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March ISM Manufacturing Index: Headline And Details Align This Time As Growth Returns

- › The ISM Manufacturing Index rose to 50.3 percent in March from 47.8 percent in February
- › The new orders index rose to 51.4 percent, the employment index rose to 47.4 percent, and the production index rose to 54.6 percent

The ISM Manufacturing Index rose to 50.3 percent in March, coming in ahead of our above-consensus forecast of 49.1 percent and, more importantly, ending a run of sixteen straight months of contraction in the factory sector. After a run this long, the first question that may spring to mind is whether the headline index topping the 50.0 percent break between contraction and expansion is a one-off fluke or whether it marks the start of a sustained expansion. Obviously, we'll only know the answer to that over time, but there are at least some encouraging signs in the March data to suggest the latter rather than the former. Recall that in each of the prior two months we noted that the headline index was out of alignment with the details of the data, with the headline index outperforming the details in the January data and underperforming the details in the February survey. As such, we felt better about conditions in the factory sector after the February survey, which showed a dip in the headline index, than we did after the January survey, which showed the headline index rising to its highest point since October 2022. Not only did the headline index top that 50.0 percent threshold in March, but the details of the data and comments from survey respondents point to a more constructive outlook. Recall that for some time we have noted our expectations that conditions in the factory sector would be on a firmer path over the second half of this year, and while you'd be getting ahead of yourself if you were expecting a blistering pace, it is reasonable to expect continued growth, however, halting and uneven, in the factory sector in the months ahead.

Of the eighteen industry groups included in the ISM's survey, nine reported growth in March, up from eight in February and the most in any month since September 2022. ISM notes demand remains in "the early stages of recovery," but with "clear signs of improving conditions." That mirrors comments from survey respondents, most of which either point to surprisingly durable demand or expectations of firming demand over coming months. On the whole comments from survey respondents are consistent with our expectations of production and shipments rising over coming months.

The new orders index rose to 51.4 percent in March, with twelve of the eighteen industry groups reporting higher orders, up from eleven in February, and only two – furniture & related products and transportation equipment – reporting lower orders. We have for some time been noting that increased breadth of orders growth was a necessary precondition for the factory sector to transition from contraction to expansion, but both have come faster than we had expected. The twelve industry groups reporting orders growth in March is the most in any month since April 2022, and it is also worth noting that March is the third straight month in which a higher share of firms – as opposed to industry groups – reported higher orders and a smaller share reported lower orders. The production index rose to 54.6 percent in March, its highest point since June 2022, with thirteen industry groups reporting increased production and only two reporting lower output. As we anticipated would be the case, the employment index rose in March but, at 47.4 percent, nonetheless remained below the 50.0 percent breakeven mark. Seven industry groups reported increased payrolls in March, while eight reported declines. ISM reports firms continue to use layoffs, as opposed to attrition or hiring freezes, as the primary means of lowering headcounts. That said, if the increases in the new orders and production indexes are sustained in the months ahead, growth in employment will follow. It is also worth noting that the index of new export orders posted a second straight month above the 50.0 percent mark, with a growing number of respondents pointing to firming growth from abroad, which is an encouraging sign not only for domestic manufacturers but for the global growth outlook over coming months.

Prices for non-labor inputs to production rose for a third straight month in March, a span over which growing shares of firms and growing shares of industries reported paying higher prices. While this is a clear indication of an increased pace of activity in the factory sector, the flip side is that this points to upward pressure on prices for capital and consumer goods, re-opening another front in the FOMC's battle against inflation.

