ISM: U.S. Manufacturing Hits Rough Patch

Mike Schmidt. Associate Editor, Manufacturing Business Technology

It looks like U.S. manufacturing has hit rough patch.

While the overall economy experienced its 38th straight month of growth, economic activity in the manufacturing sector contracted in July for the second consecutive month, according to the latest *Manufacturing ISM Report on Business*.

Bradley J. Holcomb, CPSM, CPSD

“We’re looking at a softness and a slowdown in demand for manufacturing products, both domestically and internationally,” says Brad Holcomb, CPSM, CPSD, chair of the Institute for Supply Management Manufacturing Business Survey Committee.

“Any improvements over the next few months will be gradual and incremental,” he adds.

The PMI registered 49.8 in July, an increase of 0.1 percentage point when compared to last month’s reading. A reading above 50 indicates the manufacturing economy is generally expanding. A reading below 50 percent indicates that it is generally contracting.

New Orders and Exports

According to Holcomb, new manufacturing orders are a significant driving force behind economic activity in the sector as a whole – for better or for worse. Therefore, the performance of the ISM New Orders Index and the ISM Exports Index can accurately speak to the health of manufacturing. Lately, both indexes have not performed so well.

ISM’s New Orders Index registered 48 percent in July. Yes, that marked an increase of 0.2 percentage point when compared with the June reading of 47.8 percent. However, the index dipped below 50 in June for the first time since April of 2009. Perhaps even more disconcerting is the fact that only three of the 16 industries surveyed by ISM reported growth in new orders in July. Seven reported growth in June.

Meanwhile, ISM’s New Export Orders Index registered 46.5 percent in July, one percentage point lower than the 47.5 percent reported in June.

“We always talk about new orders sort of driving this system, and that’s been off for two months in a row,” says Holcomb. “A component of that is exports, which is down another point and also contracting.”

Employment

One index that saw growth (albeit less than in the past) was employment. ISM's Employment Index registered 52 in July, but that was still down 4.6 percentage points over the previous month's mark of 56.6.

The sharp percentage point drop gives Holcomb cause for concern.

"The fact that it remains in positive territory is certainly good and welcome news," he says. "How long it can stay there is another matter. If new orders don't materialize, then all bets are off."

Inventories and Prices

The ISM Inventories Index saw a five-point jump over last month, registering 49 in July. Holcomb pointed to a low ISM Prices Index of 39.5 as one key reason for the buildup in inventories.

"What I think is behind this is the low and decreasing prices for two and now three months has encouraged these companies to purchase inventories at lower prices, but unfortunately there hasn't been enough pull-through from new orders," says Holcomb.

All in all, Holcomb says economic activity in the manufacturing sector could grow or contract in the coming months. Meanwhile, growth in the overall economy continues to inch along in a positive direction.

ISM's correlations, which it redoes with the Department of Commerce each year, indicate that every PMI about 42.6 generally indicates expansion in the overall economy.

"So we can safely say the overall economy continues to expand and has done so for 38 consecutive months," he adds. "That is really a good situation in total, but if manufacturing continues on this same trend, then we are starting to chip away at the upside possibilities."

In his role as the Chair of the Institute for Supply Management Manufacturing Business Survey Committee, Bradley J. Holcomb writes the monthly Manufacturing ISM Report on Business based on the survey results of approximately 350 professionals across 18 different industry sectors. The Report on Business is released on the first business day of each month, and features the PMI Index as its key measure. For more information on the Institute of Supply Management, visit www.ism.ws *[1].*

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