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MONDAY ECONOMIC REPORT

Manufacturing Contributed $2.35 Trillion in Value-Added Output to GDP

By Chad Moutray – March 29, 2021

The Weekly Toplines

- The U.S. economy grew 4.3% at the annual rate in the fourth quarter. Overall, real GDP was boosted by business investment, but consumer spending, particularly for goods, was held back by rising COVID-19 cases and renewed restrictions in many areas.

- The U.S. economy is expected to rebound in 2021, especially as more Americans get vaccinated and market participants resume some semblance of normalcy in their actions. The current forecast is for 6.8% annual growth in 2021.

- Real value-added output in the manufacturing sector rose to an annualized $2.234 trillion in the fourth quarter (expressed in chained 2012 dollars), the best reading since the all-time high seen one year earlier. In nominal terms, manufacturing value-added output increased to $2.348 trillion in the fourth quarter, with value-added output in the durable goods sector reaching an all-time high ($1.333 trillion). Manufacturing accounted for 10.9% of real GDP in the quarter.

- The IHS Markit Flash U.S. Manufacturing PMI strengthened from 58.6 in February to 59.0 in March, buoyed by growth in new orders, which expanded at the best pace since June 2014. Yet, extreme weather conditions and supply chain disruptions dampened output growth to a five-month low, and raw material costs soared once again.

- There were similar manufacturing trends in the Kansas City and Richmond Federal Reserve Bank reports for March, with activity in the Kansas City Fed district expanding at the fastest pace in the survey’s history. Respondents remained upbeat about growth over the next six months.

- New orders for durable goods fell 1.1% in February. Despite the weaker data in the latest report, the durable goods sector continues to reflect strong rebounds since declining sharply last spring due to the COVID-19 pandemic. Indeed, new durable goods orders have risen 3.2% over the past 12 months, with core capital goods orders —a proxy for capital spending in the U.S. economy— soaring 8.3% year-over-year. This speaks to the brighter economic outlook.

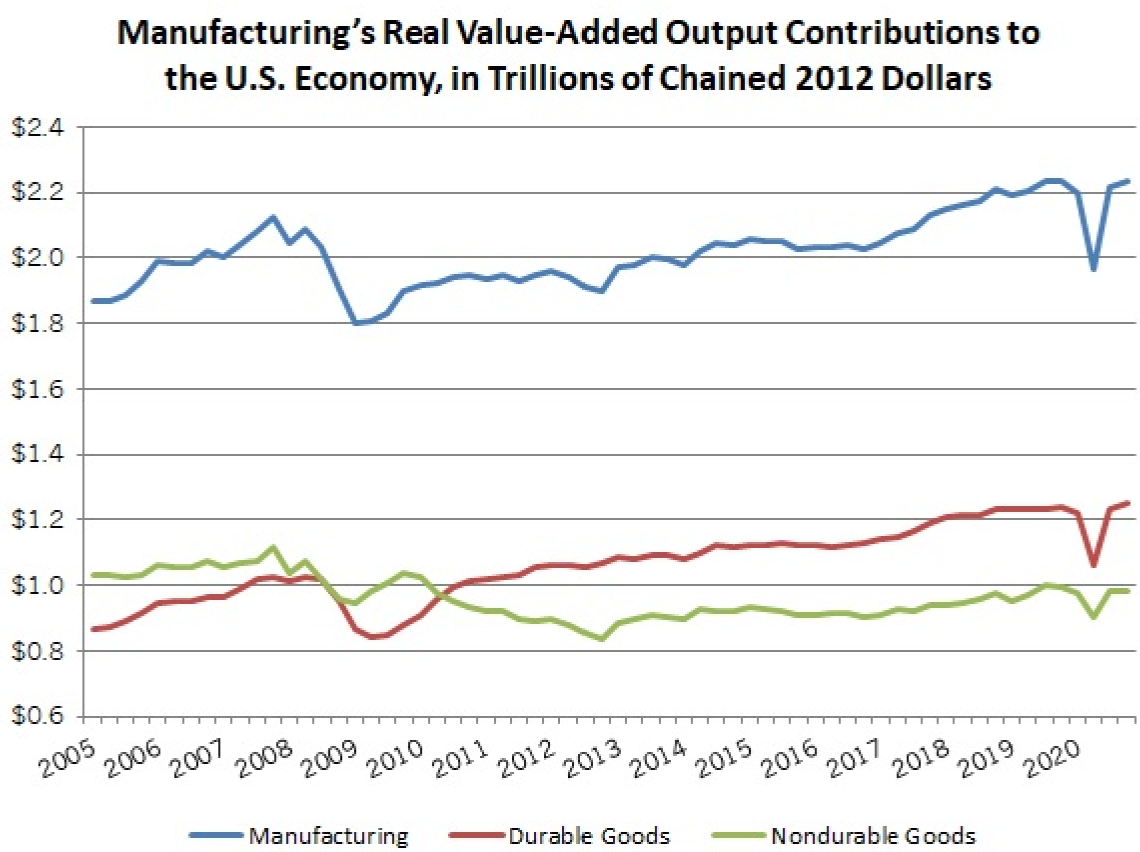
- After jumping by 10.1% in January, buoyed by stimulus checks and increased unemployment insurance from legislation enacted at year’s end, personal income fell 7.1% in February. It was the largest monthly decline in the history of the series, which dates to January 1959. These data will continue their rollercoaster ride, with a very large increase expected in March after passage of the American Rescue Plan.

