ECONOMIC UPDATE
REGIONS
November 1, 2017

October ISM Manufacturing Index: It's Still Good To Be The Manufacturing Sector . . .

- The ISM Manufacturing Index fell to 58.7 percent in October from 60.8 percent in September.
- The new orders component fell to 63.4 percent, the employment component fell to 59.8 percent, and new export orders rose.

The headline on our write-up of the September ISM Manufacturing Index was "It's Good To Be The Manufacturing Sector," which we thought a fitting characterization of the headline index hitting its highest level since May 2004. A month later, despite the headline index having slipped to 58.7 percent, we haven't changed our view at all, i.e., it's still good to be the manufacturing sector. At 58.7 percent, the October print matches our below-consensus forecast, but the details on new orders, employment, and current production remain solid. October marks the 14th consecutive month in which the headline index has been above the 50.0 percent break between expansion and contraction in the factory sector, and the expansion in the factory sector remains notably broad based, not always the case in the post-recession years.

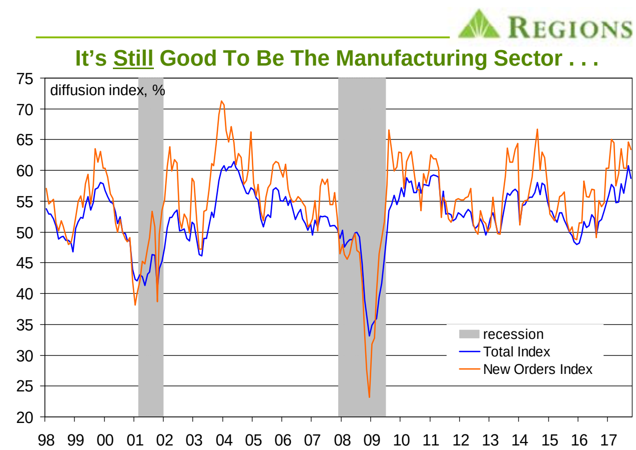
Of the 18 industry groups included in the ISM survey, 16 reported expansion in October with two reporting no change in the level of activity. Hurricanes Harvey and Irma are visible in the October data, with some respondents noting shortages of materials stemming from the storms while others noted higher orders due to the recovery efforts. More broadly, comments from survey respondents indicate capacity constraints are becoming an issue, which bodes well for production and employment levels in the months ahead. Shortages of materials are reflected in the index of prices paid (which does not factor into the calculation of the headline index). After having jumped to 71.5 percent in September, the prices paid index eased to 68.5 percent in October but nonetheless remains above the pre-hurricane average.

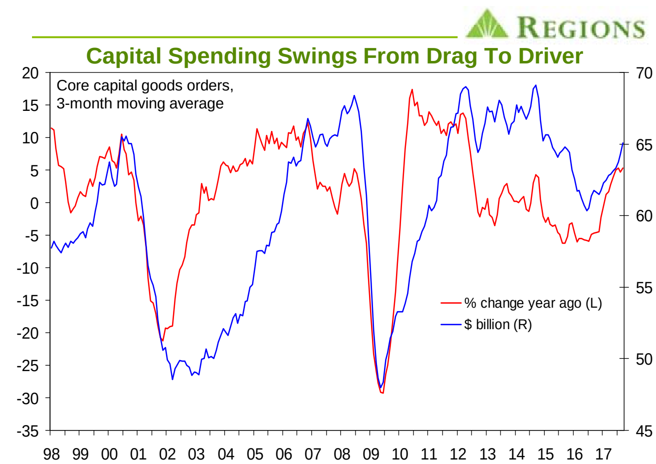
Another impact of the hurricanes had been to lengthen supplier delivery times, with the corresponding index jumping to 64.4 percent in September, the highest level since July 2004. With supply chains moving more normally, even if not completely so, in October, we expected this index to fall, which was a large factor in our below-consensus forecast. The index for delivery times fell to 61.4 percent in October, with 12 of the 18 industry groups reporting slower delivery times, but still remains higher than we think consistent with overall conditions in the manufacturing sector. As such, this poses some downside risk to the headline index over coming months.

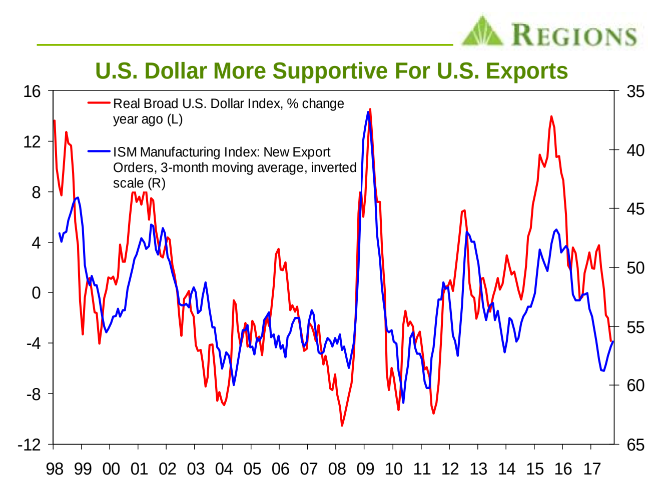
As we noted in our weekly *Economic Preview*, however, delivery times normalizing in the wake of the hurricanes is simply noise, and the reads on new orders, current production, and employment will be much more telling indicators of the state of the manufacturing sector. Though the indexes for these components each slipped a bit in the October data, they all remain notably elevated. For instance, the index for new orders fell to 63.4 percent in October from 64.6 percent in September, and 12 of the 18 industry groups reported higher order volumes with three reporting no change and three reporting lower order volumes. The current production index eased to 61.0 percent from 62.2 percent in September, but 15 of the 18 industry groups reported increased production. The same pattern is seen in the employment component, which settled back from September but, at 59.8 percent in October, remains elevated with 15 of the 18 industry groups reporting higher job counts and only one reporting a decline.

U.S. manufacturers are benefitting not only from rising domestic demand but ongoing growth in foreign demand. The ISM's gauge of new export orders fell to 56.5 percent from 57.0 percent in September but nonetheless has remained above the 50.0 percent mark – indicating growth in export orders – for 20 consecutive months. Firmer global economic growth and the effects of a sharp decline in the exchange value of the U.S. dollar are contributing to the steady growth in export orders.

The U.S. manufacturing sector remains on a nice roll, buoyed by rising domestic and foreign demand. While a slowdown in motor vehicle sales and U.S. trade policy pose downside risks, the broad based expansion is likely to endure over coming quarters.







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