
S&P Global

Market Intelligence

PMI Insights for Sept. 2023

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Call Participants

ATTENDEES

Andrew Harker

Paul Smith

Phil Smith

Unknown Attendee

Presentation

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You're listening to the economics and country risk podcast from S&P Global Market Intelligence. In each episode, our experts will provide you with the where, how and when to make decisions that transform your business.

Paul Smith

Hello. Welcome to our latest PMI-based podcast from S&P Global Market Intelligence. I'm Paul Smith, Economics Director in the team that produces PMI figures for over 40 countries and key regions across the world. Now today's podcast is one that focuses on the economic impacts of weather and how PMI and the survey data can be useful at picking up these events either in a timely fashion or helping us to assess behavioral changes as nations transition to greener and more efficient forms of energy.

Our thematic choice for this episode has largely been driven by the observation that 2023 has seen some strong impacts from extreme weather across the world, be it unusually long and intense wildfires in Canada, to extreme heat in Southern Europe to dry climate heavily impacting crop yields in Southeast Asia and Australia. Outside of the tragic human impacts of these events all have, in some way or another, shown up in our PMI data.

Now joining me today to discuss some of these themes are 2 fellow economists from the PMI team. Firstly, we have our regular podcaster, Economics Director, Andrew Harker. And secondly, I'm joined by Phil Smith, Economics Associate Director with S&P. A warm welcome to you both. And Phil, if I could come to you first, maybe and ask you to give us an update on current PMI developments in Germany.

Phil Smith

Of course, yes, thanks very much for having me. So the situation in Germany, it's not great at the moment in terms of the direction of travel of the economy. The August composite PMI, which is a measure of the combined output of manufacturing and services sectors, fell to its lowest since May 2020. This was a result of a deepening downturn in manufacturing production combined with a renewed contraction in the services side of the economy. Services had previously been a support to the economy, but the PMI showed activity falling for the first time this year in August, which panelists told us was a result of a squeeze on customer budgets due to persistently high inflation as well as an uncertain general economic outlook, which is weighing on demand.

The PMI numbers tally with some actually pretty miserable official data out in the last few weeks as well. New orders -- factory new orders fell particularly sharply in July. Now this unwound a spike in orders in May, June when the data had been somewhat skewed by a jump in big ticket orders but the sharp drop in July in the official numbers brought that series back into line with what we're seeing in the PMI. And I suppose the big question at this point is where we're heading.

We're not in the business of making forecasts, but we can look at some of the sub-indices to get hints of where we might be heading in the coming months. The manufacturing new orders index pretty much stabilized in August, albeit at a very low level. We also saw manufacturers expectations tick up, albeit, again, remaining in pessimism territory. Now these could be signs the manufacturing sector is sort of reaching a bottom. Of course, it'd be wrong to draw strong conclusions on just one set of results. And so we'll have to look for the net release or see if those trends are continuing.

And we also saw services expectations tick up in August. But given the direction of activity and new business in that sector, I don't think you'll be seeing much of a recovery until perhaps the early part of next year.

Question and Answer

Paul Smith

That's really sort of background context. And it doesn't seem like a great outlook at the moment. And just my experience of working on the PMIs in recent years as one potential risk factor that's emerged more recently, it seems or more frequently has been how the Rhine River has tended to be in terms of water levels and things like that. Largely because of the importance of the Rhine to industries like the chemical sector and its potential impact on industrial performance. What's your current read of the situation? Any potential risks from where the Rhine is at, at the moment?

Phil Smith

But I think it's probably worth starting with a quick geography lesson for anyone who is saying you might not be familiar with the Rhine route through Europe. So it originates in Switzerland, where it passes through Basel then it moves northwards along with Germany, France, border passing through Strasbourg. It continues north through the west side of Germany passing through many key towns and cities, perhaps Cologne, Düsseldorf before it veers off West into the Netherlands, passing through Rotterdam, eventually entering into the North Sea.

Just from that list of place names, you can get a real sense of the importance of this river to industry across a large part of Europe. It's really wise what you say, when the transportation of a whole range of raw materials, oil products, coal, iron ore, yes, it's relied on by a huge number of manufacturers in Europe. With the Rhine problems start to arise when you get periods of low rainfall. Which leads levels on the river to start to drop, making it difficult for certain parts of the river to be navigated.

We saw this in 2018 and again briefly in 2022. We've had a situation where vessels couldn't carry for loads. And what this does is, obviously, it means greater and ever more vessels, each carrying a lighter load. So you get potentially a constriction on the amount of goods that can be delivered, thus impacting output. But also you get supply/demand imbalances in transport capacity, so surcharges start to rise. Now these sort of effects, they did come through in the survey data, not only for Germany, but for the Netherlands, too. So yes, it's something we've been aware of for some time.

Now in terms of the current context, what we're seeing this year, the Rhine at historically low levels for the time of year, both in February, March and then again in July, which got a lot of people quite nervous about where we're headed in the second half of the year when the river tends to be at its lowest historically. Heavy rainfall during July and into August actually saw the river level spike higher. And as we talk now, it's still slightly above its sort of recent historical average. So for the time being, things are looking okay, but it's certainly something worth watching for the rest of the year and beyond that as well.

