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July ISM Manufacturing Index: Uninspired "Bounce" Leaves Factory Sector Stuck In A Rut

- › The ISM Manufacturing Index rose to 46.4 percent in July from 46.0 percent in June
- › The new orders index rose to 47.3 percent, the employment index fell to 44.4 percent, and the production index rose to 48.3 percent

The ISM Manufacturing Index rose to 46.4 percent, below what we and the consensus expected, indicating a ninth straight month of contraction in the factory sector. While there was some improvement in key components such as production and new orders, those indexes nonetheless remain below the 50.0 percent break between contraction and expansion. Moreover, the employment index plummeted to a level last seen in the early phases of the pandemic, suggesting the labor hoarding behavior ISM noted earlier this year may be turning into capitulation as firms who had been banking on a second half rebound are adapting to a less benign reality. The continued contraction in new orders while backlogs of unfilled orders are further pared down suggests little relief is in sight for the factory sector, particularly as producers of transportation equipment, which had been one of the few bright spots on the manufacturing landscape, reported contraction in July. Whether that simply marks seasonal shutdowns amongst producers of motor vehicles or something more ominous remains to be seen. Either way, there seems little impetus for the ongoing contraction in the factory sector to reverse any time soon, particularly with the domestic and global economies looking to slow further.

Only two of the eighteen industry groups included in the ISM's survey reported growth in July, matching December 2022 and January 2023 as the fewest in any month since the early days of the pandemic. Conversely, sixteen of the eighteen industry groups reported contraction in July including, as noted above, transportation equipment. Comments from survey respondents show several industry groups contending with slowing demand, and one notable comment pointed to "softening" in China markets as that country's economy is faltering after an initial reopening bounce. It is also worth noting that one respondent from the transportation equipment industry group stated that back orders have been "mostly resolved," notable in that vehicle producers scrambling to backfill production and inventories in the wake of prolonged supply chain snarls have largely caught up, particularly with higher financing costs and more stringent lending standards weigh on demand for vehicle purchases.

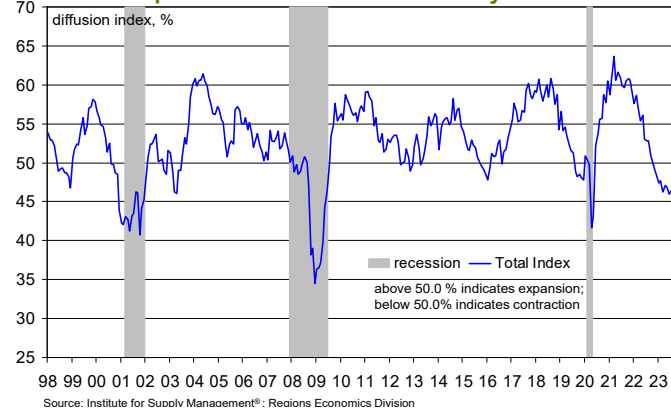
As we anticipated, the index of new orders notched a second straight monthly increase but nonetheless remains below 50.0 percent, indicating new orders continue to decline even if at a slightly slower pace. More noteworthy is that only four of the eighteen industry groups reported growth in new orders in July. Contrast this to the breadth of orders growth seen in the early phases of reopening and seen over the course of the expansion that prevailed in the years ahead of the pandemic, as we show in our middle chart. That producers of transportation equipment reported lower order volumes in July suggests there is more than seasonal patterns behind the overall contraction in this industry group in July. The production index also rose but remained below the 50.0 percent threshold, with only three industry groups reporting higher output. As noted above, the employment index plummeted in July, falling to 44.4 percent, with three industry groups reporting higher head counts and eight reporting declines. Again, in contrast to the labor hoarding noted by ISM earlier this year, they now report firms trimming payrolls to match shrinking order books.

Though not entering into the calculation of the headline index, the indexes of export orders and import volumes are nonetheless instructive as to overall conditions in the factory sector. New export orders have fallen in eleven of the past twelve months, and respondents point to weak conditions in China and Europe as weighing on growth. Import volumes fell for the ninth straight month, which is noteworthy in that imports of intermediate capital goods used in domestic production account for a sizable share of total imports into the U.S. As such, sagging import volumes are an indication of weakness in production amongst U.S. firms

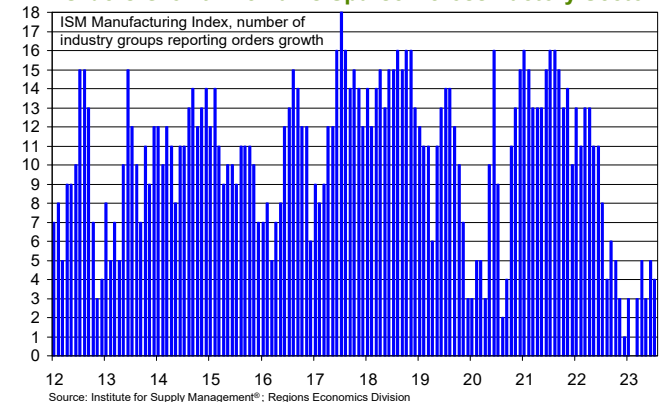
The prices paid index slipped to 42.6 percent, indicating further declines in input prices. It remains to be seen whether recent increases in energy and commodity prices will at some point put upward pressure on input prices despite still-weak demand.



An Uninspired "Bounce" Leaves Factory Sector In A Rut




Orders Growth Remains Sparse Across Factory Sector




Diminished Trade Volumes Sign Of Weakness

