

Research Briefing | US

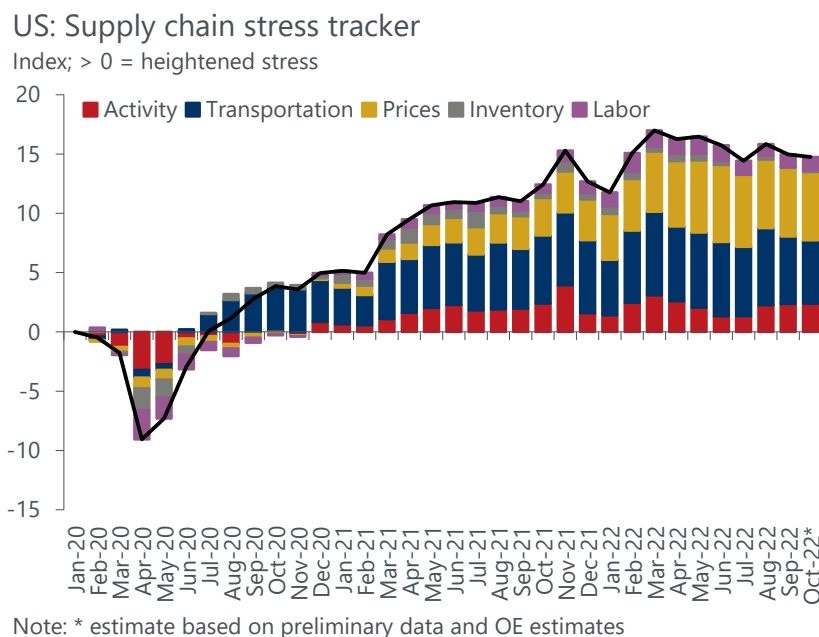
Supply chains are mending

- Supply chain developments were mixed in October, but the implications for the outlook, particularly for inflation, are modest. The easing of transportation stress helped push our supply-chain stress index lower, and a dip in price pressures helped drive the headline down. Meanwhile, increases in the activity and labor components show the economy retains momentum while inventories rose.
- While the ISM services prices paid index registered a monthly advance, manufacturing prices fell and the cost of key commodities declined – offering more evidence that goods inflation will slow. Spot rates for ocean and air freight continued to slide, and trucking rates eased.
- The infamous backlog of cargo ships off the Southern California coast looks to be nearing an end, and the impact of lower oceanborne shipping volumes is spreading downstream, with trucking companies seeing muted volumes despite entering the peak shipping season and warehouse vacancy rates creeping higher.
- Jobs growth and wage inflation moderated in October. While an increase in the unemployment rate may be an encouraging sign, we believe the October jobs report, as a whole, increases the risk that the Fed tightens monetary policy more than assumed in our November baseline forecast.

Our proprietary indicator shows that US supply chain stress diminished in October, which, all else being equal, will ease inflationary pressures and loosen supply-side constraints on GDP growth.

Price pressures eased last month, with the ISM manufacturing prices index indicating that costs fell for the first time in more than two years while the CRB commodities index trended lower over the course of the month. Risks on the price front continue to be tilted to the upside. Headaches caused by historically low levels of water in the [Mississippi River](#) are a reminder to never count out the unexpected.

Chart 1: Peak supply chain stress is well behind us



Source: Oxford Economics/Haver Analytics

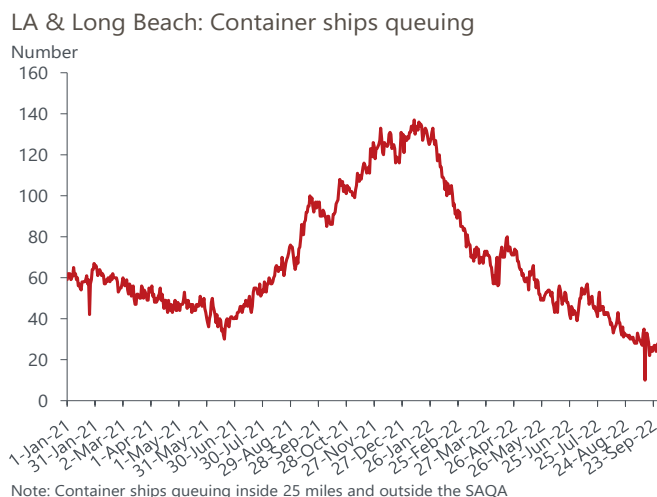
Oren Klachkin - Lead US Economist - oklachkin@oxfordeconomics.com

Matthew Martin - US Economist - mmartin@oxfordeconomics.com

Supply chains are mending

Ominous headlines persisted on the shipping front, with shipping giant Maersk warning of '[dark clouds on the horizon](#)' as weakening customer demand and overstocked retailers brought down volumes and rates. The near disappearance of the container ship backlog in Southern California points to reduced port congestion – though to be sure some ships continue to divert from the San Pedro Bay to other US ports (**Chart 2**). Other markets, including trucking and warehousing, are beginning to show these impacts, as [spot rates declined](#) and [inventory space opened](#). These developments all point to lower stress from the supply chain perspective.

