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Economics Group

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Slow Ride Gets Slower: Weak ISM Non-Manufacturing Print

Against a backdrop of what has felt like universally bad economic news in recent weeks, the ISM non-manufacturing index for July came in at 52.7—weaker than expected and consistent with slow growth.

Dialing Back Expectations Another Notch

A spate of disappointing economic statistics in recent weeks suggests that the pace of economic recovery is slowing. In less than two weeks, equity markets have sold off more than 6.5 percent, Treasury yields have slipped to their lowest levels of 2011 and growth expectations are being dialed back significantly. Today's report on service sector sentiment from the ISM is not out of sync with those reports. The headline reading of 52.7 is weaker than the 53.5 the consensus expected and is the most recent indication that the already slow recovery just got dialed back another notch.

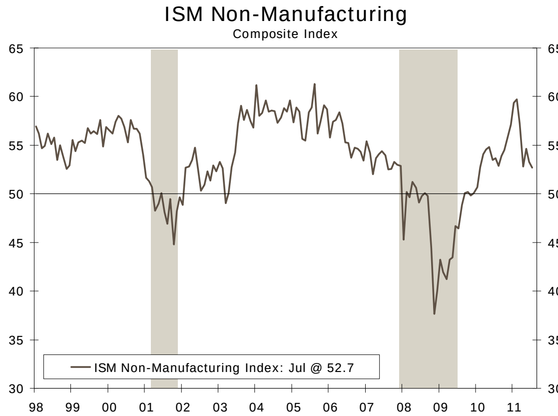
What This Report Means for Jobs

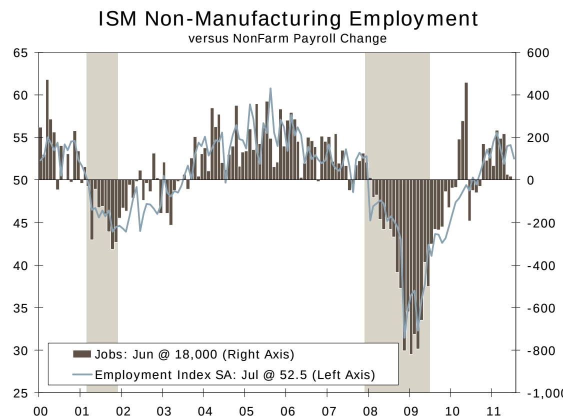
Today's ISM non-manufacturing report also offers the final clue as to what we might expect to see in Friday's critical jobs report. The consensus has been drifting lower with each successive wave of disappointing data, the most significant of which was Monday's ISM manufacturing report, which showed the employment component for July slipped to 53.5 from 59.9 in June. The employment component for the service sector from today's report came in at 52.5, which will likely nudge forecast estimates for July payrolls somewhat lower. Going into the report, the consensus was expecting 85,000 new jobs in July, which means expectations for any gain in the month will certainly be small. The middle chart offers a visual illustration on the consistency between these two measures. It is not always perfect, but over time it has proven to be a fairly reliable bellwether, which is why we include it in our model for nonfarm payrolls.

What This Report Means for the Broader Economy

The real scare in the manufacturing report earlier this week was in the new orders measure, which slipped into contraction territory. Service sector orders appear to be on somewhat firmer footing with a reading today at 51.7, but the momentum is going in the wrong direction—the orders component has been coming down on trend since its cycle peak of 64.9 back in January. The export orders component did slip into contraction territory in July, and, while this series is not seasonally adjusted, it does raise some concerns about the sustainability of export growth. Foreign PMIs have been trending lower in recent months, and that does begin to raise some concern about the ability of exports to drive economic growth going forward.

If there is a silver lining in this report, it is that businesses face less price pressure than they did just a few months ago. The prices paid index came in at 56.6. That is a far cry from the 70+ readings that we saw earlier this year. This suggests less price pressure and potential increased corporate profitability—a welcome development for businesses that are not getting much help elsewhere in this slow recovery.





Source: Institute for Supply Management, U.S. Department of Labor and Wells Fargo Securities, LLC

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