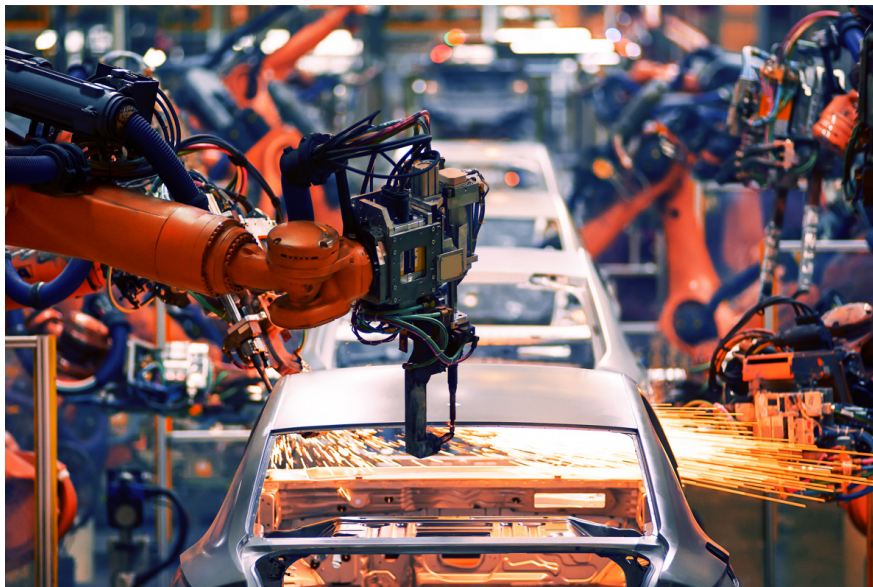


Snap | 23 May 2023

Eurozone PMI dropped in May due to manufacturing contraction

The composite PMI fell from 54.1 to 53.3 in May, which is the first decline since October last year. The divergence between services and manufacturing is growing, with services inflation accelerating again. The latter is the main concern for the European Central Bank



Source: Shutterstock

The PMI continues to point to decent economic growth, but the first decline in the index in more than half a year is indicative of the weakening manufacturing sector. The decline in the manufacturing output PMI from 48.5 to 46.3 puts it further into contraction territory. New orders continue to fall and backlogs of work are becoming smaller, adding to output concerns in the manufacturing sector.

For services, demand continues to be rather strong. The services PMI still indicates strong output growth at 55.9, but the index did come down from 56.2 in April. New business continues to grow for the service sector and demand is buoyed by a faster increase in wages. As wages are also the most important input cost for services, this has caused price expectations to increase again.

May's PMI release confirms that concerns about elevated core inflation should centre around

services, while goods inflation is set to ease markedly from here on. The economy continues in a 'muddling through' phase, as the stagnation seen around the turn of the year has not given way to a strong recovery. The strong services performance and subsequent inflation pressures will likely keep the ECB on its toes heading into the summer as any impact on overall inflation unfolds.

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