

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: 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.

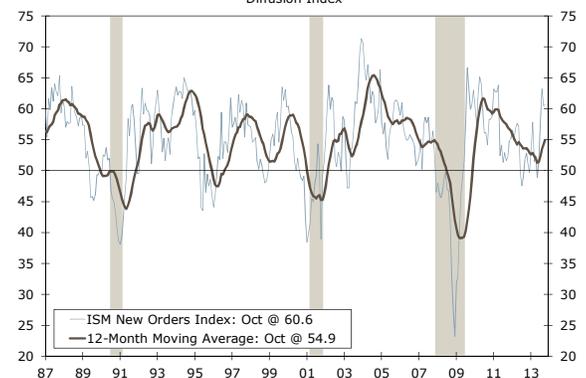
Disconnect Between Hard and Soft Data

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.

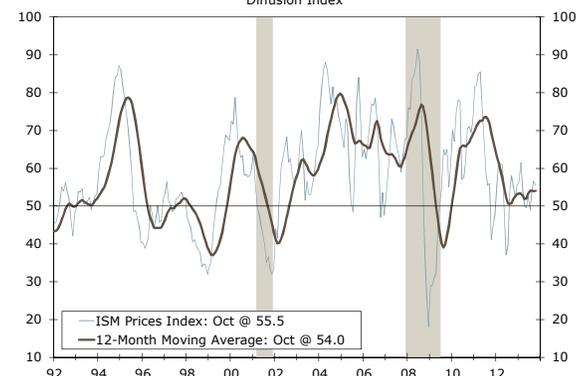
ISM Manufacturing Index & Real GDP
Index, 3-Month Moving Average, Year-over-Year Percent Change



ISM New Orders Index
Diffusion Index



ISM Prices Index
Diffusion Index



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
Michael A. Brown	Economist	(704) 410-3278	michael.a.brown@wellsfargo.com
Sarah Watt	Economist	(704) 410-3282	sarah.watt@wellsfargo.com
Michael T. Wolf	Economist	(704) 410-3286	michael.t.wolf@wellsfargo.com
Sara Silverman	Economic Analyst	(704) 410-3281	sara.silverman@wellsfargo.com
Zachary Griffiths	Economic Analyst	(704) 410-3284	zachary.griffiths@wellsfargo.com
Mackenzie Miller	Economic Analyst	(704) 410-3358	mackenzie.miller@wellsfargo.com
Blaire Zachary	Economic Analyst	(704) 410-3359	blaire.a.zachary@wellsfargo.com
Peg Gavin	Executive Assistant	(704) 410-3279	peg.gavin@wellsfargo.com
Cyndi Burris	Senior Admin. Assistant	(704) 410-3272	cyndi.burris@wellsfargo.com

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