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Economics Group

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ISM Manufacturing: Domestic Strength, Lower Prices

The ISM index, at 58.7, is a very positive report for the economy. Production and new orders were strong, with lower input prices. New export orders did not decline despite concerns about global weakness.

Continued Expansion for the Manufacturing Sector

The better-than-expected ISM index, at 58.7, signals continued expansion in the U.S. manufacturing sector and supports the case for continued overall economic growth (top graph). Our outlook is for 4.5 to 5 percent growth in industrial production for the year ahead.

Production came in at a strong 64.4, with gains in 14 industries. This was the ninth-consecutive month of expansion signaled from the production index, which reinforces the view of sustained growth in the manufacturing sector. Gains were recorded in fabricated metals, primary metals, machinery and paper and electrical equipment.

The employment index came in at 54.9 marking the 17th consecutive month of expansion, with 11 of 18 industries reporting improvement. These industries include primary metals, machinery, plastics, paper and electrical equipment. We expect another positive print for manufacturing employment when nonfarm payrolls are released on Friday.

New Orders: Signal of Continued Growth Ahead

New orders inched up to 66.0 and have remained in expansion territory for 18 straight months (middle graph). Gains were seen in 11 industries, with expansion in chemicals, transportation equipment, paper, machinery and fabricated metals. Gains in the new orders index indicate forward momentum in the economy.

Despite concerns about the global outlook, the new export orders index rose to 55.0 and the backlogs index also rose to 55.0 as well. Given the worries about a global slowdown, this is a welcome development that demand overseas is still sustaining orders.

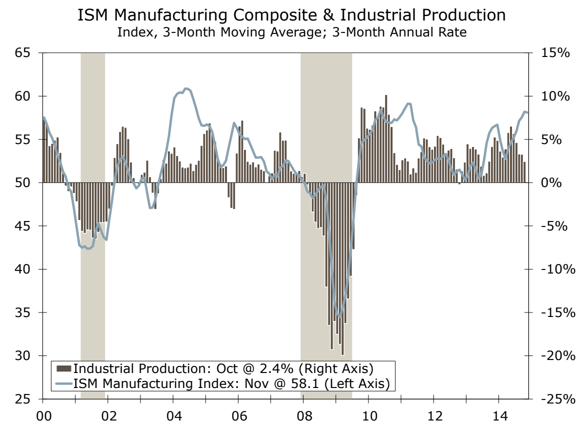
Prices Paid: Interesting and Large Drop in Prices Paid

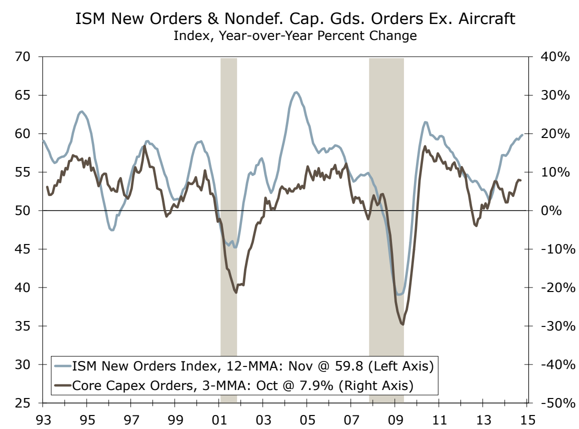
In a clear reversal of trend, the prices paid index declined to 44.5, below breakeven, from 53.5 in October and the only below-50 reading for the past six months. This result suggests reduced input price pressures, largely attributable to the selloff in oil/commodities (bottom graph).

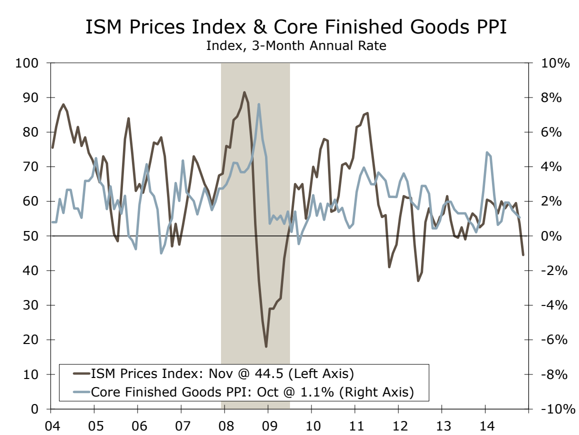
To reinforce that view, no commodities seem to be getting bid up in price. Commodities down in price include copper, diesel and gasoline, while aluminum was up in price.

This price dynamic is a positive for corporate profits and a relief to inflation concerns at the Fed. Of the 18 manufacturing industries followed in the ISM report, only two reported paying increased prices, paper and furniture. Sectors paying lower prices include machinery, chemicals, electrical equipment and fabricated metals.

The prices-paid indicator signals lower inflation pressures in the U.S. economy as oil and commodity prices fall.







Source: ISM, Federal Reserve Board, U.S. Departments of Commerce and Labor and Wells Fargo Securities, LLC

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