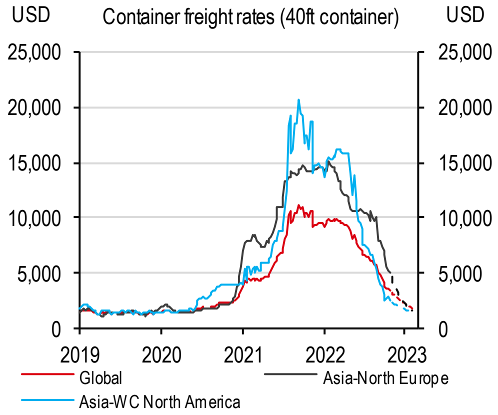

Source: Marine Exchange of Southern California. Note: Latest data point for 21 October 2022.

**3. International shipment times have also been improving…**




Source: Freightos. Note: Latest data point for September 2022. Data for Jan and Feb 2022 are estimated.

**4. …and container freights could soon be at pre-pandemic levels**




Source: Refinitiv Datastream, HSBC. Dotted lines show HSBC projections based on recent pace of w-o-w declines.

Moreover, the time taken to send a shipment from China to the US has declined to around 60 days on average in recent months, down from a peak of over 80 days at the beginning of this year, according to data from Freightos (Chart 4). And although this is still higher than the 40-50 days typically encountered pre-pandemic, it is a welcome sign that logistics congestion and backlogs are improving.

Some of these improvements have been as a result of reduced demand for goods allowing supply chain pressures to ease, but this combination of supply and demand factors has meant that freight rates have tumbled in recent months. For example, global container spot freight rates are down nearly 70% from their pre-pandemic peak, while costs are down around 65% and nearly 90% on the Asia to North Europe and Asia to the West Coast of North America trade routes, respectively. And if we forecast out the current pace of w-o-w declines (which seems plausible given that we've just been through peak shipping season), container freight rates on these key trading lanes could reach pre-pandemic levels in Q1 2023, if not earlier (Chart 4).

*The full note contains a look at whether there is further easing to come to supply chains as consumer demand continues to slow and as additional vessel capacity comes online in 2023. However, HSBC analysts caution that we are out of the woods as supply chains remain disrupted for some companies and sectors. Please contact your HSBC representative or email [AskResearch@hsbc.com](mailto:AskResearch@hsbc.com) for more information.*

# Any impact on inflation?

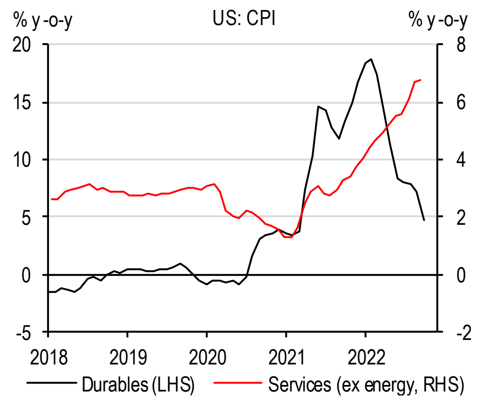
- Goods inflation has plenty of scope to fall…
- …as supply chain easing lowers costs and increases competition…
- …particularly if demand softens and pricing power wanes

## The state of inflation

**Durable goods prices fell in the US in October**

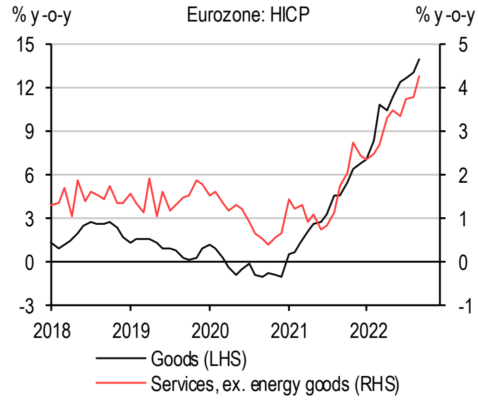
With inflation elevated in much of the world, goods prices have played a key role in pushing overall price much higher in the course of 2021 and 2022. But with supply challenges easing, will this be enough to lower inflationary pressures? There's already been a turn in US durable goods inflation, which printed a sharp m-o-m fall in October, but it isn't the same story elsewhere, at least yet.

