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Western European Indicators and Insights

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UK: Manufacturing contracting?

Providing a fifth successive clear downside surprise, the headline manufacturing PMI for July fell below the key 50 mark for the first time since September 2009. Indeed, the headline dropped 1.5 points (to 49.1), ie similar to the average drops in a sequence of what is now five successive declines, leaving it some two points below its long-term average. Indeed, the severity of the slump of late (down over 12 points since February) is looking more and more reminiscent of the tumble seen in late-2008.

Underscoring the marked turnaround from the strong start made to the year, growth in output reached a near-standstill in July following the steepest decline in new orders for over two years, while employment fell for the first time since March 2010. This all looks to be a result of a softening in the key factors that were supporting growth at the beginning of the year, namely inventory rebuilding, strength in global growth and stable domestic demand, albeit the relative impact of each being unclear. Regardless, the weakness in sterling is providing less support, both because of the softer global backdrop and due to fact high import prices have added to the inroads into domestic spending power. In regard to the latter, however, price pressures eased further in July, as input and output cost inflation eased to the weakest rates since December 2009 and last November respectively, with the lengthening in supplier delivery times pointing to further such easing ahead.

Of some solace, other alternatively-sourced survey data (such as those from the CBI) are not reporting as clear a softening in factory sector activity as these PMI numbers. Regardless, it is clear even from these other surveys that manufacturing has slowed discernibly, with the still soft pound unable to protect the UK from a softer global backdrop, the question being the extent to which softer domestic conditions (linked to the budget cuts) may be making matters worse. While the debate on monetary policy may not develop much as the BoE is very much seen being on hold well into next year, data such as these PMI numbers will intensify the debate regarding the speed and timing of budget consolidation measures in the UK.