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A long way to go for a manufacturing recovery

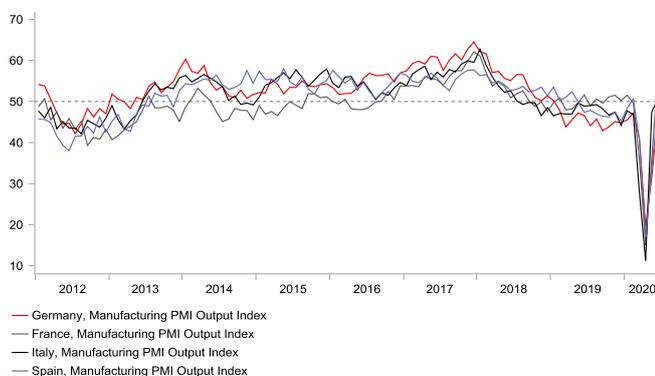
06 July 2020

Don't read too much into the PMI bounce

The steep fall in economic activity will naturally be followed by a something of a rebound as lockdown measures are eased. Last week's manufacturing PMIs for the main euro area countries all saw the manufacturing output index bounce back to around 50 (the breakeven mark). This may look like a sharp 'V shape' recovery at first glance but the PMIs, usually a reliable indicator, should be interpreted with caution as the economy recovers from such a steep plunge in output. The survey asks whether output has changed compared to the previous month and slight growth from a low base does not indicate a recovery.

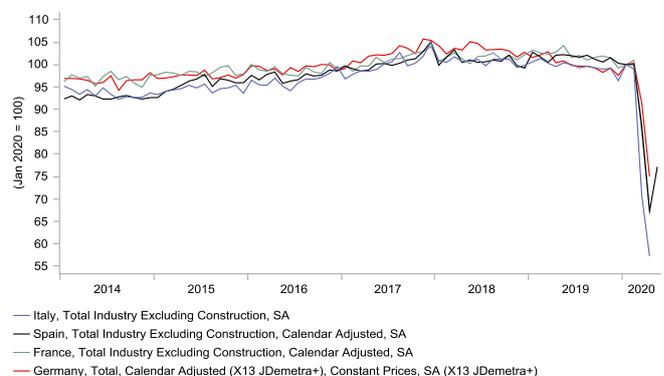
In fact, as lockdown restrictions were eased in May and June the balance of replies should have indicated a considerable expansion from the March/April low for activity. That the numbers remain at (or below) the breakeven mark, i.e. suggesting that output has remained steady, indicates that many respondents are probably considering a 'normal' level of activity as a baseline rather than the previous month.

MANUFACTURING PMIS: NOT A 'V'



Source: IHS Markit, MUFG Economic Research

INDUSTRIAL OUTPUT MAY FACE A LONG ROAD BACK



Source: National agencies, MUFG Economic Research

A limited recovery in industrial output

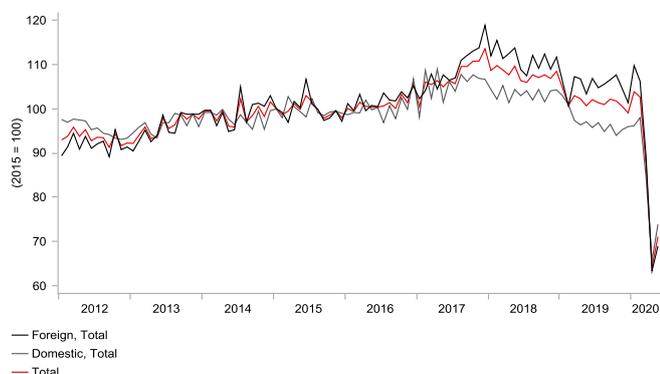
This week's industrial production figures for May will be a reminder of how far there is to go for a full recovery. There will naturally be some high monthly growth rates as the lockdown measures were eased, but the levels of activity are likely to remain well below the February numbers. German factory orders increased by 10% in May but the index remains 30% below its January 2020 level with a very similar picture in both domestic and foreign orders.

More timely data is showing a mixed picture. German truck mileage data through June has not been especially encouraging. Looking ahead, while the PMIs are problematic at the moment (and perhaps should be ignored entirely), other surveys are still relevant. The Ifo manufacturing expectations index increased sharply in June

suggesting that manufacturers are increasingly confident about the outlook.