Andrew Harker

Yes. It's really interesting to think of something like that. Natural impact of the ups and downs of the Rhine can have such an effect on industrial production in Europe. Something else that can have an impact on, say, supply chains and therefore, industrial production is flooding, which is maybe a bit more unpredictable as well. So I know, Paul, you noticed in Italy, there was some floods earlier this year, won't know which had an impact on the manufacturing sector. So it'd be good to get an update from you on what actually -- what are the main impacts there.

Paul Smith

You're right. It was really back in May, largely Northern Italy, in the areas where the River Po kind of flows through the opposite to the right equally starting in the ALPS region and then flowing through Northern Italy through a really important area like Emilia Romagna, a very important agricultural area for Italy. I think as much as 40% of Italy's food production comes from that kind of region. We've seen a period of exceptionally dry weather.

And then in May, there was something like 6 months of rainfall in 3 days, are very heavy. And you can -- it's such heavy rainfall on top of very dry soil, you have drainage challenges and then equally, rivers tended to outflow spillover banks, et cetera. And that led to what we picked up in our data with reports of roads and bridges collapsing, having issues around transportation for, like I say, quite an important area of Italy.

We tend to focus on initial impacts, but equally, they continue for many months afterwards sometimes. So this month, with our August PMIs, we found in the construction sector, we had people or constructors reporting. They were getting orders to repair damaged property from floods. And then equally in our services data, we had reports of food prices up largely, again, because of the adverse impact of flooding earlier in the year. And now that helped push cost inflation in the Italian services economy up to its high since April, which doesn't sound like too big a peak or a high, but of course, it just adds to a little bit of unexpected stickiness given where price inflation currently is in Europe.

So it's quite elevated to tick up. Just that to that view of a little bit of stickiness in what otherwise has been a recent downward trend in price inflation.

Andrew Harker

Yes. It's interesting, you're talking about agriculture there and food prices because another sort of naturally occurring weather event that we've got at the moment is El Niño is coming around again this year. And that, again, is going to have an impact on agricultural prices potentially. Normally, in an El Niño cycle, you'd see agricultural output decrease.

And so thinking back to our supply and demand economics 101, that would normally feed through to a higher price. It's potentially something else to watch out for when it comes to food prices, potentially a big issue for countries and consumers that are relying on -- or were exposed to changes in food prices.

That's something that our different teams within global intelligence and analytics are going to be looking at closely over the coming months or already looking at as well. So I encourage our listeners to look out for any research that comes out from our different teams across the world, looking at the specific impacts of El Niño on their regions as we go forward.

Paul Smith

I was having a look at that a couple of days ago, and there's some really great forward-looking stuff in there that I think really would help clients and users thinking about these potential impacts down the line. That's on potential for prices, one thing and we've hinted a little bit in our German discussion there about potential for disruption to output. Have you seen, Andrew, any other impacts of extreme weather impacting on current output levels around the world?

Andrew Harker

Yes, we'll move away from some European examples for now and look at Asia. Earlier this year, back in around June time, there was a real heat wave in Vietnam. And that caused quite a lot of power outages, which really impacted manufacturing production. It came through in our manufacturing survey for June and sort of really exacerbated the downturn that was going on in Vietnam at the time. And -- but even more recently, on a similar theme, our August data in Mainland China showed that there were some reports of extreme heat leading to shorter working weeks.

So yes, definitely having an impact on output when you get those sorts of extreme scenarios. It's worth saying, I think the Mainland China PMI data was above 50% this month. So it's showing still growth, but just maybe limiting the extent to which growth is being achieved at the moment when you get these sorts of events coming along.

Paul Smith

Obviously, we just talked a little bit there about current output. But inevitably, as these weather events become more frequent or more intense, companies also have to think a little bit forward into the future, really. Our Canadian panelist, for

instance, have been reporting in recent months that they're paying for a reduced frequency and intensity of wildfires in the coming year. Largely because they've seen the business impact. That may be an adverse impact on tourism numbers or something like that.

Equally, I guess, is also an investment angle to look at what isn't here as well potentially for mitigation against these climate impacts, but also how we're going to think about our transition to greener, more efficient energy consumption in the years ahead. And that's something I see quite often in our business outlook surveys, where we ask a bunch of forward-looking questions to our PMI panelists 3 times a year. I think the next release is in November.

So that'll be something definite to look out for. Like I say, let's pan this thing a little bit more ahead rather with the PMI, which is all about today's conditions. I think that's, for you, very big thing patiently listening to me and Andrew there discuss a few things. I know that in the U.K. at the moment, you've been doing some work where you've been serving households and their changing attitudes towards energy efficiency in their homes. Maybe you could expand a little bit more about your research in that area.