Overall, personal income has risen 4.3% over the past 12 months.

- Meanwhile, personal consumption expenditures fell 1.0% in February. Yet, over the past 12 months, the trendline is more encouraging for goods purchases. Durable and nondurable goods spending has jumped 17.2% and 6.1% since February 2020, respectively, with service sector purchases down 5.2%. Over the past 12 months, personal consumption expenditures declined 0.6%, pulled lower by the reductions in service-sector spending.

- According to the University of Michigan and Thomson Reuters, [consumer sentiment] rose to a 12-month high in March, buoyed by increased vaccinations, stimulus checks and improved assessments about the economy overall.

- [Existing] and [new] home sales were both lower in February, with poor weather and limited inventories hindering activity. Nonetheless, the housing market remains a bright spot, with strong growth year-over-year and an encouraging outlook despite rising costs and affordability issues. The [average 30-year fixed rate mortgage rate] rose last week to the highest reading since June 2020, according to Freddie Mac, at 3.17%.



Economic Indicators

Last Week's Indicators:
(Summaries Appear Below)

Monday, March 29
Dallas Fed Manufacturing Survey

Monday, March 22
Chicago Fed National Activity Index
Existing Home Sales

Tuesday, March 23
New Home Sales
Richmond Fed Manufacturing Survey

Wednesday, March 24
Durable Goods Orders and Shipments
IHS Markit Flash U.S. Manufacturing PMI

Thursday, March 25
Gross Domestic Product (Second Revision)
Kansas City Fed Manufacturing Survey
Real GDP by Industry
Weekly Initial Unemployment Claims

Friday, March 26
International Trade in Goods (Preliminary)
Personal Consumption Expenditures Deflator
Personal Income and Spending
State Employment Report
University of Michigan Consumer Sentiment (Revision)

Tuesday, March 30
Conference Board Consumer Confidence

Wednesday, March 31
ADP National Employment Report

Thursday, April 1
Construction Spending
ISM® Manufacturing Purchasing Managers' Index®
Weekly Initial Unemployment Claims

Friday, April 2
BLS National Employment Report

Deeper Dive

- **Chicago Fed National Activity Index**: The Chicago Federal Reserve Bank's National Activity Index plummeted from 0.75 in January to -1.09 in February, the first negative reading in 10 months. The three-month moving average declined from 0.46 to -0.02, falling below zero for the first time since June 2020. Readings above zero are consistent with the U.S. economy expanding above its historical trend and vice versa.

  The lower readings were largely the function of sharp reductions in industrial production, which fell 2.2% in February, mostly from poor weather and lingering supply chain disruptions. Output in the manufacturing sector declined 3.1% in February. As a result, production-related indicators subtracted 0.85 from February's NAI. Personal consumption and housing indicators also weakened, subtracting 0.29 from the headline index, with retail sales falling 3.0% and housing starts contracting 10.2% in February.

