ECONOMIC UPDATE

REGIONS

April 1, 2020

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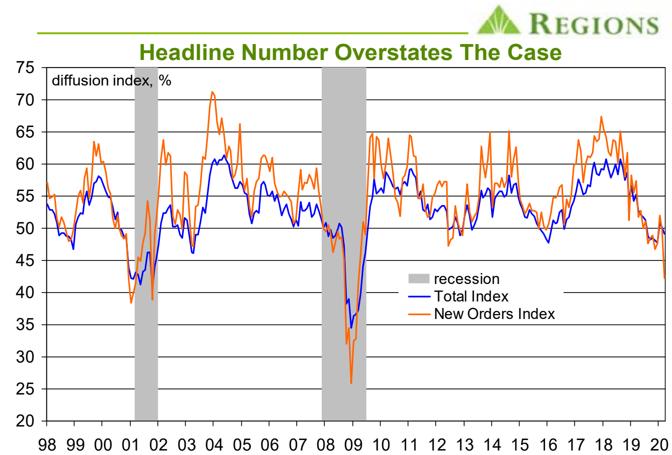
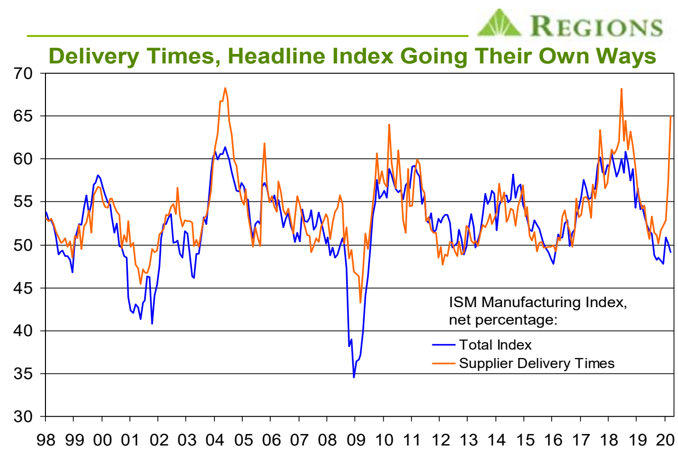
March ISM Manufacturing Index: Headline Number Overstates The Case

- The ISM Manufacturing Index fell to 49.1 percent in March from 50.1 percent in February
- The new orders index fell to 42.2 percent, the employment index fell to 43.8 percent, and the production index fell to 47.7 percent

The ISM Manufacturing Index fell to 49.1 percent in March, topping our above-consensus forecast of 46.0 percent and faring better than many had feared in the wake of the sudden and widespread halt of economic activity seen in March. That said, the ISM Manufacturing Index is yet another example of a point we routinely make, which is that the headline number is the least informative number in most data releases, with the details beneath the headline number telling you what is really happening. The details of the ISM's March survey are much weaker than the headline number, and the details will get even worse in the months ahead. At some point, the headline index will follow the details down to a much greater extent than is the case in the March data.

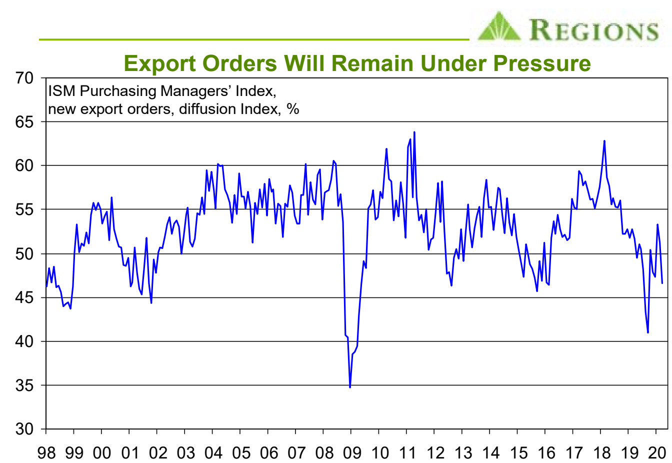


As we noted in our weekly *Economic Preview*, slower supplier delivery times work to push the headline index numbers in the ISM's manufacturing and non-manufacturing surveys higher. The premise is that slower delivery times are a sign of greater demand and, as such, act as a positive in the ISM's indexes. The measure of supplier delivery times, however, makes no distinction between stronger demand and impaired supply chains, and it is clearly the latter, in the fallout from the coronavirus, that is responsible for the sharp slowdown in supplier delivery times reported in the manufacturing survey over the past two months. ISM acknowledges this point in today's release by noting "the high (supplier delivery) index reading in March was primarily a product of coronavirus-related supply problems." Obviously, ISM cannot be expected to change their methodology out of the blue in response to special circumstances, so this is by no means to be taken as criticism of them, but instead is simply a caution to look to the details of the March data as a better gauge of factory sector conditions. Our middle chart illustrates the extent to which the supplier delivery times sub-index and the headline index went their own ways over the past two months. Had the supplier delivery times sub-index not risen so sharply in March (up to 65.0 percent), the decline in the headline index would have been worse.



Ten of 18 industry groups included in the ISM's survey reported growth in March, down from 14 in February, while six industry groups reported contraction. Comments from survey respondents were mostly negative, which comes as no surprise under the circumstances – in addition to the fallout from the coronavirus, the marked weakening in the energy sector is weighing on the factory sector. One notable comment came from a firm in the food, beverage, & tobacco products industry group, noting that they were seeing a "record number of orders due to COVID-19."

The new orders index, which we often note is one of our favorite forward looking indicators, fell to 42.2 percent in March, the lowest reading since March 2009. It is likely that the new orders component will fall further in the April survey. The index of production fell to 47.7 percent, a smaller decline than our forecast anticipated, but only 7 of the 18 industry groups reported higher production in March. The employment index fell to 43.8 percent in March, the lowest reading since May 2009. Only 3 of the 18 industry groups reported employment increased in March while 13 reported lower levels of employment. These details suggest the March employment report, to be released Friday, could show a larger than expected decline in manufacturing employment, though timing effects will push the biggest declines off to the April employment report. Backlogs of unfilled orders contracted in March, the tenth contraction in the past eleven months. Combined with declining new orders, the fading backlog of unfilled orders points to further declines in factory employment and output in the months ahead. Also contributing to those declines will be falling export orders, as trade flows have slowed sharply amidst the fallout from the coronavirus. In short, even focusing on the weak details, the ISM's March survey is but a modest preview of what's to come in the months ahead. This will be a common theme across the data releases for March.



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