# ECONOMIC UPDATE

REGIONS

January 2, 2013

*This Economic Update may include opinions, forecasts, projections, estimates, assumptions and speculations (the "Contents") based on currently available information which is believed to be reliable and on past, current and projected economic, political and other conditions. There is no guarantee as to the accuracy or completeness of the Contents of this Economic Update. The Contents of this Economic Update reflect judgments made at this time and are subject to change without notice, and the information and opinions herein are for general information use only. Regions specifically disclaims all warranties, express or implied, with respect to the use of or reliance on the Contents of this Economic Update or with respect to any results arising therefrom. The Contents of this Economic Update shall in no way be construed as a recommendation or advice with respect to the taking of any action or the making of any economic, financial or other plan or decision.*

## December ISM Manufacturing Index: Mixed Details Behind Higher Headline

- The ISM Manufacturing Index rose to 50.7 percent in December from 49.5 percent in November.
- The new orders component held steady at 50.3 percent, while the component for export orders jumped to 51.5 percent.

The ISM Manufacturing Index rebounded in December, rising to 50.7 percent from November's 49.5 percent reading. Despite the increase in the headline index, the underlying details are somewhat inconsistent and don't alter our view that the manufacturing sector will see continued growth at a moderate rate in the near term. There is, however, one detail that is particularly encouraging – after six consecutive months of contraction, new export orders grew in December, with the sub-index for export orders rising to 51.5 percent.

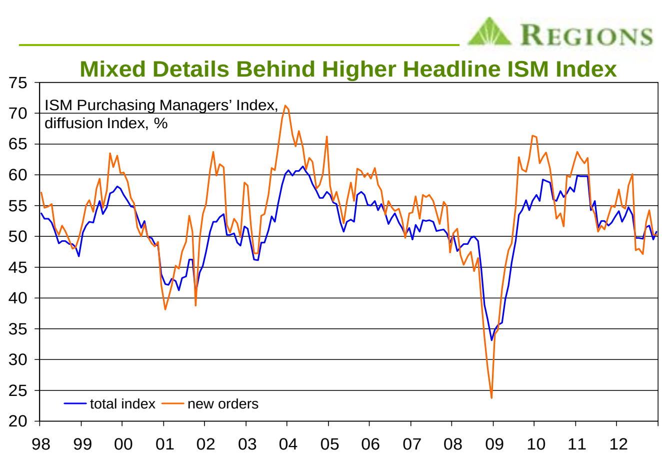
The index for new orders was unchanged in December, coming in at 50.3 percent, consistent with modest growth. Still, only five industry groups reported higher orders during the month, most notably primary metals and furniture & related products, while ten industry groups saw orders decline, including transportation equipment, machinery, and computer & electronic products. The index for current production fell in December but, at 52.6 percent, remains consistent with modest growth. Five industry groups reported increased production, seven reported lower production, and the remainder reported no change. The index for employment exhibits the same sort of split, with nine industry groups reporting higher employment levels, seven reporting lower levels, and two reporting no change in employment.

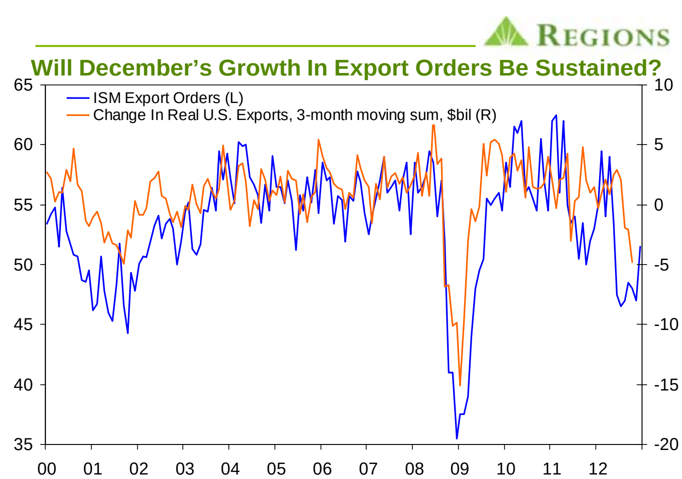
A jump in the index for supplier deliveries also contributed to the higher headline reading, but the cause for the increase is uncertain. The supplier delivery index came in at 54.7 percent in December from 50.3 percent in November – an index value above 50 percent indicates slower customer delivery times. With no change in new orders and a decline in the current production index, it could be that the reported slowdown in customer delivery times is due to disruptions caused by Hurricane Sandy.

Inventories contracted in December at a faster pace than was the case in November, with the sub-index falling to 43.0 percent from 45.0 percent. That this component was below 50 percent in both November and December is consistent with our expectation that inventories will act as a sizeable drag on Q4 real GDP growth. At the same time, however, the gap between the index for new orders and the index for inventories widened again in December, and this gap is a fairly reliable proxy for future production levels.

As noted above, export orders increased in December following six consecutive monthly declines. The behavior of the ISM index for new export orders is a good indicator, with a one quarter lag, of changes in the value of real U.S. exports of goods. As such, December's increase is encouraging, but with the caveat that it must be sustained over coming months. We have for some time been pointing to two drags on the U.S. economy in general and the factory sector in particular – the fiscal cliff and an uncertain global growth outlook. During the summer months, the outlook for global growth had become somewhat cloudy but by year-end 2012 that outlook had begun to improve, which does suggest that December's growth in new export orders will prove to be more than a one-off occurrence.

The increase in the headline index is encouraging, but December's increase did not even capture half the ground lost between the October and November readings. It is of note that the machinery and transportation industry groups report lower orders and lower employment, with machinery also reporting lower production (unchanged in transportation equipment). At the same time, furniture manufacturers and makers of wood products report stronger business, which is consistent with a housing market on the mend. Overall, however, the U.S. manufacturing sector continues on a path of modest growth, though there has seemingly been a transition in which machinery and transportation equipment has given way to housing oriented industry groups as the sector's strong points. The latter should continue to thrive in 2013, while the former will need firmer global economic growth to see sustained improvement in business conditions.





Regions Financial Corporation, 1900 5th Avenue North, 17th Floor, Birmingham, Alabama 35203

Richard F. Moody, Chief Economist • 205.264.7545 • richard.moody@regions.com