- **Durable Goods Orders and Shipments**: New orders for durable goods fell 1.1% in February, pulling back somewhat after jumping 3.5% in January, likely from poor weather and lingering supply chain disruptions. Excluding transportation equipment, new durable goods orders decreased 0.9% in February. Yet, despite the weaker data in the latest report, the durable goods sector continues to reflect strong rebounds since declining sharply last spring due to the COVID-19 pandemic. Indeed, new durable goods orders have risen 3.2% over the past 12 months, or 1.5% with transportation equipment excluded. In addition, while nondefense capital goods excluding aircraft—a proxy for capital spending in the U.S. economy—declined 0.8% in February from January's record high, activity has soared 8.3% year-over-year, as firms have ramped up activity on the brighter economic outlook.

In February, the underlying data mostly decreased, including declines for motor vehicles and parts (down 8.7%), defense aircraft and parts (down 3.7%), other durable goods (down 2.0%), fabricated metal products (down 0.9%), machinery (down 0.6%), computers and electronic products (down 0.5%) and primary metals (down 0.5%). In contrast, orders increased for nondefense aircraft and parts (up 103.3%) and electrical equipment, appliances and components (up 0.2%).

Meanwhile, durable goods shipments decreased 3.5% in February, with a 1.2% decline with transportation equipment excluded. Over the past 12 months, durable goods shipments have jumped 8.2%. Excluding transportation, shipments have increased 6.1% year-over-year. In addition, core capital goods shipments eased by 1.0% from January's all-time high, but with 7.1% growth year-over-year.

- **Existing Home Sales**: The National Association of Realtors reported that existing home sales fell 6.6% from 6.66 million units in January to 6.22 million units in February, a six-month low. NAR Chief Economist Lawrence Yun attributed the decline to low inventory, but poor weather also likely played a factor. The February data weakened in every region except the West. Single-family and condominium and co-op sales decreased 6.6% and 6.7%, respectively, in February.

  Despite the disappointing data, the housing market continues to be a bright spot, and the outlook remains more encouraging. Existing home sales have risen 9.1% over the past 12 months, up from 5.70 million units in February 2020, with single-family and condo/co-op sales rising 8.0% and 18.6% year-over-year, respectively.

  Inventories of existing homes for sales inched up from 1.9 months of supply on the market in December and January, a record low, to 2.0 months in February. The median sales price for existing homes has jumped 15.8% year-over-year, up to $313,000 in February.

- **Gross Domestic Product (Second Revision)**: The U.S. economy grew 4.3% at the annual rate in the fourth quarter, slightly better than the prior estimate of 4.1% growth. Overall, real GDP was boosted by business investment and service-sector consumer spending, but goods purchases, government spending and net exports were drags on headline activity. Consumer spending was held back by rising COVID-19 cases and renewed restrictions in many areas in the fourth quarter. In 2020, real GDP shrank 3.5%, the largest annual decline in economic activity since 1946.

  The U.S. economy is expected to rebound in 2021, especially as more Americans get vaccinated and market participants resume some semblance of normalcy in their actions. The current forecast is for 6.8% annual growth in 2021. While real GDP will likely hit its pre-pandemic level by the second quarter of this year, it is important to note that economic growth remains well below trend.

- **IHS Markit Flash U.S. Manufacturing PMI**: Manufacturing activity in the U.S. strengthened somewhat, with the headline index rising from 58.6 in February to 59.0 in March. The data were buoyed by growth in new orders (up from 57.4 to 60.8), which expanded at the best pace since June 2014, reflecting overall strength in the sector. Yet, extreme weather conditions and supply chain disruptions dampened output growth (down from 57.8 to 54.5), slowing to a five-month low. Exports (down from 53.6 to 52.7), employment (down from 56.3 to 55.1) and future output (down from 75.5 to 75.1) also eased in March, with the latter continuing to point to upbeat assessments in the outlook for future production. Yet, raw material costs (up from 73.2 to 74.9) soared once again, growing at the fastest rate since the question was added in May 2007.