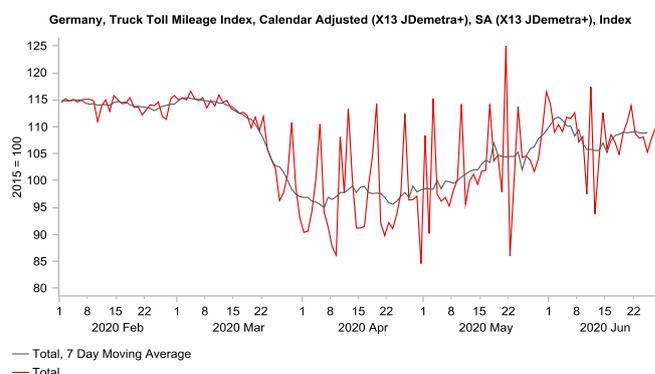
However, while some sectors of the economy will naturally recover more quickly than others, for some time there is likely to be a combined headwind for industrial output from weak global trade and lower productivity as a result of social distancing measures in the workplace. It's likely to be a long slog back for manufacturing.

GERMAN NEW ORDERS – MAY ‘RECOVERY’ WAS MUTED



Source: Statistisches Bundesamt, MUFG Economic Research

TRUCK MILEAGE SUGGESTS JUNE WAS TOUGH TOO

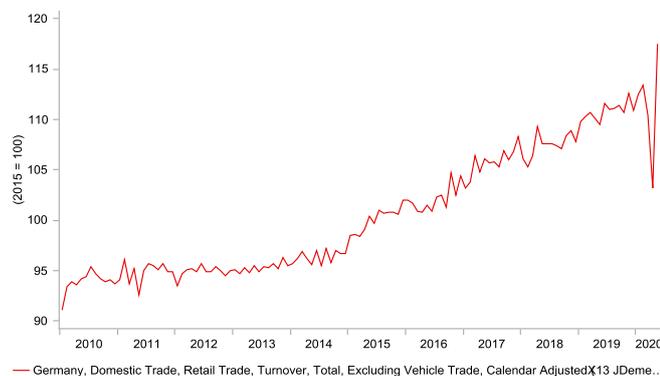


Source: Statistisches Bundesamt, MUFG Economic Research

Retail sales are more encouraging – but it is overall consumption that matters

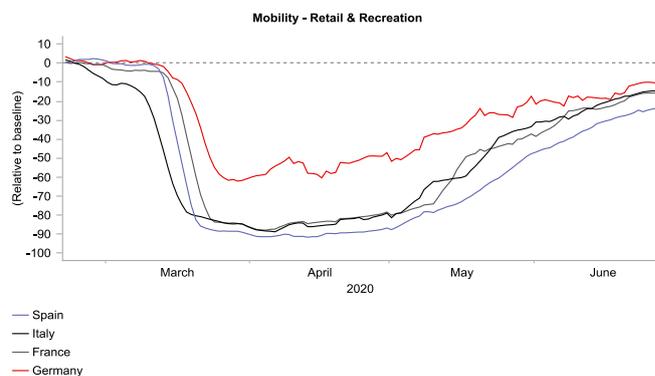
In terms of domestic demand, last week's German retail sales figures last week *did* show a genuine V-shape bounce, increasing by 13.9% in May and now exceeding the pre-virus levels. Germany has introduced a VAT cut from 1 July which should provide further support to retail sales.

GERMAN RETAIL SALES



Source: Statistisches Bundesamt, MUFG Economic Research

MOBILITY



Source: Google, MUFG Economic Research

It's not quite back to normal just yet, however – sales were boosted by internet shopping as some households continue to avoid the high street. There are plenty of things that can't be done online, of course. It is total consumer spending rather than just retail sales that will matter for GDP in Q2 and beyond. Persistently lower spending in bars, restaurants and on culture and recreation is clearly a risk. Data from Google shows that mobility in 'retail and recreation' did recover fairly quickly as lockdown measures were eased, but is now flattening below the pre-virus baseline as some people continue to avoid public places.

The imposition of fresh regional or local lockdowns in Germany at the end of June,

now also in Spain, is a reminder that the virus is not going away. A swift recovery to normal consumption levels is unlikely, and it might be a case of 'two steps forward, one step back' if regional flare-ups of the virus continue through the summer.

Over the medium-term, a lot will hinge on the labour market. Last week's data showed that unemployment rates have remained low as governments have stepped in to provide support. Unwinding these short term working schemes will be a delicate task. Unemployment rates will inevitably rise later in the year, but could easily soar if support is withdrawn too quickly.

KEY RELEASES AND MUFG FORECASTS – WEEK BEGINNING 6 JULY

Day	BST	Region	Indicator/Event	Period	Prev.	Cons.	MUFG
Mon 6 Jul	07:00	GE	Factory Orders MoM	May	-26.2	10.4(A)	-
Mon 6 Jul	08:00	SP	Industrial Production MoM	May	-28.1	14.7(A)	-
Tue 7 Jul	07:00	GE	Industrial Production SA MoM	May	-17.9	10.5	8.9
Fri 10 Jul	07:45	FR	Industrial Production MoM	May	-20.1	15.3	14.0
Fri 10 Jul	09:00	IT	Industrial Production MoM	May	-19.1	20.8	19.0

Source: Bloomberg

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