ECONOMIC UPDATE

REGIONS

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June ISM Manufacturing Index: The Good But Could Be Better Expansion Presses On

- The ISM Manufacturing Index fell to 60.6 percent in June from 61.2 percent in May
- The new orders index fell to 66.0 percent, the employment index fell to 49.9 percent, and the production index rose to 60.8 percent

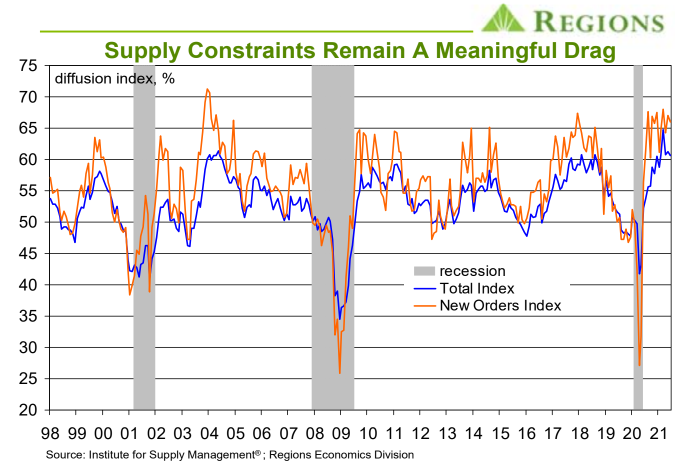
The ISM Manufacturing Index fell to 60.6 percent in June, just below the 60.9 percent reading we and the consensus expected. June marks the thirteenth consecutive month in which the headline index was above the 50.0 percent break between contraction and expansion. Though the headline index points to further growth, the details of the data indicate supply side stresses remain a meaningful drag on the pace of the expansion in the factory sector. Order books continue to expand faster than firms can fill them, as shortages of materials, shipping delays, and labor supply constraints are acting as increasing drags on production, and to that point, the employment index dropped below the 50.0 percent threshold in June. Price pressures continue to build, with the ISM's gauge reaching its highest point since July 1979. For months now we've stated that the most pressing problem in the manufacturing sector isn't a lack of demand, it's the ability to meet demand, and the ISM data continues to reinforce our view.

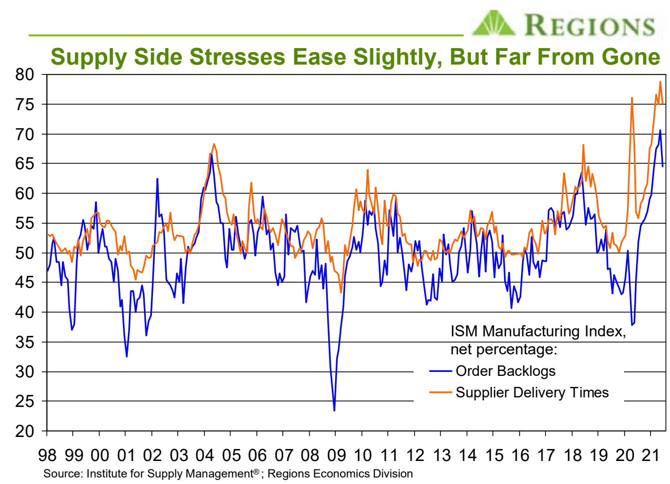
Of the 18 industry groups included in the ISM's survey, 17 reported expansion in June, up from 16 in May, with no industry group reporting contraction. June marks the ninth consecutive month in which at least 15 of the 18 industry groups reported growth, a sign of how broad based the expansion in the factory sector remains. Comments from survey respondents remain dominated by material shortages, shipping delays, and labor supply concerns, and a general theme is that firms would be producing more if they could be producing more. One respondent indicated that ongoing supply chain bottlenecks are causing customers to begin focusing on longer-term demand, placing orders for further out into the future than would be the case were supply chains and transport networks functioning normally. As to labor supply constraints, one respondent in the primary metals industry group put noted that "lack of labor is killing us" and while others may not have phrased it so starkly, they clearly share the sentiment.

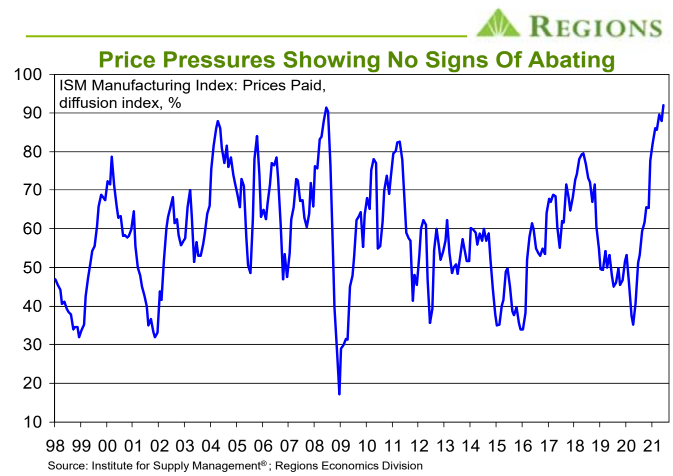
The new orders index slipped to 66.0 percent in June from 67.0 percent in May but nonetheless points to continued growth, with 15 of the 18 industry groups reporting growth in orders. Following back-to-back monthly declines, the production index increased to 60.8 percent in June but nonetheless remains below its recent peak of 68.1 percent, set in March. Fourteen of the 18 industry groups reported higher output in June with only one industry group reporting a decline. The employment index fell to 49.9 percent in June, ending a run of six months above the 50.0 percent mark, with ten industry groups reporting employment growth in June and five reporting declines. ISM notes widespread difficulty in filling open positions and that a "significant number of panelists are noting employee turnover due to wage dynamics in the markets." To the extent this reflects workers leaving for positions in other industry groups, as opposed to another job in manufacturing, it is certainly consistent with the degree to which wages have risen across all industry groups over recent months.

While the index of supplier delivery times slipped from 78.8 percent in May to 75.1 percent in June, manufacturers remain hamstrung by delivery issues, and the more relevant number is that 17 of the 18 industry groups reported slower delivery times in June. ISM notes that suppliers themselves are facing labor, materials, and delivery constraints, which are now expected to persist through the third quarter and possibly stretch into the fourth quarter. If so, this will further constrain manufacturers' ability to fill orders and will further weigh on their inventories of materials needed for production. That will contribute to further growth in backlogs of unfilled orders; order backlogs got larger in June, albeit at a slightly slower pace than in prior months.

The prices paid index jumped to 92.1 percent in June, the highest reading since July 1979 and the sixth straight month above 80.0 percent. All 18 industry groups reported paying higher prices for inputs in June. It seems likely that higher input, shipping, and labor costs will be passed along in the form of higher prices for final goods.







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