January 4, 2016

TD Economics

Data Release: U.S. manufacturing activity remains in contractionary territory in December

- The Institute for Supply Management (ISM) manufacturing index edged down 0.4 points to 48.2 in December. The reading disappointed consensus expectations, which called for a slight pick up to 49.0.
- The details of the report were somewhat mixed. Most disappointing was the employment subcomponent (-3.2 pts to 47.5), which gave up the bulk of the gains registered in the prior month and slipped back into contractionary territory. Imports (-3.5 pts to 45.5), the backlog of orders (-2.0 pts to 41.0), prices paid (-2.0 pts to 33.5), and supplier deliveries (-0.3 pts to 50.3) also declined on the month.
- On the bright side, the export index rose by 3.5 points to 51.0, moving back into expansionary territory after six months of contraction. The customer inventory sub-index rose 1.0 pt to 51.5, while production (+0.6 pts to 49.8), inventories (+0.5 pts to 43.5), and new orders (+0.3 pts to 49.2) all registered gains, albeit all remained in contractionary territory.
- The spread between new orders and inventories – which tends to lead the headline index by about three months – narrowed only slightly from 5.9 to 5.7.
- Eleven of the eighteen manufacturing industries reported contraction in December: Wood Products; Apparel, Leather & Allied Products; Plastics & Rubber Products; Electrical Equipment, Appliances & Components; Transportation Equipment; Fabricated Metal Products; Nonmetallic Mineral Products; Furniture & Related Products; Computer & Electronic Products; Machinery; and Food, Beverage & Tobacco Products.

Key Implications

- This was certainly a disappointing report, with relatively broad weakness and a headline print that slid to its lowest level since mid-2009.
- Despite a pick-up in the export sub-index, the U.S. manufacturing sector continues to face headwinds stemming from soft global economic activity, with disappointing manufacturing data out of China released last night corroborating this notion. Additionally, the sector continues to contend with the protracted slump in energy prices which is weighing on energy related investment and hindering demand for drilling equipment and other heavy machinery. Lastly, the sector is not getting any help from the U.S. dollar which continues to rally making U.S. made products more expensive in foreign markets.
- Much of the divergence in monetary policies between the U.S. and other major central banks appears priced in to the lofty value of the U.S. dollar. However, global weakness and a potential for an even higher dollar continue to pose near-term risks for U.S. manufacturers. Still, any near term weakness should be somewhat offset by continued strength in U.S. domestic demand, effectively bolstering manufacturing activity over the coming months.

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