TD Economics

February 2, 2015

Data Release: U.S. manufacturing activity continued to moderate in January

- The Institute for Supply Management (ISM) manufacturing index fell 1.6 points to 53.5 in January from a downwardly revised reading of 55.1 in December. This marked the lowest level since exactly a year-ago. The headline print was well below market expectations, which called for the index to soften to 54.1.

- The slowdown was broad-based, with most sub-components edging lower on the month. Backlog of orders (-6.5), supplier deliveries (-5.7), new orders (-4.9) and prices paid (-3.5) sub-components led the declines. Production (-1.2) and employment (-1.9) were also lower in January.

- Meanwhile, inventories (+5.5) and imports (+0.5) were the only two sub-components to post gains on the month.

- With new orders falling and inventories rising, the spread between the two – which tends to be a leading indicator of future activity – has narrowed sharply to just 1.9 from 12.3 in December.

- Some of the decline in activity could be related to the dock slowdown and increased congestion at West Coast ports due to ongoing labor issues. Respondents from more than one industry cited that the situation is causing significant delays and logistical challenges.

Key Implications

- This was a disappointing report, with activity in the manufacturing sector decelerating to its weakest pace in a year. Details of the report added to the downbeat sentiment, with broad-based weakness across key forward-looking indicators such as new orders, backlog of orders, and employment, in addition to a contraction in new orders-to-inventories spread. Decelerating manufacturing activity points to some moderation in U.S. economic growth in the first quarter of the year.

- Despite the slowdown, the measure remains above the 50-point threshold, which corresponds to expanding activity in the manufacturing sector. Ongoing growth in the sector is corroborated by the fact that just two out of eighteen surveyed industries – textile mills and nonmetallic mineral products – reported a contraction in January. Moreover, delivery backlogs at the West Ports could have exaggerated the slowdown in the index.

- American manufacturers face opposing forces of stronger U.S. dollar on one hand and lower commodity prices on the other. Both of these were highlighted in today's report with prices paid and exports sub-components extending their declines in January and weighing on the headline. While exporters will continue to face competiveness challenges, at the end of the day, the benefit to American consumers from lower energy prices is likely to win out, increasing demand for U.S. manufactured goods and supporting ongoing growth in the sector.

Ksenia Bushmeneva,
Economist