

Economics Group

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ISM: Manufacturing Gains Continue—Price Pressures Modest

U.S. manufacturing continues to record modest gains, with orders, output and employment each expanding. Export orders were up and suggest less downside risk due to Europe. Price pressures remain modest.

Growth at a Moderate Pace, Once Again

American manufacturing firms continue to align production and employment with a subpar pace of growth in the overall economy. The headline ISM index rose to 53.9 in December from 52.7 in November (top chart), with gains in production, orders and employment—a very nice result. Production and employment came in at 59.9 and 55.1, respectively, above breakeven and consistent with improvement in the overall economy. Ten industries reported production gains in December, including primary metals, machinery, electrical equipment and computers. We are sticking with our outlook for a moderate pace of growth for the national economy for the first half of this year.

Employment gains suggest continued improvement in manufacturing employment to be reported on Friday. According to the ISM survey, 10 industries reported a gain in jobs, including fabricated metals, paper, computers, transportation and machinery.

New Orders Component Suggests Continued Growth Ahead

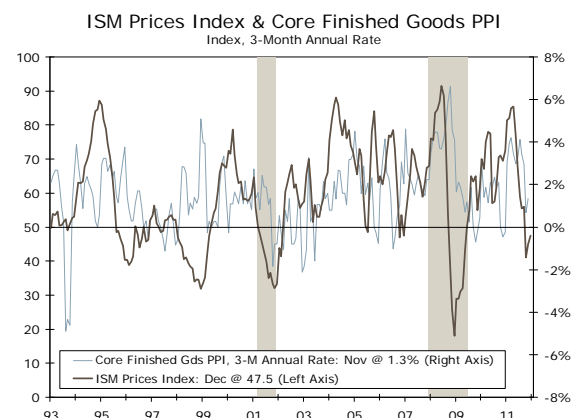
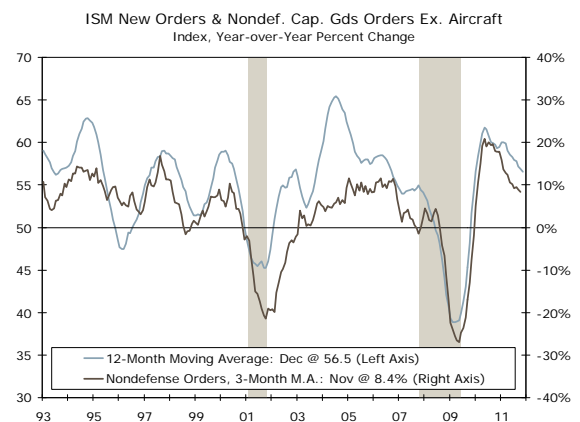
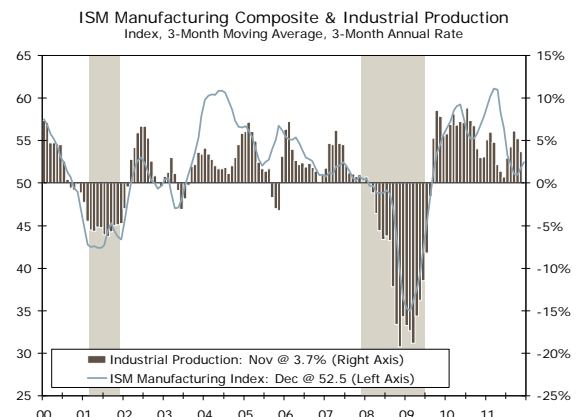
New orders (middle chart) remained above breakeven at 55.3 in December, suggesting that there is continued support for gains in manufacturing production in the months ahead. Nine industries reported growth in new orders, including primary metals, paper, machinery, electrical equipment and computers. Since orders are a leading indicator, the rise in the index indicates continued growth for industrial production in the period ahead.

On the trade side, the new export orders component continued to improve in December at 53.0, indicating that European weakness has not yet shown up in the data. Five industries reported a gain in export orders. This result suggests that many manufacturing industries continue to compete effectively on the global scale.

Prices Paid: Slowdown a Good Sign for Cost Control and Profits

Continued moderation in the prices paid component indicates reduced input cost pressures on businesses and is a welcome sign of reduced inflation pressures at the wholesale level. The price index rose modestly to 47.5 in December and remains below the breakeven 50 level. This indicates input price pressures are declining and is a good sign for corporate profit margins (bottom chart). Only six of the 18 sectors reported higher prices paid. Commodities up in price include rubber based products, electronic components and steel.

For inflation, the complete pass-through of rising commodity prices to consumer prices appears to be moderating, but there certainly continues to be some elevation in prices. For decision makers in the private and public sectors, the continued higher, but not accelerating, pace of inflation and modest overall economic gains remain a challenge to profit margins.



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