Encouragingly—and in contrast to the European data, which are described below—the IHS Markit Flash U.S. Services Business Activity Index improved from 59.8 to 60.0, the best reading since July 2014. This reflected rebounding activity, with COVID-19 restrictions lifted in many areas.

Meanwhile, the IHS Markit Flash Eurozone Manufacturing PMI jumped from 57.9 in February to 62.4 in March, a record high. Manufacturing activity rose sharply across the board, including all-time high paces for new orders, exports and output. Hiring grew at the best rate since August 2018. Respondents felt very upbeat in their assessments of future output despite pulling back from an all-time high. Input costs soared at rates not seen since March 2011. At the same time, the IHS Markit Flash Eurozone Services PMI declined at a slower rate but contracted for the seventh straight month, as renewed COVID-19 cases and restrictions continued to take a toll on the Eurozone economy.

In Germany, manufacturing activity also soared to a record pace, with "flash" PMIs in France and—outside of the Eurozone—the United Kingdom expanding at rates not seen in more than three years.

- **International Trade in Goods (Preliminary)**: In advance statistics, the goods trade deficit rose from $84.58 billion in January to $86.72 billion in February, a three-month high. Goods exports decreased from $135.28 billion to $130.14 billion, more than outpacing the decline in goods imports, which declined from $219.86 billion to $216.86 billion.

  In February, goods exports were lower across the board, led by steep declines in capital goods (down $2.46 billion), consumer goods (down $921 million), foods, feeds and beverages (down $754 million) and automotive vehicles (down $740 million). At the same time, sizable decreases in goods imports for automotive vehicles (down $3.39 billion) and consumer goods (down $2.90 billion) were enough to offset higher imports for industrial supplies (up $3.52 billion). Final data will be released April 7, which will also include the service-sector trade surplus.

- **Kansas City Fed Manufacturing Survey:** Manufacturing activity expanded at the fastest pace in the survey's history, which dates to July 2001, with the composite index of general business conditions rising from 24 in February to 26 in March. Growth in new orders, shipments and the average employee workweek strengthened in March, but production, employment and exports slowed. The sample comments noted supply chain and logistics constraints and rising raw material costs, but respondents also cited strength in the overall marketplace. On the topic of costs, the index for raw materials prices edged down from 68 in February, which was the highest since April 2011, to 66 in March, suggesting that input costs are still expanding at a very elevated pace.

  Respondents continued to feel upbeat about additional growth over the next six months, with the forward-looking composite index rising to the best reading since June 2018. Solid expansions were expected for new orders, production, hiring and capital spending, with modest growth for exports.

- **New Home Sales**: New single-family home sales plummeted 18.2% from 948,000 units at the annual rate in January to 775,000 units in February, a nine-month low. Sales fell sharply in every region of the country, with poor weather likely being a factor. To that extent, it would be expected that new home sales will rebound moving forward, with the housing market remaining a bright spot. Even with weaker data in February, new single-family home sales have risen 8.2% over the past 12 months, up from 716,000 units in February 2020.

  There were 4.8 months of supply on the market in February, up from 3.8 months in January, but with inventories of new homes for sale remaining very low overall. The median sales price registered $349,400 in February, up 5.3% year-over-year.

- **Personal Consumption Expenditures Deflator**: The PCE deflator rose 0.2% in February, slowing from the 0.4% and 0.3% gains in December and January, respectively. Overall, the PCE deflator has risen 1.6% year-over-year, a 12-month high, and core inflation, which excludes food and energy costs, has increased 1.4% since February 2020. Energy prices increased 3.8% in February, with food costs rising 0.2%. On a year-over-year basis, food and energy prices have increased 3.3% and 1.2%, respectively.

  Despite higher costs in recent months (and a major concern for manufacturers), the core PCE deflator has remained below 2% for 27 consecutive months. For its part, the Federal Reserve remains more worried about economic growth than inflation, as seen in the extraordinary measures taken over the past year to help prop up the economy, but it is also closely monitoring inflationary pressures and supply chain constraints.

