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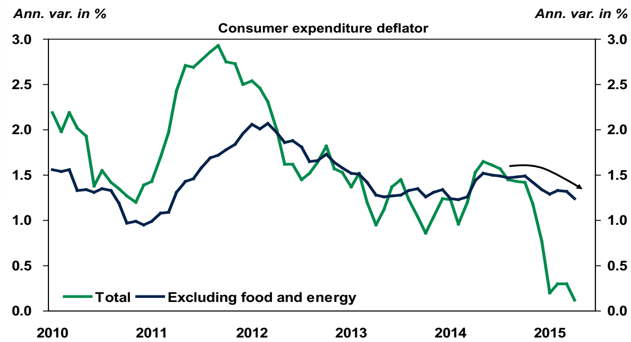
UNITED STATES

The manufacturing ISM is finally up, but consumption stagnates

HIGHLIGHTS

- The ISM manufacturing index increased from 51.5 to 52.8 in May. Eight of the ten sub-indexes are up. The main gains are in new orders (+2.3 points), employment (+3.4 points) and order backlogs (+4.0 points). In addition, the prices paid component shot up 9.0 points to 49.5. Current production (-1.5 points) counts among the sub-indexes that are down.
- Real consumption stagnated in April following a 0.5% increase in March. Consumption of goods contracted 0.4%, while spending on services only increased 0.1%. Real disposable income advanced 0.3%. The annual change in the consumer expenditure deflator continues to be sluggish at 0.1%, and the change in the core deflator, which excludes food and energy, slowed from 1.3% to 1.2%.

The consumer expenditure core deflator is also showing signs of weakness



Sources: Bureau of Economic Analysis and Desjardins, Economic Studies

COMMENTS

Increasing stronger than the consensus called for, the manufacturing ISM finally seems to be leaving behind the downward trend it has been suffering since the latest cyclical high of 58.1 in August 2014. The monthly increase of 1.3 points seen in May is even more remarkable as many regional manufacturing indicators continued to deteriorate during the month.

The increase in the new orders component is especially welcome. Orders have recently been hard hit by the weather, the conflict in West Coast ports and, especially, by the sharp decline in investment in the oil sector. The recovery began in April, and in May the sub-index reached its best level this year. This could signal that weakness in business investment within GDP is coming to an end.

For households, weakness in real consumption is no big surprise. The weakness in goods has already been felt in automobile and retail sales. After the cold winter, the 5.1% retreat in energy prices in April limited the advance of services consumption, while the data on food services suggested better growth. We also note that U.S. households are becoming more cautious; the savings rates continues to be up, going from 5.2% to 5.6% from March to April. Therefore, despite strong income growth, supported by job creation and lower gas prices, households are still not inclined to ramp up spending. We must hope that it is just a matter of time and that the remainder of spring will see consumption deliver a more encouraging performance.

Implications: After several months falling or stagnating, the manufacturing ISM finally seems to be waking up; this should lead to better growth in investment, which would help the U.S. economy rebound from the disappointing 0.7% contraction recorded in the first quarter. The situation is less clear for consumption, but growth in personal income remains encouraging. The Federal Reserve (Fed) could become worried about weakness in the core deflator, however, which is on a downward slope. If this inflation indicator does not show signs of a recovery soon, the Fed could be tempted to further delay its initial rate increase.

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Note to readers: The letters k, M and B are used in texts and tables to refer to thousands, millions and billions respectively.