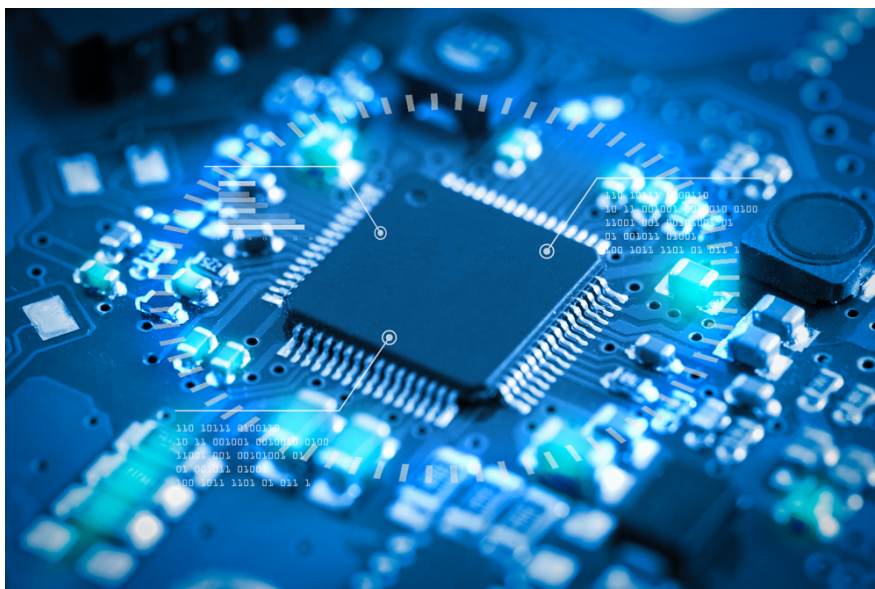


US: Hungry for chips

The manufacturing ISM fell in April as the global semi-conductor chip shortage hit output and orders throughout supply chains. With demand looking so strong and inventories so low, corporate pricing power is back and the risks of higher, more prolonged inflation becomes greater



Supply constraints hurt output and orders

The US ISM manufacturing index has surprisingly fallen in April to 60.7 from 64.7 – the consensus was 65 and we had penciled in something a little higher given the readings from the regional surveys.

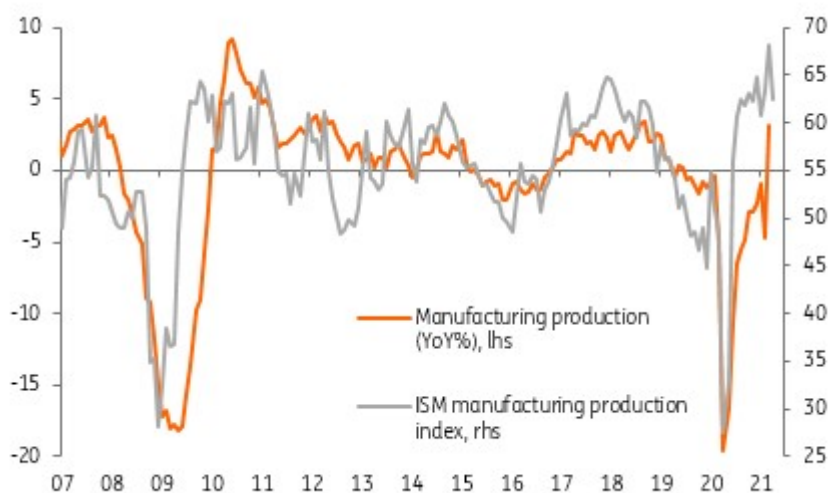
From this report it is clear that supply issues, centered on the global semi-conductor chip shortage, are constraining output growth. Auto makers have been very vocal about the difficulties this has presented and have already indicated that output could fall despite buoyant demand.

Other industries are also going to be impacted and it will have knock-on effects for companies throughout the supply chains – if you can't get enough chips, there is no point ordering other components in the same numbers

As a result, orders growth slowed and so did employment, but it is important to remember that

these are still very strong levels and manufacturing will make a strong contribution to the economic expansion this year. Indeed, while the rate of growth is slowing, all 18 industries classified as being manufacturing recorded rising output levels.

US ISM manufacturing output survey versus actual official output data



Source: Macrobond, ING

Pricing power is back, risking more inflation

Assuming these supply constraints get resolved in coming months we should see a sharp bounce-back in output, orders and employment to what will be record levels. After all there is still significant stimulus fueled domestic demand in the economy with another \$4tn of government spending/investment planned by President Biden. Meanwhile, export markets should strengthen as Covid containment measures are eased in response to effective vaccination programs.

The downside is that these supply-related constraints in the economy mean inflation pressures will continue to build. The ISM prices paid component rose to its highest level for 13 years, but the bigger issue for the Federal Reserve is likely to be the prospect that firms increasingly pass this onto consumers and we see higher, more persistent CPI and PCE deflator readings than the Fcentral bank is currently projecting.

Today's report showed that the backlog of orders is at an all-time high while customer inventories remain near record lows, which is the story every manufacturer wants to hear. It also means pricing power and the very real risk of inflation with surveys from the Philly Fed, the Empire manufacturing survey and the NFIB small business survey already starting to flash warning signals.

Author

James Knightley

Chief International Economist, US

james.knightley@ing.com

Disclaimer

This publication has been prepared by the Economic and Financial Analysis Division of ING Bank N.V. ("ING") solely for information purposes without regard to any particular user's investment objectives, financial situation, or means. *ING forms part of ING Group (being for this purpose ING Group N.V. and its subsidiary and affiliated companies)*. The information in the publication is not an investment recommendation and it is not investment, legal or tax advice or an offer or solicitation to purchase or sell any financial instrument. Reasonable care has been taken to ensure that this publication is not untrue or misleading when published, but ING does not represent that it is accurate or complete. ING does not accept any liability for any direct, indirect or consequential loss arising from any use of this publication. Unless otherwise stated, any views, forecasts, or estimates are solely those of the author(s), as of the date of the publication and are subject to change without notice.

The distribution of this publication may be restricted by law or regulation in different jurisdictions and persons into whose possession this publication comes should inform themselves about, and observe, such restrictions.

Copyright and database rights protection exists in this report and it may not be reproduced, distributed or published by any person for any purpose without the prior express consent of ING. All rights are reserved. ING Bank N.V. is authorised by the Dutch Central Bank and supervised by the European Central Bank (ECB), the Dutch Central Bank (DNB) and the Dutch Authority for the Financial Markets (AFM). ING Bank N.V. is incorporated in the Netherlands (Trade Register no. 33031431 Amsterdam). In the United Kingdom this information is approved and/or communicated by ING Bank N.V., London Branch. ING Bank N.V., London Branch is authorised by the Prudential Regulation Authority and is subject to regulation by the Financial Conduct Authority and limited regulation by the Prudential Regulation Authority. ING Bank N.V., London branch is registered in England (Registration number BR000341) at 8-10 Moorgate, London EC2 6DA. For US Investors: Any person wishing to discuss this report or effect transactions in any security discussed herein should contact ING Financial Markets LLC, which is a member of the NYSE, FINRA and SIPC and part of ING, and which has accepted responsibility for the distribution of this report in the United States under applicable requirements.

Additional information is available on request. For more information about ING Group, please visit www.ing.com.