



Economics Group

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Manufacturing Nearing Stall Speed

U.S. manufacturing activity continued to weaken in July, with the ISM manufacturing index slipping to 51.2. We expect weakness to persist amid global headwinds and continued uncertainty regarding trade policy.

Trade War, What Is It Good For?

The ISM manufacturing index slid lower for a fourth consecutive month in July, landing at 51.2. At this level, growth remains slightly positive, but is close to stalling out. The lack of visibility on any sort of trade resolution continues to hamper the sector, even as tensions eased up in July. Although U.S. activity is holding up better when compared to other major economies, domestic producers cannot escape the global manufacturing cycle. The continued deterioration comes in the context of last week’s news that the IMF downgraded its global growth forecast, and justifies some of the Fed’s concerns about a weakening global economy.

The production index fell more than three points to 50.8, its lowest level since 2016. A turnaround in the near term does not appear to be in store either. New orders remained worryingly close to contraction territory at 50.8. With the ISM reading on new orders still so low, the 1.9% jump in core capital goods orders in last week’s report on durable goods looks more likely to be noise than a sign of demand turning around.

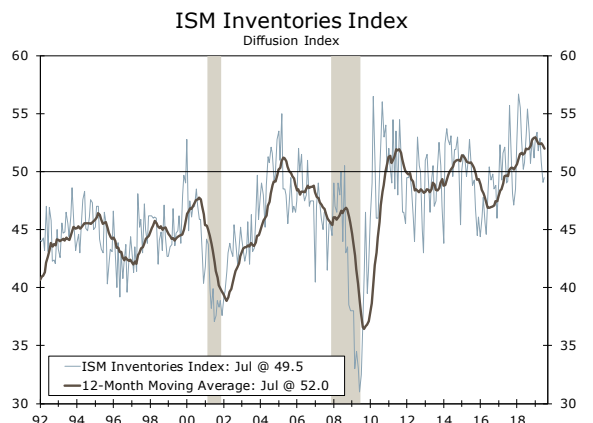
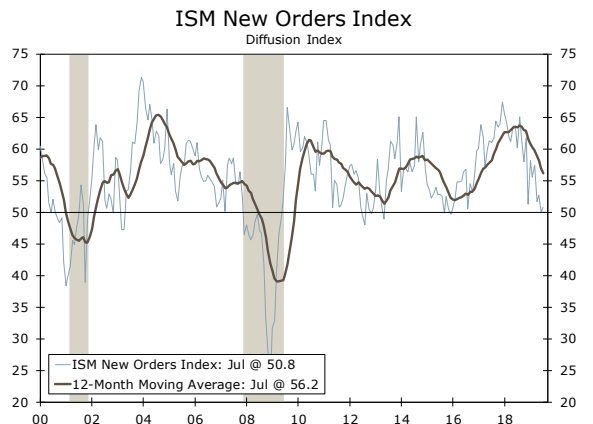
Export orders turned negative again in July as growth overseas continues to struggle. At 48.1, the index is at its lowest level since early 2016. Only three of 18 industries reported seeing exports increase, the fewest number of industries in more than four years. Only one industry reported increasing imports.

Prices are showing signs of weaker demand. Input costs are falling, with the prices paid index slipping to 45.1. Despite more manufacturers reporting falling input costs on net, tariffs continue to factor into pricing decisions. Respondents noted passing tariff effects through to customers—not just as they relate to China—remaining a general concern.

Manufacturers also continue to ease up on hiring, with the employment index slipping nearly three points. The decline to 51.7 supports our expectations for weaker hiring in the manufacturing sector in tomorrow’s July payroll report after a surprisingly strong gain of 17K jobs last month.

Looking ahead, we expect the manufacturing sector to continue to expand, but at an anemic rate. The overhang of inventories at the start of the year has been worked down, as inventories fell for a second straight month in July based on today’s report. That should soften the blow of worsening new orders and a sharply declining backlogs.

While a resolution to trade issues between the United States and China appears to remain a ways off, an escalation has been tabled for the time being as negotiations have resumed. This holding pattern on trade policy should also help to stabilize the manufacturing sector. While domestic demand for U.S. manufacturers remains favorable, weak growth abroad and some renewed strength in the dollar will continue to pose headwinds for the sector.



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