September 3, 2019

US Manufacturing: Down and Out, No Homecoming

- ISM-manufacturing sharply disappointed expectations…
- …including through weak details
- New export orders are at their weakest since 2009...
- ...as clear evidence Trump's policies are hitting US manufacturing…
- ...which may help to focus the minds toward trade peace
- The decline portends weakness in actual production
- Stocks fell, Fed rate cut bets intensified & the dollar depreciated

US, ISM Manufacturing Index, August:
Actual: 49.1
Scotia: 52.0
Consensus: 51.3
Prior: 51.2

President Trump's policies are bringing US manufacturing down and out instead of home, as evidenced by the latest reading on the health of the manufacturing sector. The headline disappointment is backed up by weak details. The USD depreciated and the two year Treasury yield plunged by nearly 8bps in the aftermath. The S&P500 fell by about 3/4% before regaining just over half of that thus far on raised Fed bets. Fed funds futures contracts are fully pricing a cut on September 18th and cumulative two and a half cuts by year-end. At about 11% of the US economy, the manufacturing sector is not, by its own, enough to induce recession, but this adds to the concerns.

There is little better evidence of the cost to the domestic economy stemming from the Trump administration's policies than the **sharp decline in new export orders** that coincides with Trump's increased tariffs announced in August. New export orders are contracting at the fastest pace since 2009 (chart 1). It's not the Fed that is behind this; economists outside of the Trump administration would likely universally agree upon the driver being Trump's tariffs.

Across other details summarized in the accompanying table, total new orders shrank and that sub-index reached 47.2 from 50.8. That ties the reading in June 2012 during the depths of the Eurozone crisis and that, in turn, was the weakest reading since April 2009.

The employment subcomponent fell 4.3 points to 47.4 which is the weakest reading since August 2016. Manufacturing is about 8% of nonfarm payroll employment.

The back log of orders subcomponent improved by 3.2 points to 46.3, but has remained in contraction for four consecutive months.

Prices paid (46.0 from 45.1) remained in contraction for the 3 straight months indicating weaker input prices such as WTI oil as well as the effects of the Trump administration's unwittingly strong dollar policies.

The headline manufacturing index correlates with longer term trends in US manufacturing output and suggests that there is further deterioration expected in manufacturing sectors. Chart 3 shows the movements between ISM-manufacturing and the three-month moving average of actual production.

Boston Fed President Rosengren will be the first FOMC official to speak in the aftermath of the report. This may give him some of the evidence of weakening that he would prefer to see before entertaining additional easing.

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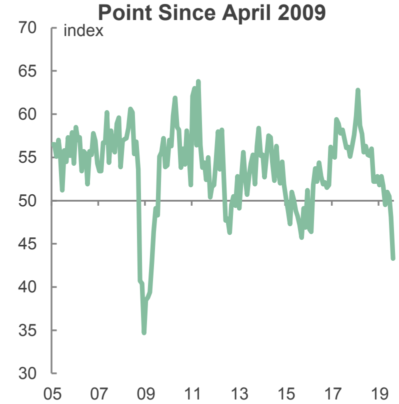
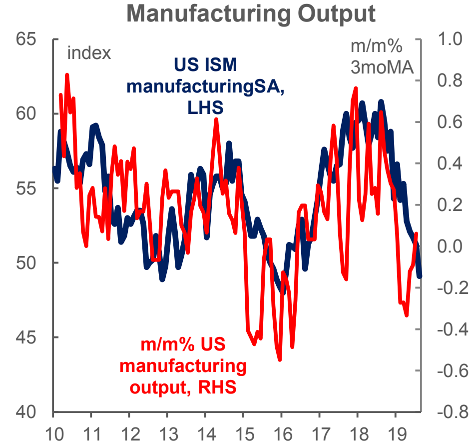


Sources: Scotiabank Economics, ISM.

Subcomponents of ISM Manufacturing, August

Seasonally Adjusted	Value	m/m
Composite	49.1	-2.1
New Orders	47.2	-3.6
Production	49.5	-1.3
Employment	47.4	-4.3
Supplier Deliveries	51.4	-1.9
Inventories	49.9	+0.4
New Export Orders	43.3	-4.8
Imports	46	-1.0
Not Seasonally Adjusted	**Value**	**m/m**
Customer Inventories	44.9	-0.8
Prices	46	+0.9
Backlog	46.3	+3.2

Value above 50 indicates expansion; value below 50 indicates contraction.



Sources: Scotiabank Economics.