

Is UK Manufacturing Off Life Support

The UK manufacturing industry appears poised to rebound. The recent PMI report is clear testimony to manufacturing's improved prospects, and points to further progress in the months ahead. The index has risen 7 point from its post September 11 trough of 42.9. In its most recent monthly trends survey the CBI recorded the biggest rise in output optimism (over the previous three months) on record.

After a 0.5% contraction in January, manufacturing output rose by 0.4% during February. This was the first rise for nine months. The main reason for the rise output in February was a sharp increase in pharmaceutical production. Output in the chemicals and man-made fibres area rose 2.4% on the month. More encouragingly, production of electrical and optical equipment rose 0.5%. This sector of UK industry was particularly hard hit by the global downturn.

Overall, manufacturing conditions remain weak. On the year, output declined 5.8%, after a 6.2% contraction in January. Industrial production, which includes utilities and mining, was also weak in February, declining 0.2% on the month and 5.1% on the year. Nonetheless the data are encouraging and if current improvement in surveys is maintained then Q2 should see the first rise in industrial production for nearly two years. However, it is likely to be well into the second half of the year before the annual growth rate turns positive.

While manufacturing is showing signs of recovery we do not feel that this will hasten any decision by the central bank to hike interest rates. Next week's budget is probably much more crucial in terms of the timing of a BoE hike. We still believe that, despite the strength of consumer spending, that the central bank will wait until the second half of the year to hike rates. In comments made late this week BoE Governor Sir Eddie George remained cautious on the economy saying that the while the global economy is in the early stages of recovery there is no guarantee that the early momentum will be maintained. The strength of expansion is still uncertain and it is possible, even quite likely that the consumer will cool of its own accord.

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