Coronavirus hits UK supply chains, overshadowing better PMIs

The latest UK manufacturing PMI may have risen, but it masks some stark trends below the surface that indicate supply chains are taking a hit from Covid-19

Source: iStockphoto

Don't be fooled - manufacturing is suffering Covid-19 impact

There are two interesting stories in the latest UK purchasing managers indices, published by IHS Markit/CIPS.

Firstly, manufacturing supply chains are feeling the hit from the coronavirus. Production did rise in February – at 51.9, the manufacturing PMI is now the highest it has been in almost a year. But firms are reporting that stocks of inputs are dwindling, meaning it is taking longer to make deliveries. This follows a number of reports from companies that they are facing disruption to supplies of intermediate goods/components from China in the wake of factory closures.

Slightly alarmingly, the nine-point drop in the supplier delivery component of the PMI – a sign that deliveries are taking longer – is the sharpest month-on-month slide in the survey's history (since 1992).

There are two interesting stories in the latest UK PMIs. Firstly, manufacturing supply chains are feeling the hit from the coronavirus. But the more relevant for the Bank of England – is that the services PMI continues to point to healthier growth

In normal times, an increase in supplier delivery times would be interpreted as a positive signal. It is taken as a signal that firms are grappling with more orders, such that it is taking longer to fulfil them. In this case, though, the rationale is rather less positive – and suggests that not all of the rise in the manufacturing PMI is for 'good' reasons.

One caveat though is that the PMIs can overstate the impact of sudden shocks. The surveys simply tell us how many firms are reporting deteriorating levels of stocks/delivery times, but not necessarily by how much. Either way, it suggests the sector could face a challenging couple of months and we could see a short-term hit to production as a result.

Uncertainty clouds outlook for improving services industry

The other interesting story – and the one more relevant for the Bank of England – is that the services PMI continues to point to healthier growth. While a little lower than the January reading, the services PMI remained at the respectable level of 53.3, and is consistent with a "greater willingness to spend" according to the Markit/CIPS press release.

But there are questions surrounding how long this renewed optimism can last, or to what it extent it will translate into the official activity data over the next few months. While we are likely to see an increase in growth during the first quarter, the ongoing uncertainty surrounding UK-EU trade talks will continue to inhibit investment – particularly given there could be big changes to the way Britain trades with Europe from 2021.

We're a little cautious in assuming we will see a big increase in growth over the next few months. But even so, we think the Bank of England will be comfortable with keeping rates on hold for the time being.

Don't forget policymakers have only pencilled in 0.2% growth for the first quarter, after the flat reading for the final quarter of 2019. That suggests that activity doesn't need to rebound much for policymakers to be content with keeping rates where they are.

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