**5. US CPI shows a big divergence between goods and services…**




Source: Refinitiv Datastream

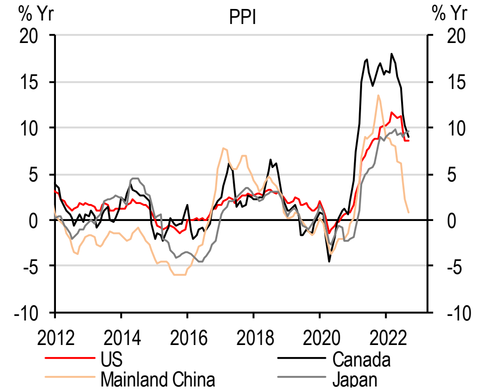
**6. …but no such break in Europe, for now**




Source: Refinitiv Datastream

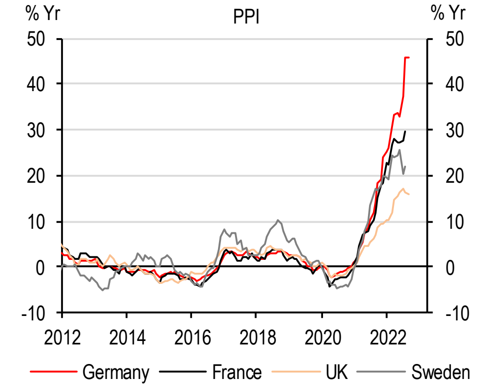
Energy prices may be a key part of this divergence, meaning that PPI inflation in the eurozone sits at over 40% y-o-y, while it is now under 10% y-o-y in the US. However, input cost challenges persist across the world, with higher energy and wage bills still impacting firms.

**7. Firms are still seeing high input costs…**




Source: Refinitiv Datastream

**8. …particularly in Europe**

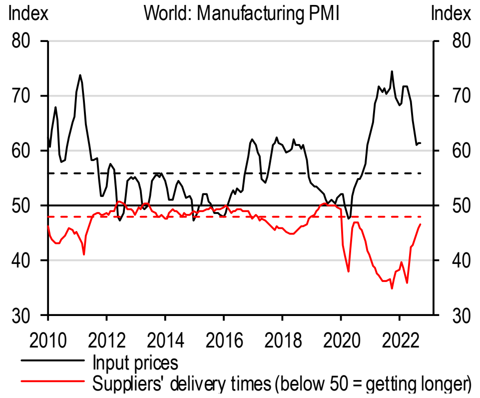



Source: Refinitiv Datastream. Note: Germany's PPI data are influenced by energy firms being included.

**Leading indicators suggest price pressures may be easing up**

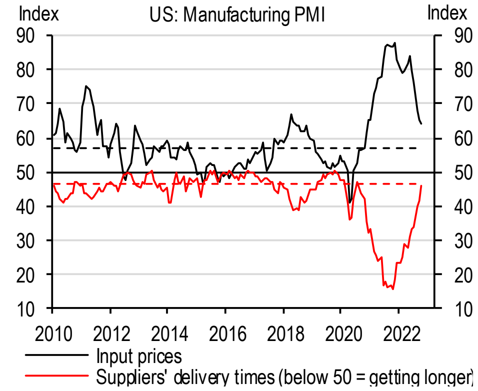
That said, many input price data are starting to fare better, at least in part due to the improving supply-side improvements many firms are seeing. The PMI data have shown a significant improvement in the past few months, with input price indices coming down as supply challenges lessen. Whilst input price pressures remain intense, they may be fading somewhat.

**9. Delivery times and price pressures are easing…**




Source: S&P Global. Note: Dotted lines show 2010-19 averages

**10. …quite quickly in much of the world**




Source: S&P Global. Note: Dotted lines show 2010-19 averages

## What are the scenarios?

In 2023, the reasons for a slowdown in goods inflation are building. Improvements in supply chains and weaker consumer demand are leading to a world where inventories are higher, discounting is more likely and input costs for businesses are lower. All in all, this should mean a lower rate of goods inflation, and possibly even goods deflation in the course of the year.

*The full note contains a further look of the inflation picture to get a sense of whether supply chain easing can impact inflation materially. In other words, whether inflation is demand or supply-driven; whether retail inventories will affect pricing or whether competition will matter as well as a discussion of the possible scenarios for inflation in 2023. Please contact your HSBC representative or email [AskResearch@hsbc.com](mailto:AskResearch@hsbc.com) for more information.*

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2 All market data included in this report are dated as at close 10 November 2022, unless a different date and/or a specific time of day is indicated in the report.

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