

MARKET SIGHT LINES



Exploring the Data: Supply Chain Pressures May Be Easing

By Michael O'Keeffe, *Chief Investment Officer*



The Federal Reserve (Fed) is hiking rates to slow down economic activity as a means to ease the demand side of our elevated inflation problem. In last week's SightLines ([Are We in a Recession?](#)), we explained that the economy contracted in the first two quarters of 2022. In our article [Learnings From Economic Theory](#), we explain that demand is only *one side of the equation* when it comes to inflation. Supply chain issues have also pushed inflation higher, and a break in demand may help ease supply chain pressures.

In this week's SightLines, we take a deep dive into the data to understand where we are on the supply side of the inflation equation, with a particular focus on signals of whether or not supply chain pressures are easing.

BACKLOG OF ORDERS

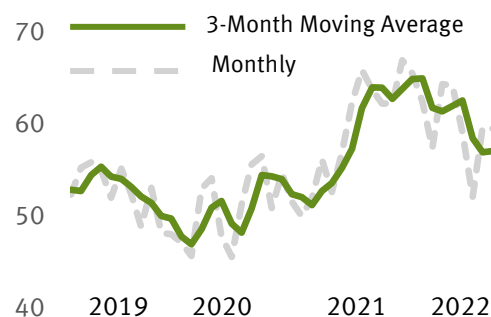
Maybe you've experienced this recently: you place an order expecting it to be filled quickly, only to learn that the delivery is delayed by weeks. Supply chain pressures have gotten personal for many of us. However, Figure 1 shows that, while volatile, backlogs appear to be easing when we observe the 3-month moving average. To understand the metrics, a reading above 50 means that companies are reporting that they are still experiencing more back orders, but we see that the number of companies doing so is declining, which is a positive.

DELIVERY TIMES

We see a similar pattern with delivery times. A reading above 50 indicates that more companies are experiencing longer delivery times than not, a classic measure of supply chain issues. And while the reading remains above 50, the trend is positive, meaning fewer companies are experiencing delayed delivery times than before.

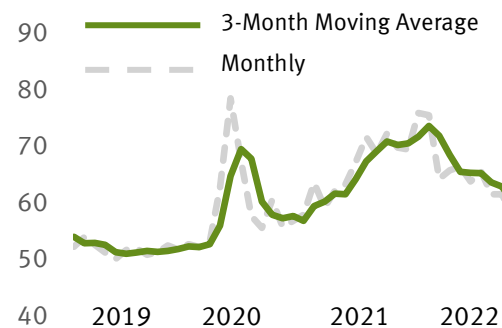
Clearly, we'll see more relief in terms of the supply chain when this reading hits and falls below 50.

Figure 1.
ISM – Backlog of Orders



Source: Stifel Investment Strategy via Bloomberg as of August 3, 2022

Figure 2.
ISM Supplier Deliveries



Source: Stifel Investment Strategy via Bloomberg as of August 3, 2022

CHINA SUPPLY CHAIN ISSUES

China has experienced supply chain issues due, in good part, to its zero-COVID policies. They have experienced factory shutdowns trying to keep the virus at bay. But China has been making an effort to improve logistics to lessen the costs of zero-Covid. Some factories now use a “closed loop” system, where workers are asked to live at the factory. This allows continued production and orders to be filled, even while restrictions tighten outside the factory. Couple these improvements with falling shipping costs, and we see hope for improved supply chain issues in Asia.

SUPPLY CHAIN PRESSURE

The New York Fed’s Global Supply Chain Pressure Index (GSCPI) measures global supply chain pressures associated with inflation in the United States and Europe, integrating several commonly used metrics like some of the data presented above.

For July, the GSCPI fell to 1.84, a level last seen in early 2021. This provides evidence that supply chain pressures have eased further and are halfway back to pre-pandemic levels.

PRICES

We’ll report on inflation next week, but the ISM Prices Paid Index gives us a sense of what we might see. The index gauges if companies are paying higher prices for materials and services and is a popular measure of inflationary pressure more broadly. These input prices have fallen recently, which is a positive sign.

CONCLUSION

Investors remain worried about high inflation and a slowing economy. While Fed policy is focused on demand, such falling demand may be helpful to the supply side of the inflation equation. We’ve reviewed some supply chain data and see signs of relief. Improvements in backorders, delivery times, China logistics, and sea freight costs are all positive. We’ll explore the impact of this result on inflation next week.

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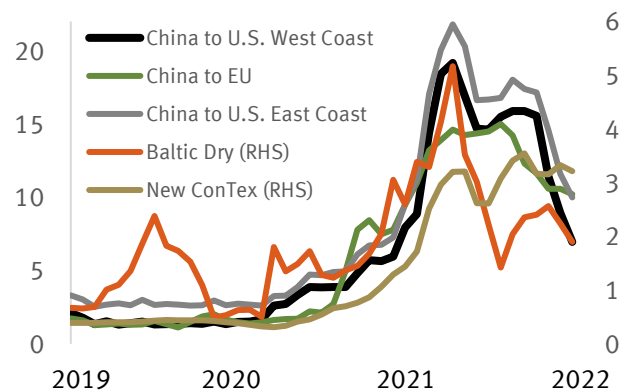
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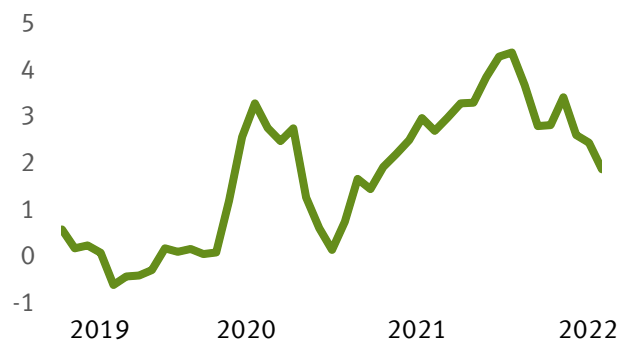


Figure 3.
Shipping Costs (\$000)



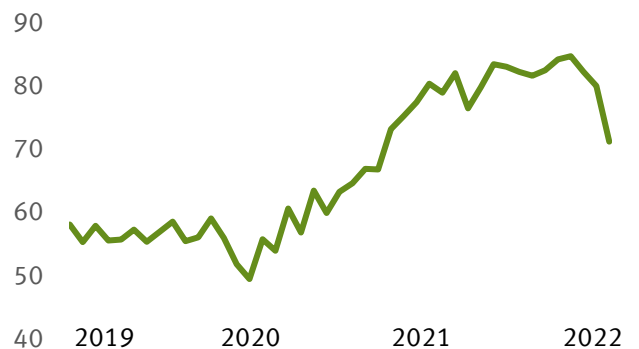
Source: Stifel Investment Strategy via Bloomberg as of August 3, 2022

Figure 4.
Global Supply Chain Pressure



Source: Stifel Investment Strategy via Bloomberg as of August 3, 2022

Figure 5.
ISM Prices Paid



Source: Stifel Investment Strategy via Bloomberg as of August 3, 2022

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