Chart 2: Southern California shipping backlogs continue to ease

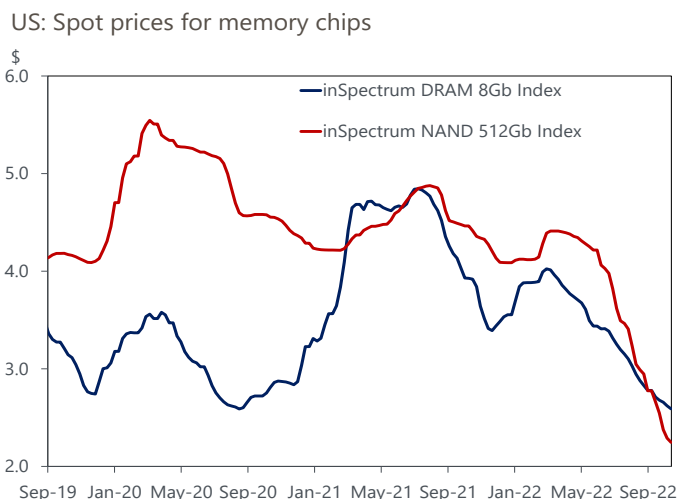


Source: Oxford Economics/Haver Analytics

The latest developments regarding semiconductor chips – the poster child industry for supply chain woes – corroborate that supply chain problems are easing. Semiconductor prices were down more than 35% in October from their March peak, and major electronics companies such as Samsung announced [cuts to earnings](#) as consumers and businesses pare back demand (**Chart 3**). On the bright side, this may be a boost for automakers, who have suffered from an inability to procure memory chips and semiconductors.

There were also notable, "big picture" developments for advanced computing chips and semiconductors in October as the US Commerce Department [announced new restrictions](#) aimed at reducing China's ability to adopt more advanced technologies. And, Micron Technology is the latest chipmaker to announce a [large US-based investment plan](#), set to benefit from subsidies from the CHIPS Act. There is a clear policy initiative by the Biden Administration to shore up domestic chip production.

Chart 3: Memory chip prices are tumbling



Source: Oxford Economics

Supply chains are mending

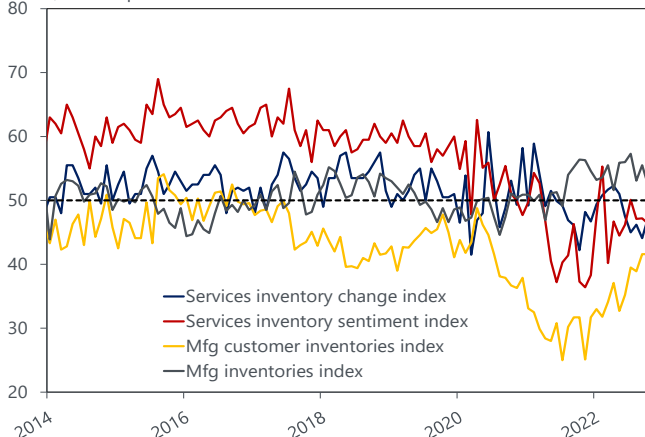
Nonfarm employment increased a [healthy 261k](#) last month while wage growth moderated to 4.7% y/y, holding well above the pre-pandemic pace. The unemployment rate rose from 3.5% to 3.7%, while the prime age employment-to-population ratio declined in October. A buoyant employment report in an environment of stubborn inflation increases the risk that the Fed tightens monetary policy more than we anticipate. Our reading of the tea leaves suggests the Fed isn't as confident as in the past that they can return inflation to their 2% target without pushing the economy into a recession.

The ISM [manufacturing](#) inventories index slipped to its lowest level in six months while the ISM [services](#) inventories index reported a contraction for the fifth straight month amid stubborn supply constraints (**Chart 4**). We expect inventory conditions to improve as supply constraints wane, but stockpiling growth will likely moderate as consumer demand retrenches and the economy enters a recession.

Chart 4: Three of four inventory measures remain in contraction territory, but are improving

US: ISM manufacturing and services inventory measures

Index; 50+ = expansion



Source: Oxford Economics/Haver Analytics

The activity component of our supply-chain tracker rose modestly, corroborating news from the labor market that economic growth is cooling and not coming to a sudden stop. Looking ahead, our activity component will register lower readings as the economy weakens into 2023.

Our [alternative](#) US supply chain indicator (which encompasses more than 30 real and survey datapoints in a principal-component approach and provides more historical data for comparison) showed reduced supply chain pressures in October. Conditions remained quite constrained compared to pre-Covid norms, but the index fell for a fifth straight month and is now at its lowest since July 2021 (**Chart 5**).

Chart 5: Our alternative tracker continues to show diminishing stress

US: Supply chain stress tracker, PCA approach

0=average stress



Source: Oxford Economics/Haver Analytics