

# UK manufacturing

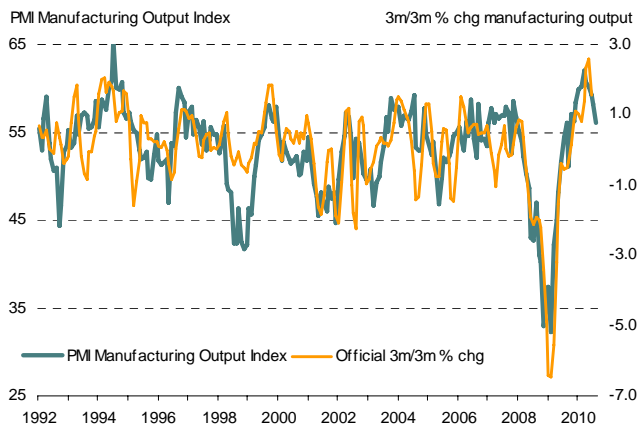
## Manufacturing expansion surge shows signs of fading

- **Manufacturing output and order book growth slow sharply in August.**
- **Current production achieved only by firms eating into backlogs of work, meaning capacity and employment may be scaled back again.**

### Output growth falls further from recent peak

The latest Markit/CIPS Manufacturing PMI showed that output growth continued to slow from the fifteen-and-a-half year high recorded back in March. Comparisons with official manufacturing data suggest that the recent downturn in the PMI Output Index is consistent with output growth (measured on a quarterly basis) slowing from the peak of 2.6% seen in May to around 0.8%.

### Manufacturing output



Sources: Markit; ONS.

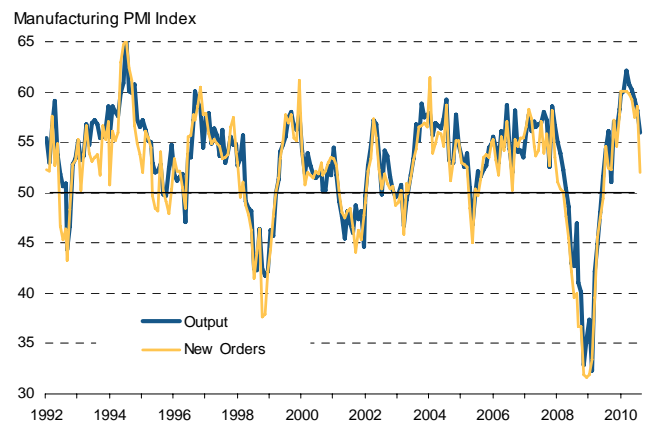
The survey therefore also suggests that the manufacturing sector's contribution to GDP will have moderated in Q3, with quarterly growth slowing from the buoyant 1.6% pace seen in Q2 (the best quarter for over a decade) to perhaps less than 1% for Q3 as a whole, providing the Index does not change substantially in September.

### Outlook darkens

Although growth has slowed, the recent data indicate that the goods-producing sector should nonetheless help stimulate further GDP growth in Q3. However, the outlook for later in the year has darkened.

First, the rate of growth of new orders slowed even more sharply than output in August (the steepest monthly fall in the New Orders Index for six-and-a-half years). A particularly weak reading for consumer goods (total new orders almost stagnated, despite a modest rise in overseas orders) corroborates the weakness signalled for the consumer sector by the YouGov/Markit Household Finance Index, which has shown confidence to have fallen since the emergency Budget.

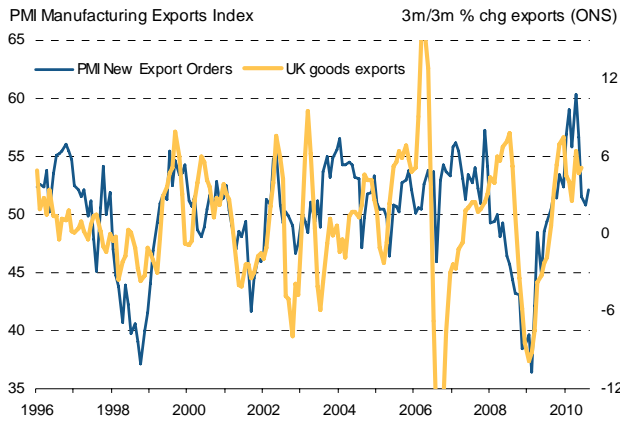
### Output and order books



It is not unprecedented for the PMI's output and new orders indices to diverge in such a way, and for output to even continue rising in coming months, but the severity of the drop in the New Orders Index is a concern and suggests that the slowdown in output has further to run.

Second, the strength of output growth earlier in the year was to a large extent fuelled by a surge in global trade flows, which benefitted UK exporters. The PMI survey's New Export Orders Index hit a record high in April but has since fallen sharply, recovering only slightly in August from the near-stagnation signalled in July, as growth has slowed in many trading partners in recent months.

**Manufacturing exports**



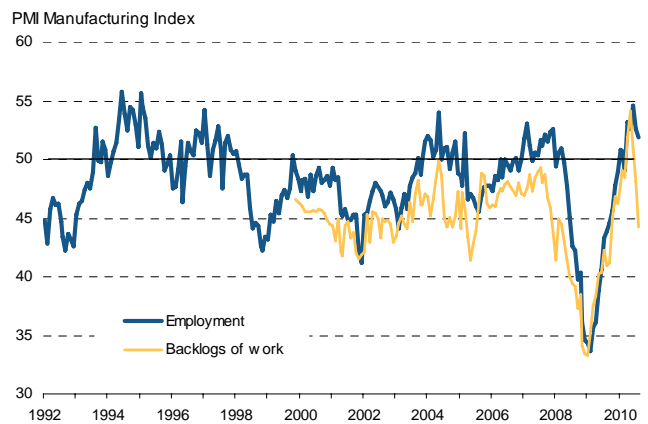
Sources: Markit, ONS.

Third, backlogs of work fell for the second month running in August, with the rate of decline accelerating markedly. Thus, while the surge in worldwide manufacturing growth earlier in the year led to a record rise in backlogs, as UK producers struggled to meet rapidly rising demand (linked in part to inventory rebuilding), the increase in production in August was achieved only through manufacturers eating into these previously-placed orders. Unless inflows of new orders pick up again, output growth is likely to slow further in coming months.

**Employment at risk**

The backlogs of work data also have an implication for employment. The record rise in backlogs of work earlier in the year helped generate the fastest job creation since 1995, according to the PMI indices. The recent fall in backlogs and slower inflows of new business suggest that companies will be more circumspect about expanding capacity, and may even begin to trim workforces again.

**Employment and order books**



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