

September 1, 2016



UNITED STATES

The ISM manufacturing index falls back below the 50 mark!

HIGHLIGHTS

- After sitting above the 50 mark for five straight months, the ISM manufacturing index dropped in August, from 52.6 to 49.4.
- Nine of the ten sub-indexes lost ground. The main declines were in new orders (-7.8 points) and current production (-5.8 points). The prices paid component fell by 2.0 points, coming in at 53.0. The employment component lost 1.1 points to reach 48.3, its lowest level since March.
- The only index that did not decline was that of exports, which remained stable.

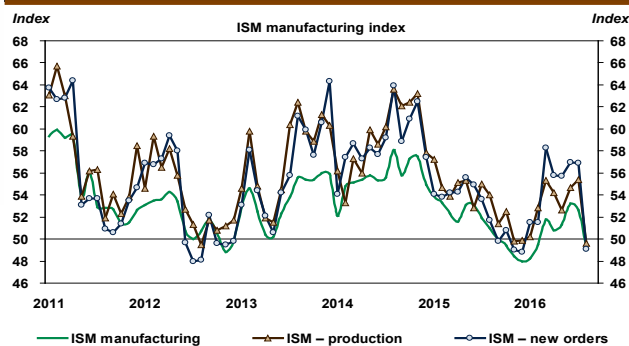
COMMENTS

While not extremely high, the ISM manufacturing index had been showing some improvement since the winter. From late 2015 to early 2016, it had stayed below the 50 mark, which is the dividing line between growth and contraction of manufacturing activity. Its recent low was 48.0 in December 2015. That weakness was subsequently reflected in disappointing U.S. real GDP growth in the first half of 2016. The ISM later climbed to 53.2 in June, only to fall back in July, and again in August.

Declines in some of the regional manufacturing indexes in recent weeks pointed towards a drop in the ISM manufacturing index for the month of August. The consensus was expecting a slight dip, from 52.6 to 52.0. What is surprising, then, is the size of the drop and, more importantly, the fact that it has fallen back below the 50 mark.

One thing that is particularly disappointing is the pullback in the new orders component. Having averaged 56.7 between March and July, it was suggesting improvement in business investment. In fact, new capital goods orders other than defence and aviation recently posted two consecutive monthly increases, for the first time since January 2015. Thus the 7.8-point drop in the ISM new orders component seriously undermines that upward movement.

Sharp drop in the ISM manufacturing index and its main components in August



Sources: Institute for Supply Management and Desjardins, Economic Studies

Implications: The slump in the ISM manufacturing index is a bad news story that reawakens doubt about the strength of the U.S. economy. At a time when the Federal Reserve (Fed) was starting to show that it might soon consider raising its key interest rates, this weakness in the ISM could temper the enthusiasm of some of its leaders. However, we should keep in mind that the Fed decided on its first interest rate hike of this cycle in December 2015, when the ISM was even lower than it is now. Furthermore, the Fed will wonder whether the August data is truly representative, or merely a temporary hiccup in a more positive economic trend. The future decisions by Chair Yellen and her colleagues will depend on what happens with the other indicators, especially those relating to the labour market.

Francis Généreux
Senior Economist

François Dupuis
Vice-President and Chief Economist

Hélène Bégin
Senior Economist

Benoît P. Durocher
Senior Economist

Francis Généreux
Senior Economist

514-281-2336 or 1 866 866-7000, ext. 2336
E-mail: desjardins.economics@desjardins.com

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

IMPORTANT: This document is based on public information and may under no circumstances be used or construed as a commitment by Desjardins Group. While the information provided has been determined on the basis of data obtained from sources that are deemed to be reliable, Desjardins Group in no way warrants that the information is accurate or complete. The document is provided solely for information purposes and does not constitute an offer or solicitation for purchase or sale. Desjardins Group takes no responsibility for the consequences of any decision whatsoever made on the basis of the data contained herein and does not hereby undertake to provide any advice, notably in the area of investment services. The data on prices or margins are provided for information purposes and may be modified at any time, based on such factors as market conditions. The past performances and projections expressed herein are no guarantee of future performance. The opinions and forecasts contained herein are, unless otherwise indicated, those of the document's authors and do not represent the opinions of any other person or the official position of Desjardins Group. Copyright © 2016, Desjardins Group. All rights reserved.