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April ISM Manufacturing Index: Supply-Side Stresses Weigh On Expansion

- › The ISM Manufacturing Index fell to 55.4 percent in April from 57.1 percent in March
- › The new orders index fell to 55.3 percent, the employment index fell to 50.9 percent, and the production index fell to 53.6 percent

The ISM Manufacturing Index fell to 55.4 percent in April, below what we (57.9 percent) and the consensus (57.6 percent) anticipated and the lowest reading since July 2020. While April marks the 23rd straight month in which the headline index was above the 50.0 percent break between contraction and expansion, the details of the April survey indicate a slower pace of growth with renewed supply chain stresses taking a toll while price pressures remain intense. While survey respondents maintain a favorable outlook for demand, they were notably less upbeat in the April survey than was the case in the March survey. That said, the most likely course seems to be continued expansion in the manufacturing sector in the months ahead but at a slower pace absent more broad based relief from supply side constraints.

Of the 18 industry groups included in the ISM's survey, 17 reported expansion in April, up from 15 in March with petroleum & coal products the only industry group reporting a decrease in activity. ISM reports that for each cautious comment on demand in the April survey, there were three positive comments, down from the six-to-one ratio in the March survey. Comments relayed by ISM note ongoing strength in demand, but what is more interesting is that takes on supply chain/logistics constraints vary across industry groups. Some industry group, including non-metallic mineral products and transportation equipment, note some easing of supply-side constraints while others, including chemical products and machinery, note no improvement. The latest round of shutdowns in China are impacting production in some industry groups.

The new orders index fell to 53.5 percent in April from 53.8 percent in March, with 11 of the 18 industry groups reporting growth in orders and three reporting lower order volumes. On the firm level, however, just 25.1 percent reported higher orders in April, the lowest share since January. It could be that sizable, and still growing, order backlogs, sustained price pressures, and uncertain delivery times are impacting growth in new orders, which ultimately will be reflected in employment and output. The narrowing breadth of orders growth is a counter to the still-upbeat tone of comments by survey respondents on the strength of demand, and the new orders index dropping below 50.0 percent would be a clear warning sign, not only for the manufacturing sector but also for the broader economy. The production index fell from 54.5 percent in March to 53.6 percent in April, though 14 of the 18 industry groups reported higher output while only two reported lower output. The employment index slipped to 50.9 percent in April from 56.3 percent in March, the lowest reading since August, with some respondents indicating higher numbers of quits and increasing difficulty in filling open positions.

Though they did so at a slower rate, backlogs of unfilled orders continued to grow in April, with 10 of the 18 industry groups reporting larger backlogs and two reporting smaller backlogs. With slower growth in new orders and further growth in output, it makes sense that the growth in order backlogs has slowed some, but unfilled orders nonetheless remain sizable, indicating that order cancellations are not yet common across industry groups. The supplier delivery index rose in April by more than our forecast anticipated, with 16 industry groups reporting slower delivery times and none reporting faster delivery times. In addition to sourcing issues, suppliers continue to contend with labor supply challenges. It is interesting to note that, while firms reported growth in inventories of inputs in April, that growth slowed substantially, with a jump in the percentage of firms reporting lower inventories. At 51.6 percent, the inventory index is in danger of tipping under the 50.0 percent threshold which, were that to occur, would act as a further weight on output growth. Though down from 87.1 percent in March, at 84.6 percent the prices paid index indicates ongoing upward pressure on non-labor input prices, with 17 of the 18 industry groups reporting paying higher prices. Thus far, firms have been successful in passing higher input costs along to customers, but this pricing power will dissipate rapidly if demand slows.