Phil Smith

Absolutely. So we've been collecting data for NatWest for the greener homes attitude tracker. And the name does give away a bit. But what that is exactly, it's a monthly survey of 1,500 U.K. individuals, representative sample of the population, so as intended to anticipate changes in consumer behavior and sentiment towards the green transition in the U.K. housing market, as you mentioned, Paul. It's a survey we've been running since May 2021. Yes, we've got about 2.5 years. So we start a bit of a pretty decent time series for that one now.

Paul Smith

It feels quite rare to have a time series in this kind of work and this kind of space. What's your latest results, what's the latest data points showing?

Phil Smith

The latest data points are for the second quarter. And what they showed is that at the moment, energy efficiency around the home is a nice-to-have feature. So we asked people looking to buy a house in the next 10 years, what factors are important. So 40% of people looking to buy a property in the next 10 years, so energy performance certificate rating. So that's essentially a measure of a property's energy efficiency.

The EPC rating was a very important factor in 40% of cases. So to give that some sort of context, 68% said that the cost of a property was a very important factor and 63%, the location. So the 40% is pretty sizable, but it's not up there with the likes of location and cost at the moment. We're also tracking plans for green home improvements. So around 1 in 5 homeowners that plan to make sustainable upgrades to their property in the next 12 months and around 2/3 said they plan to make upgrades in the next 10 years as a whole.

In terms of the items looking to install, the longer-term outlook, as you can imagine, it's more big-ticket items such as electric vehicle charging points and solar panels. It was cited by about 40%. And in the very near term, we're looking at smaller items. So energy meters are the #1 priority in the next 12 months.

Andrew Harker

It's really interesting to think about as someone who's buying a house at the moment, hopefully, then makes me think how much importance I put on the EPC rating. Given the EPC rating is pretty bad on the one I'm buying, obviously, not too much. But again, as you're saying, there's those mitigation of those improvements you can make to try and improve it once you're in there, can't you?

The one thing I was just wondering about is to what extent the recent pressures we've seen on cost of living have impacted the results because I think that's something that we're seeing, not just in the U.K. but all around the world is that those sort of cost of living pressures that have been quite acute really in the past year or 2 now. Has that really impacted on the results and how people feel about energy efficiency and the sort of improvements?

Phil Smith

Yes, it has. So as I mentioned, we have a decent amount of history now in the series, so we can really track changes in behaviors across time. So it takes us right back to the start of the series, really. In 2021, we saw a bit of an uplift in plans for improvement around the home, around the time of COP26. So it seems that event really raised awareness in the area of sustainability. Not long after that, we had the beginning of the war in Ukraine. I mean, all the issues around potential energy security worries in the U.K. and the potential for energy prices to spike higher in the future.

And that, again, we saw people react to that and bring forward their plans for making these changes. Of course, for a large part of the series, we saw a general upturn in awareness and plans for the future. However, when we reached the winter just gone, when energy prices started to spike like they did and inflation soared, it was noticeable that people are starting to really tighten their purse strings.

For the first time in the series history, we actually saw plans for sustainable home improvements suffer a bit of a setback. But yes, it definitely seems it's coming through in the data of this cost of living pressures, and making people think twice about what they can afford and if they really need to make changes right now. We have seen a slight recovery in the latest data, but we're not back to the level we were before the energy crisis restruct.

But interestingly, away from the housing side of things, we also track general actions that households are taking to tackle sustainability issues. And one thing we saw, again, over the winter just gone, was people were less considerate of the environment when shopping. We saw a drop in the proportion that said that they were considering the environment when doing their shopping. So it seemed that there was a turn away from that environmental consideration more towards choosing value over anything else. Yes, we are seeing some noticed effects in the data.

Andrew Harker

Yes, it's really interesting, although the difference of breakdowns and splits that we can get and how we can track those attitudes and actions over time. It's a really interesting report. So when is the next one, Phil? And when can we expect to see the next update?

Phil Smith

So I think the next one is early part of next year. We're looking at January for Q4 results. We'll keep an eye in January for those.

Paul Smith

Fantastic stuff. So I thank you for that. I think these types of surveys and understanding how solid and firm, of course, how their behavioral changes, understanding these trends is only going to grow in importance that we measure and evaluate our progress towards net 0 targets over the coming years.

Just summing up and coming back to our earlier PMI discussion. Just to reiterate the best way to see how weather impacts economies or indeed any other events is really to keep a careful abreast of our PMI data. Just to those who list new to our surveys and how our release schedule works, figures are usually released after the end of a reference month for manufacturing services and, in some instances, construction sectors across the world.

Although I will know in some instances, we actually released preview or what we call flash readings for several countries, regions around a week before the end of the month. This PMI data really is the first look at how economies are faring around the world on a monthly basis. So I guess just looking at the calendar, the next set of releases to watch out for is September 22. We'll be covering economic developments in Australia, Japan, the Eurozone, the U.K. and the United States. But for now, my thanks to Andrew and Phil for their contributions today after what is another useful, engaging discussion on the PMIs.

And of course, some of that wider research that we end up here at S&P Global. Please do head over to our PMI web page on the S&P Global website to see some of our other research and resources. But in the meantime, I look forward to chairing another PMI podcast later in the year.

Unknown Attendee

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