



Economics Group

John E. Silvia, Chief Economist
john.silvia@wellsfargo.com • (704) 410-3275
 Tim Quinlan, Economist
tim.quinlan@wellsfargo.com • (704) 410-3283

ISM: Continued Growth Signal for Manufacturing, Prices Up

Broad-based expansion signals for orders, production, employment and delivery times remain a plus for gains in industrial production and the economy. Fed will likely revise its forecasts higher later this month.

Continued Expansion for the Manufacturing Sector

At 59.0, the ISM manufacturing survey result provides further evidence of a continued expansion in the U.S. manufacturing sector and thereby supports the case for continued overall economic growth (top graph). Our outlook is for four percent growth in industrial production for the second half of this year.

Production came in at 64.5, with gains in 15 out of 17 industries. This was the sixth consecutive month of expansion in the production index which reinforces the view of sustained growth in the manufacturing sector. Industries reporting improvement included fabricated metals, machinery, paper, plastics, chemicals and computer/electronics. Electrical equipment production was softer.

In another signal of continued growth, the employment index came in at 58.1, with 14 of 18 industries reporting improvement. These industries include fabricated metals, machinery, plastics, chemicals, computers & electronics and transportation equipment. We expect another positive print for manufacturing employment when nonfarm payrolls are released Friday.

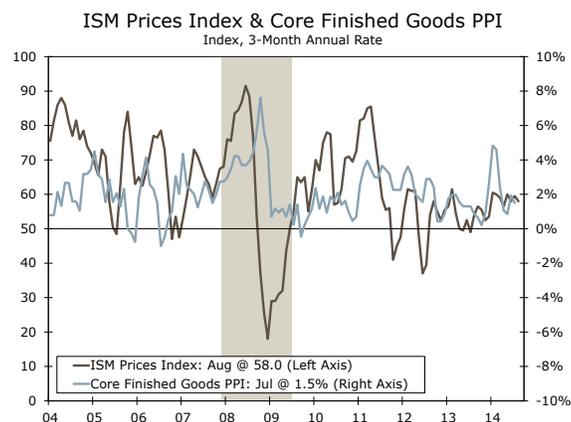
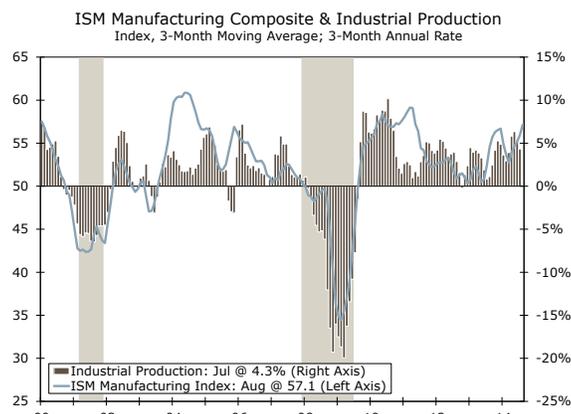
New Orders: Strongest Since January 2004

New orders (middle graph) rose to 66.7 from 63.4 and this represents the fourth consecutive monthly improvement in orders. Gains were in 14 of 16 industries, with expansion in machinery, plastics, chemicals, transportation equipment, paper and fabricated metals. The new orders index indicates forward momentum in the economy. This indication is reinforced by the increase in the new export orders index and the backlogs index as well. Given the lack of conviction in business spending earlier this year, this is a welcome development. This report signals a bigger contribution from equipment outlays than the more modest growth environment we have been expecting.

Prices Paid: Continued Signal of Rising Input Pressures

Amid renewed attention to inflation, the prices-paid measure from the ISM takes on a greater level of significance. We learned today that the prices paid index registered 58.0 and has been at or above this level for the past four months, which is consistent with rising prices (bottom graph). Moreover, the prices-paid measure has been above its 12-month moving average for the past seven months.

This price dynamic presents a challenge to corporate profits. Of the 18 manufacturing industries followed in the ISM report, 9 of them reported paying increased prices. These prices-paid indicators corroborate other signs of rising inflation pressures in the U.S. economy and strike us as more than noise. The Fed will likely revise its economic and inflation higher forecasts later this month for 2014 and 2015.



Wells Fargo Securities, LLC Economics Group

Diane Schumaker-Krieg	Global Head of Research, Economics & Strategy	(704) 410-1801 (212) 214-5070	diane.schumaker@wellsfargo.com
John E. Silvia, Ph.D.	Chief Economist	(704) 410-3275	john.silvia@wellsfargo.com
Mark Vitner	Senior Economist	(704) 410-3277	mark.vitner@wellsfargo.com
Jay H. Bryson, Ph.D.	Global Economist	(704) 410-3274	jay.bryson@wellsfargo.com
Sam Bullard	Senior Economist	(704) 410-3280	sam.bullard@wellsfargo.com
Nick Bennenbroek	Currency Strategist	(212) 214-5636	nicholas.bennenbroek@wellsfargo.com
Eugenio J. Alemán, Ph.D.	Senior Economist	(704) 410-3273	eugenio.j.aleman@wellsfargo.com
Anika R. Khan	Senior Economist	(704) 410-3271	anika.khan@wellsfargo.com
Azhar Iqbal	Econometrician	(704) 410-3270	azhar.iqbal@wellsfargo.com
Tim Quinlan	Economist	(704) 410-3283	tim.quinlan@wellsfargo.com
Eric Viloría, CFA	Currency Strategist	(212) 214-5637	eric.viloria@wellsfargo.com
Sarah Watt House	Economist	(704) 410-3282	sarah.house@wellsfargo.com
Michael A. Brown	Economist	(704) 410-3278	michael.a.brown@wellsfargo.com
Michael T. Wolf	Economist	(704) 410-3286	michael.t.wolf@wellsfargo.com
Zachary Griffiths	Economic Analyst	(704) 410-3284	zachary.griffiths@wellsfargo.com
Mackenzie Miller	Economic Analyst	(704) 410-3358	mackenzie.miller@wellsfargo.com
Erik Nelson	Economic Analyst	(704) 410-3267	erik.f.nelson@wellsfargo.com
Alex Moehring	Economic Analyst	(704) 410-3247	alex.v.moehring@wellsfargo.com
Donna LaFleur	Executive Assistant	(704) 410-3279	donna.lafleur@wellsfargo.com
Cyndi Burris	Senior Admin. Assistant	(704) 410-3272	cyndi.burris@wellsfargo.com

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