Manufacturing production slows worldwide

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Surveys published at the end of last week show that manufacturing output is falling worldwide in the wake of the downturn in the United States.

While the growth rate in the US remains positive, largely because of continued consumer spending and an expansion of employment in service industries, manufacturing industry is continuing its downward slide of the past 10 months.

According to the US Labor Department, a further 124,000 jobs were lost in US manufacturing last month, bringing the total job losses since last July to more than 670,000. This is the biggest reduction in any 10-month period since the recession of 1990-91.

Katharine Abraham, commissioner of the Bureau of Labor Statistics, said the jobs losses in factories during 2001 were “roughly equivalent” of those incurred in the recession a decade ago.

Even more significant is the fact that the pace of the decline appears to be accelerating. The National Association of Purchasing Management said that an index based on a survey of its membership came in at 42.1 in May compared to 43.2 for April. Anything below 50 is indicative of a contraction in activity.

The head of the NAPM's survey committee, Norbert Ore, said there was “no evidence of recovery in this month's report as the key indicators continue to decelerate at a faster pace.”

In Europe a survey of purchasing managers in the euro zone recorded the 13th month of decline and the second consecutive month in which the aggregate index came in below 50. In Germany, the index fell from 49.3 in April to 48.8 in May, in France the decline was from 49.4 to 48.1 and in Italy from 49.2 to 48.3.

The situation was no better in Britain where the Chartered Institute of Purchasing and Supply's survey of British manufacturing showed a decline in its index from 47.7 in April to 46.4, its lowest level since January 1999. British manufacturers maintain that the three-quarter-point cut in interest rates by the Bank of England since February are not enough because of the slowdown in the world economy.

The worsening international trend has been set in motion by the downturn in the US economy, which acted as the chief source of stimulus for the global economy in the last half of the 1990s. Since reaching growth rates of more than 5 percent in 1999-2000, the US economy slowed to an annual growth rate of just 1.3 percent in the first quarter of this year.

The chief factor has been the decline in investment spending as a result of falling profit expectations. But there is no relief in sight on this front. According to data published in *BusinessWeek*, analysts expect average earnings of companies in Standard and Poor's 500-stock index to fall by 12 percent in the first quarter, after dropping by 6.5 percent in the first three months of this year.

Judging from the latest comments by chairman Alan Greenspan, it seems that the US Federal Reserve Board does not expect a revival in capital investment in the immediate future.

Speaking to the New York Economic Club last month, Greenspan said that with investment capacity in high-tech manufacturing industries rising by nearly 50 percent last year, a “temporary glut” in these industries and a fall in prospective rates of return were “inevitable at some point.” The adjustment, however, had occurred “much faster than most businesses anticipated.”

Greenspan indicated that the initial cause of the slowdown appeared to be cutbacks in production as high inventory stocks were liquidated. At some point this liquidation would come to an end, leading to increased demand, thereby boosting production.

But that is not all there was to the picture. “The demand for capital equipment, however, is more problematic. Despite evidence that expected rates of return on the newer technologies remain high,

investment in equipment and software has slowed," Greenspan said.

The fall in demand, he continued, appeared to have gone beyond the necessary adjustment resulting from over-capacity "reflecting a deterioration in short-term profitability and cash flows." The pressures on profit margins and cash flow, he noted, have been "unrelenting."

The emergence of a simultaneous slowdown in the economies of the US, Europe and Japan has also resulted in the emergence of conflicting tendencies in international currency markets, complicating the situation facing central banks and governments.

The downturn in the US should be expected to lead to a fall in the US dollar against the euro. But, on the contrary, the euro has continued to remain weak against the US currency, and has been pushing towards its all-time low of below 85 cents in the past few days.

Insofar as it increases inflation rates in Europe, the fall in the euro's value will add to pressure on the European Central Bank not to cut interest rates, even in conditions where this would give a boost to manufacturing.

At the same time, the falling euro has tended to push up the value of the Japanese yen. This movement is cutting across the policies of the Japanese government, which would like to see a fall in the value of the yen in order to ease the disruption that will follow the "restructuring" policies it has pledged to implement.