



Economics Group

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ISM: Manufacturing Sector Continues Growth Path

Growth remains the story for the manufacturing sector as production, employment and orders all remain in expansion mode. Price pressures remain modest. Our outlook is for stronger industrial production ahead.

Manufacturing Gains Pick Up at Start of Fourth Quarter

Despite all the hype on the budget/debt ceiling and the negative impact on the economy, the actual actions of manufacturers continued to say growth. The ISM Manufacturing Index came in at 56.4 in October, which corroborates our outlook for continued gains in industrial production. We look for annualized growth of about 5 percent in industrial production in the fourth quarter, up from around 2 percent in the third quarter. This level of the ISM index is consistent with continued overall GDP gains (top graph). In October, 12 industries reported a gain in production, including electrical equipment, fabricated metals, computers & electronics, machinery and paper. These results are an indication that the factory sector will continue its modest growth path, but at a slightly faster pace in the fourth quarter. We also expect capacity utilization to rise in the fourth quarter, indicating less slack in the factory sector. The employment index came in at 53.2—with 12 industries reporting an improvement in jobs, including paper, printing, fabricated metals and electrical equipment. We expect another positive employment report for October.

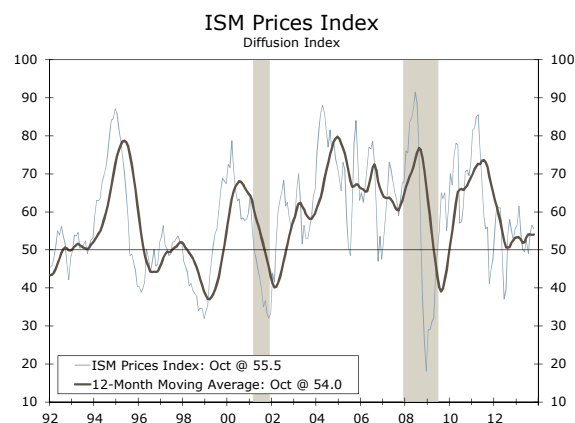
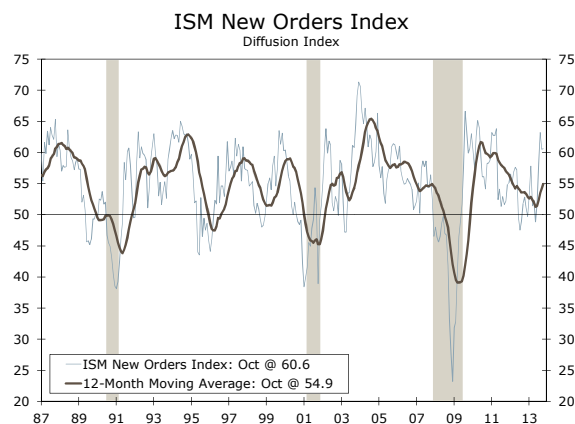
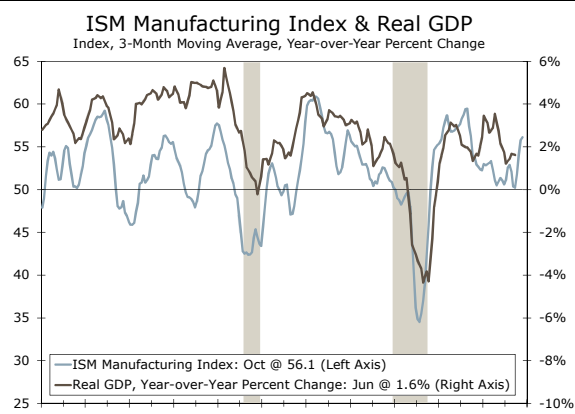
New Orders and Export Orders Still Positive

New orders remained positive for October at 60.6 (middle graph), with 10 of 14 industries reporting an increase. There were gains in computer & electronic products, electrical equipment, machinery and fabricated metals. Export orders, meanwhile, jumped to 57.0 from 52.0 and are above the 50 breakeven level for the eleventh straight month. Ten industries reported a gain in export orders including fabricated metals, machinery, electrical equipment and appliances. Orders are a leading economic indicator and the gains here suggest the outlook remains for modest growth going forward over the next six months.

The prices paid component slowed slightly to 55.5 and suggests mild input cost pressures on profits. Of 18 industries, 8 reported higher input prices, thereby suggesting that there are modest input cost pressures in certain industries.

Disconnect Between Hard and Soft Data

Earlier this week financial markets absorbed a mixed report on September industrial production. While output increased more than expected (up 0.6 percent on the month), the gain was almost entirely a function of a surge in the volatile utilities component. Manufacturing output increased a far more modest 0.1 percent. Similarly, the September durable goods report posted a larger-than-expected gain, but the strength was limited to aircraft orders. Excluding transportation, durable goods orders fell for the second month in September. It is difficult to reconcile the disconnect between survey results and hard data. We suspect this has much to do with varying sensitivity to the ongoing situation in Washington.



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