Investec Manufacturing PMI® Ireland

Economics | Monthly

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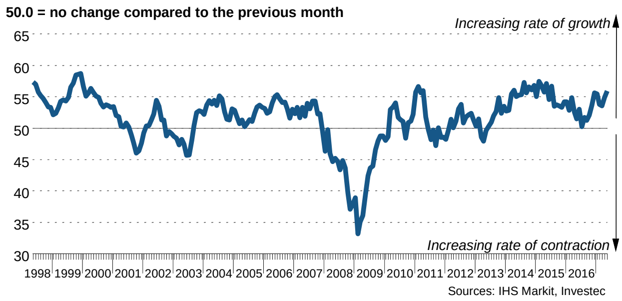
Output growth quickens to 22-month high

Summary:

Growth in the Irish manufacturing sector strengthened further during May. Improvements in client demand led to higher new orders, which in turn fed through to growth of production. Confidence regarding future output levels also picked up, with positive expectations encouraging firms to take on extra staff.

Investec Purchasing Managers' Index®:



The seasonally adjusted Investec *Purchasing Managers' Index® (PMI®)* – an indicator designed to provide a single-figure measure of the health of the manufacturing industry – rose to 55.9 in May from 55.0 in April to signal a marked improvement in business conditions. The health of the sector has now strengthened on a monthly basis throughout the past four years, with the latest improvement the greatest since July 2015.

The rate of growth in Irish manufacturing output quickened for the second month in a row and was the sharpest in 22 months. Respondents linked higher output to rising new orders and improving economic conditions.

New business also rose at a faster pace in May amid reports of stronger client demand. New export orders, on the other hand, rose at a weaker pace than in April, albeit one that was still sharp.

Rising new orders was the principal cause of a return to growth in backlogs of work following a marginal reduction in April, while also causing a further decline in stocks of finished goods as firms used inventories to help fulfil orders. That said, the sharp rise in production meant that inventories of finished goods fell only fractionally over the month.

Manufacturers increased their purchasing activity in line with higher production requirements. Moreover, the rate of growth was the joint-fastest in two years. The sharp rise in input buying was insufficient to prevent a further depletion of stocks of purchases, however, as items were used in the production process.

Rising demand for inputs imparted pressure on capacity at suppliers to the manufacturing sector. As a result, delivery times lengthened at a solid pace. Panellists also mentioned shortages of some raw materials.

Firms are broadly confident that output will continue to rise over the coming year, with optimism linked to predictions of new order growth amid stronger economic conditions. Moreover, sentiment rose to a three-month high.

Positive expectations led manufacturers to take on extra staff in May, the eighth month running in which job creation has been recorded. The pace at which employment rose was the fastest in two years.

Input costs continued to rise sharply, although the rate of inflation eased for the third consecutive month from February's recent peak to the weakest in the year-to-date. Output prices also increased at a slower pace, with the rate of inflation at a three-month low. Where charges rose, this was linked by panellists to the passing on of higher input costs.

Investec Contact Details: www.investec.ie Investec.Economics@investec.ie +353 1 421 0496
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IHS Markit, Henley on Thames, Oxon RG9 1HG, UK Tel: +44 1491 461000 Fax: +44 1491 461001 e-mail: economics@ihsmarkit.com

Comment:

Commenting on the Investec Republic of Ireland Manufacturing PMI survey data, Philip O'Sullivan, Chief Economist at Investec Ireland said:

"The latest Investec Manufacturing PMI Ireland report shows a strengthening in the rate of growth in activity in May, with the headline PMI improving to a 22 month high of 55.9.

"Manufacturers reported faster growth in New Orders (to a three month high), with roughly twice as many respondents signalling a rise in new business as opposed to those who recorded a fall. While the pace of expansion in New Export Orders moderated in May, it was still substantial and much faster than the series average.

"Given the improving demand profile, it is no surprise to see firms step up their buying activity, with the rate of growth in Quantity of Purchases strengthening to the joint-fastest in the past two years. Firms have been using Stocks of Finished Goods to help meet client orders, but with the rate of depletion in this index moderating to the slowest in the current seven month sequence of declines and the brighter international backdrop we suspect that manufacturers may be about to start investing in growing inventories once more. It's a similar situation for Stocks of Purchases, where a marginal decline was also recorded in May.

"On the margin side, the rate of increase in Input Prices cooled to the slowest in the year to date. However, it remains substantial and therefore we are unsurprised to see firms hike Output Prices (for a 12th successive month), presumably in a deliberate move to protect margins. This strategy appears to be paying off, with the Profits index posting its first above-50 reading in the year to date.

"Apart from signs of higher investment in inventories, another indication of firms' confidence in the outlook is the Employment index, which expanded at its fastest pace in the current eight month sequence of growth. In spite of these increased resources, Backlogs of Work returned to growth in May, a factor that presumably explains the improvement in the Expectations of Future Output index (to a three month high) after the eight month low that was recorded in April.

"Last month we outlined our belief that "the outlook for Irish manufacturing firms remains positive, supported by the improving international backdrop". After estimated growth of 3.1% in 2016 we forecast that the global economy will expand by 3.6% this year and by a further 3.9% next year (which would be the best annual GDP growth rate for the world economy since 2011) so, given such a supportive profile, we would anticipate further strong Manufacturing PMI readings over the coming quarters."

For further information please contact:

IHS Markit
Andrew Harker, Senior Economist
Telephone +44-1491-461-016
Email andrew.harker@ihsmarkit.com

Joanna Vickers, Corporate Communications
Telephone +44-207-260-2234
Email joanna.vickers@ihsmarkit.com

Investec
Philip O'Sullivan, Chief Economist
Telephone +353-1-421-0496
Email philip.osullivan@investec.ie

Ronán Roche, The Reputations Agency
Telephone +353-1-661-8915
Email ronan@thereputationsagency.ie

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Notes on Data and Survey Methodology

The Investec Republic of Ireland Manufacturing PMI® is based on data compiled from monthly replies to questionnaires sent to purchasing executives in around 285 industrial companies. The panel is stratified by GDP and company workforce size. Survey responses reflect the change, if any, in the current month compared to the previous month based on data collected mid-month. For each of the indicators the 'Report' shows the percentage reporting each response, the net difference between the number of higher/better responses and lower/worse responses, and the 'diffusion' index. This index is the sum of the positive responses plus a half of those responding 'the same'. Diffusion indexes have the properties of leading indicators and are convenient summary measures showing the prevailing direction of change. An index reading above 50 indicates an overall increase in that variable, below 50 an overall decrease. IHS Markit do not revise underlying survey data after first publication, but seasonal adjustment factors may be revised from time to time as appropriate which will affect the seasonally adjusted data series.

The Purchasing Managers' Index® (PMI®) is a composite index based on five of the individual indexes with the following weights: New Orders - 0.3, Output - 0.25, Employment - 0.2, Suppliers' Delivery Times - 0.15, Stock of Items Purchased - 0.1, with the Delivery Times Index inverted so that it moves in a comparable direction. The PMI is designed to show a convenient single-figure summary of the health of the manufacturing sector.

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