# ECONOMIC UPDATE

REGIONS

February 3, 2025

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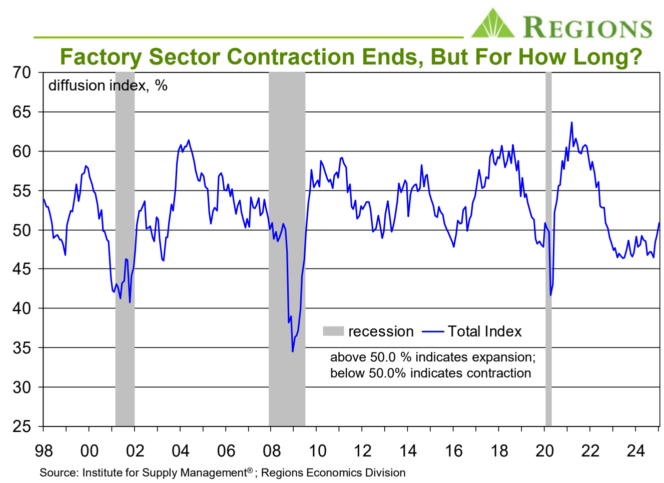
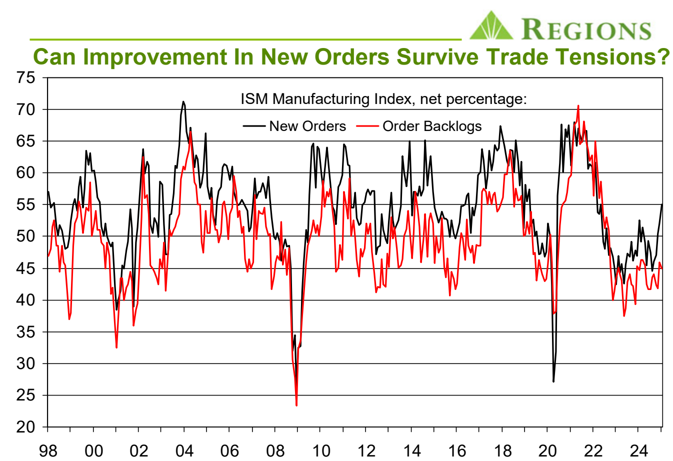
## January ISM Manufacturing Index: Contraction Ends, But For How Long?

- The ISM Manufacturing Index rose to 50.9 percent in January from 49.2 percent in December
- The new orders index rose to 55.1 percent, the employment index rose to 50.3 percent, and the production index rose to 52.5 percent

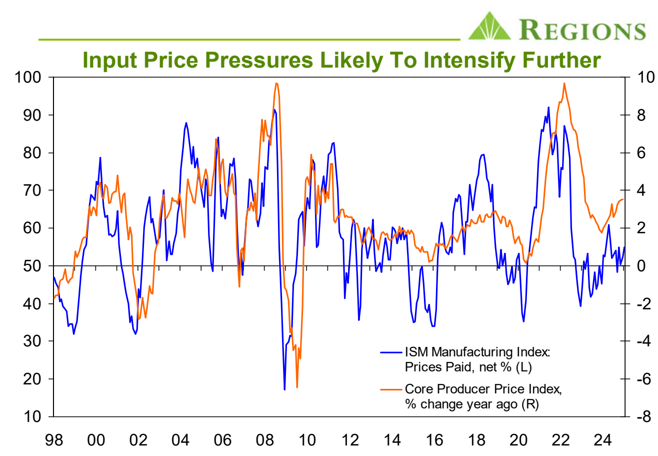
The ISM Manufacturing Index rose to 50.9 percent in January, topping our above-consensus forecast of 50.3 percent and ending a run of twenty-six straight months of contraction. Note that, as in each year, the January data incorporate revisions to the recent historical data, and in that process what had previously been reported as a reading above the 50.0 percent break between contraction and expansion last March has been revised lower, hence the twenty-six month streak. Of more relevance, the details of the January data do hint at genuine improvement in conditions in the factory sector; recall that in our preview of the January data we noted that the above-50.0 percent print we expected could easily reflect the quirks in the manner in which the ISM's diffusion indexes are calculated as opposed to signs of genuine improvement. While we're happy to have been wrong on that front, that the release of the January data comes amid what, at least as we're writing this, appears to be a significant escalation in global trade tensions that is unlikely to work out all that well for the manufacturing sector will likely temper any enthusiasm around the improvement in the data. That is a worry for tomorrow, specifically, 12:01 AM tomorrow, so for now we'll just focus on the results of the ISM's January survey.




Eight of the eighteen industry groups included in the ISM's survey reported growth in January, and while less than half this is nonetheless the most in any month since June. Several of the comments from survey respondents relayed by ISM noted improvement in demand while several cited uncertainty around tariffs and one noting that Chinese caps on mineral purchases were causing supply chain problems. One respondent expressed relief that the potential port strike last month was averted.




The new orders index, which we always consider the single most important component of the monthly surveys, rose to 55.1 percent in January from 52.1 percent in December. Nine of the eighteen industry groups reported growth in orders in January, the most in any month since last March, while five industry groups reported lower orders. To our point about whether or not the diffusion index printing at over fifty percent reflects genuine improvement, January saw a meaningful increase in the percentage of firms reporting higher orders and a meaningful decline in the percentage of firms reporting lower orders, which was not the case in December even though the diffusion index printed over fifty percent. Moreover, ISM reports a two-to-one ratio of positive comments versus comments expressing concern about near-term demand, the best in some time. Again, though, it remains uncertain whether, or to what extent, this improvement can be built on in the months ahead given escalating trade tensions. One telling sign of the importance of sustained improvement in new orders is that backlogs of unfilled orders continue to contract, with January marking the twenty-seventh straight month of slimming backlogs. Without sustained improvement in new orders, thinning backlogs of unfilled orders pose risks to employment and output in the factory sector.




The production index rose to 52.5 percent in January, while the employment index rose to 50.3 percent, up from 45.4 percent in December. ISM notes that less workforce reduction activity was taking place as 2025 kicked off, which is an improvement over the past several months when firms were resorting to attrition and layoffs to manage headcounts. There is, however, reason for caution around the January data, as less than one-fifth of firms reported higher output in January and only around twelve percent reported adding workers, neither exactly a firm foundation for sustained growth. This goes straight to our point about the diffusion indexes and the firm level data often telling different stories, and also goes to our point about the importance of the recent growth in new orders being sustained over coming months.

Upward pressure on prices for non-labor inputs intensified in January, with the prices paid index rising to 54.9 percent, with a meaningfully higher percentage of firms reporting paying higher input prices. We'd noted the oddity of input prices pushing higher despite the factory sector being in contraction, and with conditions firming and tariffs seeming likely to increase, price pressures could continue to intensify going forward.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