ECONOMIC UPDATE

REGIONS

October 1, 2019

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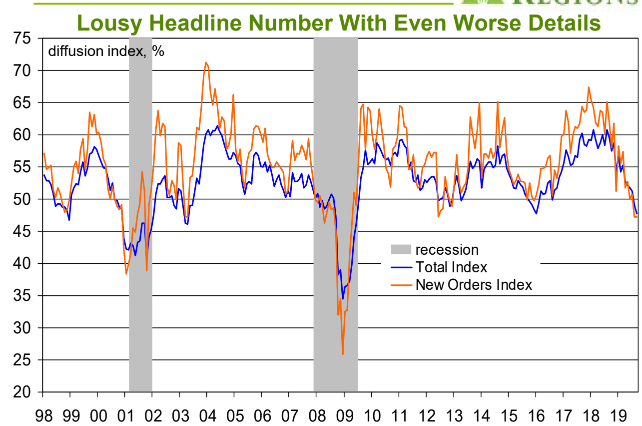
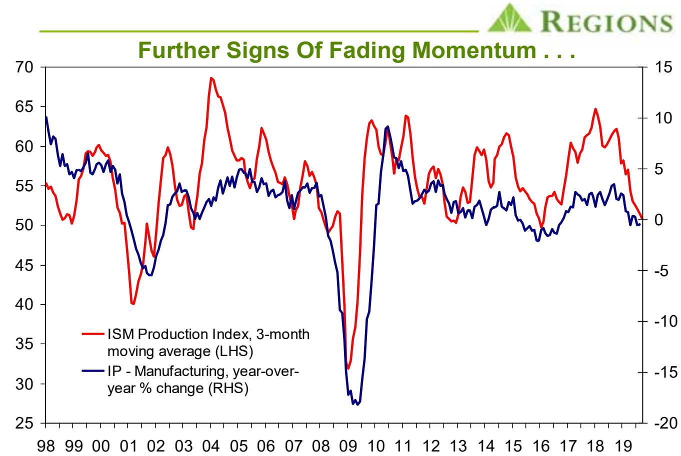
September ISM Manufacturing Index: Lousy Headline Number With Even Worse Details

- The ISM Manufacturing Index fell to 47.8 percent in September from 49.1 percent in August
- The new orders index rose to 47.3 percent, the employment index fell to 46.3 percent, the production index fell to 47.3 percent

The contraction in the manufacturing sector intensified in September, with the ISM Manufacturing Index tumbling to 47.8 percent, the lowest since June 2009. We and most others expected a modest bounce in the headline index after it dropped below the 50.0 percent break between contraction and expansion in August, as other indicators pointed to some stabilization in the factory sector. To the contrary, the details of the September data are even worse than the headline number. Perhaps the most telling detail is that only three of the 18 industry groups included in the ISM's survey reported growth in September, the fewest since April 2009 when the economy was still in the clutches of the 2007-09 recession. It is of little solace to note that a contraction in the factory sector and ongoing expansion in the broader economy are not mutually exclusive, and instead it becomes reasonable to ask how much longer firms in the services sector can remain immune to drop-off in business confidence that is gripping the manufacturing sector.



As noted above, only three of the 18 industry groups included in the ISM survey reported growth in September, with 15 reporting contraction. Over the past few months we've pointed to the steadily narrowing base of growth within the factory sector as one of the details in the ISM data that we found the most troubling, our point being that this has eroded the base for growth in orders, production, and employment. That erosion picked up pace in September – recall that in August nine of the 18 industry groups reported growth. "Slower" and "softer" are the main themes of the comments from survey respondents relayed by ISM, with tariffs/trade the most commonly cited cause. One firm in the computer and electronic products industry group noted that shipments had outpaced orders for a second straight month, pointing to lower production in the months ahead. Representatives from other industry groups noted that demand had dropped off more sharply and more rapidly than anticipated, indicating that unwanted inventory accumulation may act as an even more significant drag on employment and production in the months ahead.



The index of new orders inched up to 47.3 percent in September from 47.2 percent in August. Only three industry groups – miscellaneous manufacturing, food, beverage, & tobacco products, and chemical products – reported growth in new orders, with 11 industry groups reporting declining order volume. The three industry groups reporting growth in new orders are the same who reported growth in overall activity in September. The index of new orders, which we've long looked to as a reliable leading indicator, had been eroding for several months before falling below the 50.0 percent line in August, which presaged the declines seen in the gauges of employment and current production. In September, the index of current production fell to 47.3 percent, the lowest since April 2009, with only three industry groups reporting higher output and 11 reporting decreased output. The employment index fell to 46.3 percent, with four industry groups reporting employment growth while 11 reported declining employment. While sizable backlogs of unfilled orders had for some time acted as a buffer against diminishing new orders, those backlogs have been worked off, thus removing a key support for production and employment, as evidenced by the contractions reported in the past two months. With backlogs contracting further in September as new orders continued to slip, production and employment will remain under pressure over coming months. Finally, the sharp and steady erosion in export orders has removed another buffer against contraction in the U.S. factory sector.

Though trade tensions are the most visible factor, weak global economic growth, elevated inventories, gradually easing motor vehicle sales, and Boeing's issues have contributed to the deteriorating conditions in the U.S. manufacturing sector over recent months. The ISM data for the past two months suggest there is no quick end to what ails the factory sector.

Regions Financial Corporation, 1900 5th Avenue North, 17th Floor, Birmingham, Alabama 35203
Richard F. Moody, Chief Economist • 205.264.7545 • richard.moody@regions.com