UPSC Civil Services Examination

UPSC Notes [GS-III]

Topic: Purchasing Manager's Index (PMI) - UPSC Notes

The Purchasing Manager's Index (PMI) is an economic indicator derived from the monthly survey of the private sector companies. PMI aims in providing information regarding the current and future conditions of a business to the decision-makers, analysts and investors of the company.
There are three principal producers of Purchasing Manager's Index (PMI) namely: Institute for Supply Management (ISM), Singapore Institute of Purchasing and Materials Management (SIPMM) and the Markit Group. PMI values and its components play a major role in providing useful insight into the economic activity of a business to the decision-makers, market analysts, and investors.

Purchasing Manager's Index (PMI) is an important topic for the IAS Exam and is included under the Economics section of the UPSC Syllabus.

How do PMI works?

Purchasing Manager's Index (PMI) is released and compiled by ISM every month. The PMI value is based on the survey that is conducted monthly and is sent to the senior executives of over 400 companies under 19 primary industries that are weighted by their contribution to U.S. GDP.

Purchasing Manager's Index (PMI) focuses mainly on the five major survey areas:

1. Employment
2. New orders
3. Production
4. Inventory levels
5. Supplier deliveries

The Institute for Supply Management (ISM) weighs all of these five surveys equally. The headline PMI is a number which ranges from 0 to 100. If a PMI is above 50, it represents an expansion when compared with the previous month.

If the PMI value falls below 50, it indicates a contraction while a PMI value of 50 indicates no change.

How to calculate PMI?

Purchasing Manager's Index (PMI) can be calculated using the following formula:

Purchasing Manager's Index (PMI) = [P1 * 1] + [P2 * 0.5] + [P3 * 0]

In the above formula, P1 is equal to the percentage of answers that are reporting an improvement.

P2 represents the percentage of answers with no change whereas, P3 is the percentage of answers having a deterioration.

Role of PMI in Economy

PMI plays an important role in the economy of the country as it is an essential decision-making tool for both the manager and the suppliers. PMI provides information regarding the current and future conditions of a business to the decision-makers, analysts and investors of the company. Some of the major roles played by PMI are as follows:

1. The suppliers follow the PMI values of a particular company for the estimation of the amount of future demand for the desired products. The Purchasing Manager's Index also allows the supplier to know how much inventory its customers have on hand and as a result, it can affect the production amount generated by its clients.
2. The information provided by the PMI on supply and demand may affect the prices charged by the suppliers. The manufacturer can accept a price increase from its suppliers during an increase in the growth rate of new orders. While, if the new orders are declining, the manufacturer has to lower its prices and demand a lower cost for the parts it purchases.
3. The PMI can be used by a company in planning the annual budget, managing staffing levels and also in forecasting cash flow.
4. Purchasing Manager's Indexes are also used by the investors as a leading indicator of economic conditions. PMI plays a major role in providing useful insight into the economic activity of a business which includes the GDP, Industrial Production, and Employment.

PMI value plays a major role in developing the economic condition of a company. The economy of a country is an important topic for the Civil Service Exam. Candidates preparing for UPSC 2020 are also advised to keep a track on the latest current affairs topics related to several economic developments in the country.