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## October Industrial Production: Motor Vehicles Not The Only Drag On Manufacturing

- › Industrial production **fell** by 0.8 percent in October, with manufacturing output **down** by 0.6 percent
- › The overall capacity utilization rate **fell** to 76.7 percent, while the utilization rate in manufacturing **fell** to 74.7 percent
- › On a year-over-year basis, total industrial production was **down** by 1.1 percent in October, with manufacturing output **down** by 1.5 percent

Total output amongst the nation's factories, mines, and utilities fell by 0.8 percent in October, doubling down on our forecast of a 0.4 percent decline, with manufacturing output falling by 0.6 percent thanks in large measure, but not solely, to another sharp decline in motor vehicle production due to the GM strike. Mining output fell by 0.7 percent in October, with utilities output dropping by 2.6 percent. The overall capacity utilization rate fell to 76.7 percent in October, with the utilization rate in the manufacturing sector slipping to 74.7, the lowest utilization rate in the factory sector since March 2017. To be sure, with the GM strike having been settled, motor vehicle production will rebound, likely sharply, in the November data, and that will in turn be reflected in the headline industrial production number. We'd caution, however, against brushing aside the weak September and October data on the grounds that it is simply noise resulting from the GM strike. As we noted in our weekly *Economic Preview*, the list of what ails the manufacturing sector has more on it than the GM strike, and to that point ex-auto manufacturing output declined for a second straight month in October. The November and, to a lesser degree, December data on manufacturing output will reflect payback as GM production comes back on line, meaning the data on ex-auto manufacturing output will be the more useful guide to the health of the factory sector. While we expect the data to show conditions are stabilizing, it is hard to see a catalyst for a meaningful rebound in activity in the manufacturing sector.

Assemblies of automobiles and light trucks fell to an annualized rate of 8.812 million units in October, a 12.7 percent decline from September, which itself saw a 6.8 percent decline in assemblies. October's pace is the slowest monthly pace since September 2011 when the industry was still climbing out of the deep hole that was the 2007-09 recession. As we noted last month, the noise, both upside and downside, from the GM strike should not deflect attention away from what prior to the strike had been a downward drift in production. This reflects a slowing pace of motor vehicle sales to consumers, and had fleet sales not been as strong as they have been over recent months the decline in production would have been more pronounced, though there are signs that this support has already started to fade. Though assemblies of heavy trucks remain fairly steady, what is growing excess capacity in truck transportation suggests assemblies of heavy trucks will weaken at some point.

Aside from motor vehicles, output of computers, electrical equipment, chemicals, and fabricated metals also fell back in October. Production in the broad business equipment category, a marker of trends in broader business investment as measured in the GDP data, fell by 0.6 percent in October, which comes on the heels of a 1.1 percent decline in October. This joins other high frequency data, such as core capital goods orders, in pointing to a weak print on business investment in equipment and machinery in the Q4 GDP data after a contraction in Q3 – back-to-back contractions in this category are rare outside of recessionary periods. Though idle capacity in the motor vehicles segment resulting from the GM strike is clearly weighing on the capacity utilization rate in the manufacturing sector, that is not the only culprit, as utilization rates remain notably low across a wide swath of industry groups. These low utilization rates call into question the need for firms in these industry groups to invest in additional capital, which would bode poorly for any rebound in business investment. We've questioned, however, whether this is idle capacity or, given the advanced age of the capital stock, obsolete capacity that is still lingering on the books. To the extent this idle capacity is functional, that would suggest little upside room for business investment but if, as we've argued, it is obsolete, that points to more upside room for business investment than is implied by simply looking at utilization rates. Unless and until there is clarity on trade and firmer business sentiment, however, that will remain a purely academic question.

