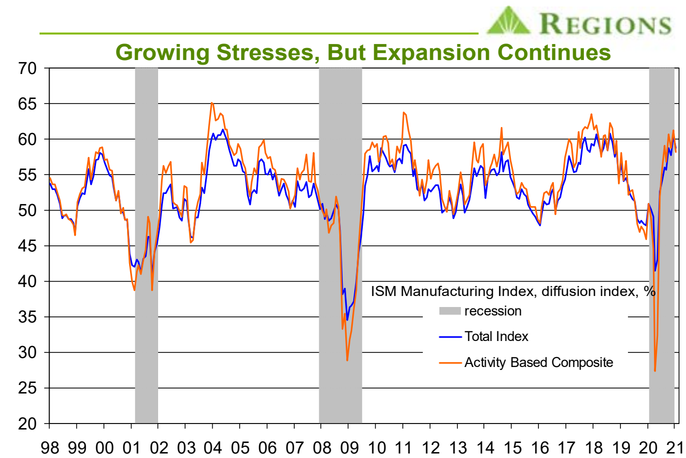
ECONOMIC UPDATE
REGIONS
February 1, 2021

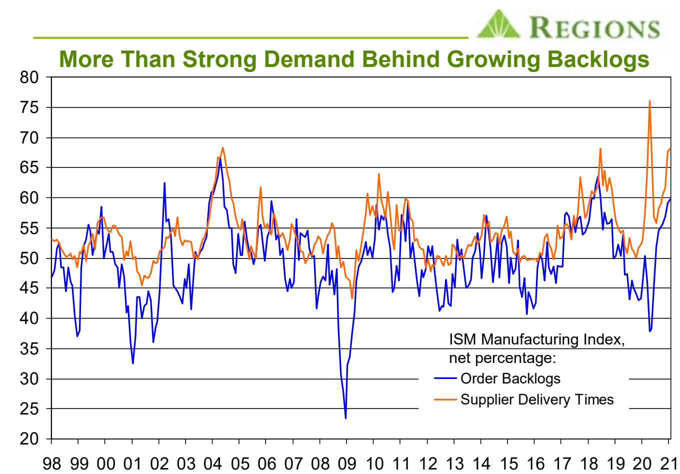
January ISM Manufacturing Index: Growing Stresses On Factory Sector Expansion

- The ISM Manufacturing Index fell to 58.7 percent in January from a revised reading of 60.5 percent in December
- The new orders index fell to 60.7 percent, the employment index rose to 52.6 percent, and the production index fell to 60.7 percent

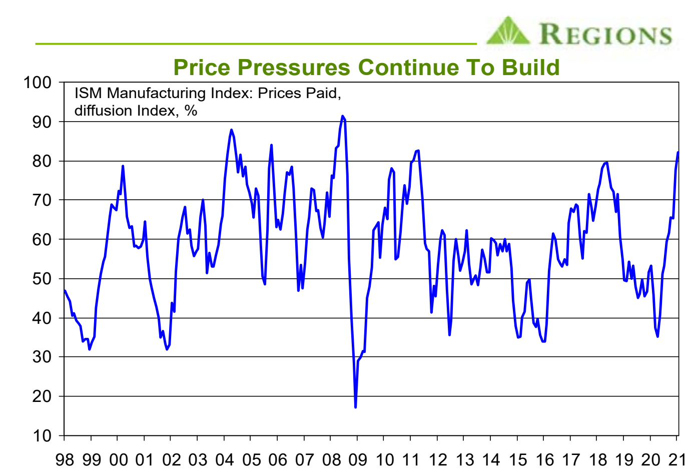
The ISM Manufacturing Index fell to 58.7 percent in January, a bit below what we and the consensus expected but nonetheless marking the eighth consecutive month with the headline index above the 50.0 percent break between contraction and expansion. The details of the January survey point to further broad based expansion in the factory sector in the months ahead, though labor supply issues and logistics challenges continue to hamper the pace of growth. Price pressures continue to build, reflecting continued strong growth in demand along with growing stresses on supply chains, and it will bear watching over coming months whether, or to what extent, these price pressures begin to register in the broader inflation gauges. Still, with order books growing faster than firms can fill them, output and employment in the manufacturing sector are poised for further growth in the months ahead.



For a third straight month, sixteen of the 18 industry groups included in the ISM's survey reported growth, with two industry groups (petroleum and coal products and printing/support activities) reporting contraction. This goes to our point about a broad based expansion in the manufacturing sector. There were three common themes in the comments from survey respondents – strong, demand, labor supply constraints, and logistics bottlenecks. Though manufacturers have been spared a repeat of the broad shutdowns seen last spring, the surge in COVID-19 cases has led to increased absenteeism, while finding new workers has also become more difficult, and some firms report their suppliers are contending with the same issues. At the same time, increased supply chain disruptions, including ports being backed up to the point it is taking weeks to unload ships, are also curbing production. To be sure, contending with the problem of how to meet demand is a better than contending with the problem of there being little or no demand, but nonetheless can foster its own set of disruptions.



The new orders index fell to 61.1 percent in January from 67.5 percent in December, with 13 of the 18 industry groups reporting growth in new orders and two reporting a decline in orders. A separate gauge of new export orders, which does not enter into the calculation of the headline index, registered 54.9 percent in January, the seventh consecutive month of growth as global trade flows continue to normalize. The ISM's production index slipped to 60.7 percent in January from 64.7 percent in December, with 12 of the 18 industry groups reporting higher output and two reporting lower output. After having dipped below the 50.0 percent threshold in November, the ISM's employment index has rebounded, rising to 52.6 percent in January, though only 6 of the 18 industry groups reported higher employment. As noted above, comments from survey respondents indicate high rates of absenteeism and increased difficulty in finding new workers continue to hamper production.



The index of supplier delivery times rose to 68.2 percent in January from 67.7 percent in December, with 16 of the 18 industry groups reporting slower delivery times. This reflects not only strong growth in demand from manufacturers, but also suppliers contending with labor supply issues and logistics bottlenecks. Continued growth in new orders, slower supplier delivery times, and labor supply issues hindering production have all contributed to further growth in backlogs of unfilled orders. The ISM's gauge of order backlogs rose to 59.7 percent in January, with 12 of the 18 industry groups reporting growing backlogs. An additional detail in the ISM data we look to as a leading indicator is the gap between the indexes of new orders and customer inventories. The vast majority of industry groups report customer inventory levels are too low, suggesting further gains in new orders and production in the months ahead and thus reinforcing the signal being sent by growing backlogs of unfilled orders. The prices paid index jumped to 82.1 percent in January, the highest reading since April 2011, and for a second straight month all 18 industry groups reported paying higher prices for inputs.

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