- **Personal Income and Spending**: After soaring by 10.1% in January, buoyed by stimulus checks and increased unemployment insurance from legislation enacted at year's end, personal income fell 7.1% in February. It was the largest monthly decline in the history of the series, which dates to January 1959. These data will continue their rollercoaster ride, with a very large increase expected in March after passage of the American Rescue Plan. Overall, personal income has risen 4.3% over the past 12 months.

  Wages and salaries were flat both for the month of February and year-over-year. In the manufacturing sector, wages and salaries edged up from $899.3 billion in January to $899.4 billion in February, essentially unchanged, with the total down 3.0% over the past 12 months.

  Total unemployment insurance payments were $537.0 billion in February, down from $555.5 billion in January, which was a five-month high. At the same time, other government social benefits to persons soared to $2.36 trillion in January, the highest since April 2020, with many Americans receiving $600 checks each. That dropped to $781.1 billion in February.

  Meanwhile, personal consumption expenditures fell 1.0% in February, pulling back somewhat after the 3.4% gain in January and the largest monthly decline in 10 months. Durable and nondurable goods purchases fell 4.7% and 2.0% in February, respectively, with service-sector spending inching up 0.1%. Yet, over the past 12 months, the trendline is more encouraging for goods purchases. Durable and nondurable goods spending has jumped 17.2% and 6.1% since February 2020, respectively, with service sector purchases down 5.2%. Over the past 12 months, personal consumption expenditures declined 0.6%, pulled lower by the reductions in service-sector spending.

With income falling by more than spending, the saving rate declined from 19.8% in January to 13.6% in February—still a highly elevated pace.

- **Real GDP by Industry**: The U.S. economy grew 4.3% at the annual rate in the fourth quarter (see above). According to the Bureau of Economic Analysis, real value-added output in the manufacturing sector rose from $2.213 trillion at the annualized rate in the third quarter to $2.234 trillion in the fourth quarter, as expressed in chained 2012 dollars. This was the best reading in one year, with real value-added output in manufacturing totaling $2.236 trillion in the fourth quarter of 2019, an all-time high. The current reading is just shy of that amount, suggesting that activity in the sector has rebounded strongly after plummeting sharply last spring. In the latest data, real value-added output for durable goods increased from $1.230 trillion to $1.250 trillion, a record pace, with nondurable goods activity up from $982.4 billion to $982.8 billion, the best reading in four quarters.

  Overall, real value-added output in manufacturing grew 3.9% at the annual rate in the fourth quarter, adding 0.43 percentage points to headline real GDP growth. Manufacturing accounted for 10.9% of real GDP in the fourth quarter, edging down from 11.0% in the third quarter.

  Digging into the data, manufacturing value-added output increased from $2.329 trillion in the third quarter to $2.348 trillion in the fourth quarter, which was just 0.9% below the record pace seen in the fourth quarter of 2019 ($2.370 trillion). Value-added output for durable goods rose to a new record level, up from $1.324 trillion to $1.333 trillion, with nondurable goods value-added output rising from $1.005 trillion to $1.014 trillion. Similarly, manufacturing gross output increased from $6.013 trillion in the third quarter to $6.186 trillion in the fourth quarter, a one-year high. This was 0.4% lower than in the fourth quarter of 2019 ($6.210 trillion).

- **Richmond Fed Manufacturing Survey**: Manufacturing businesses in the Richmond Federal Reserve Bank's district continued to expand, with the composite index of general business activity rising from 14 in February to 17 in March, a three-month high. Shipments, capacity utilization and capital expenditures strengthened for the month, with new orders and employment expanding at a solid pace. Yet, the data also show lingering supply chain challenges, with vendor lead times jumping to the highest point since January 1996 and input costs soaring at rates not seen in 29 months.

  Meanwhile, the forward-looking indicators remained encouraging, with manufacturers in the district expecting continued growth in activity over the next six months. The expected composite index rose from 22 to 28, with strong growth across the board in the underlying measures.

  As noted above, raw material costs increased from 4.47% at the annual rate in February to 6.15% in March, the fastest pace since October 2018. Likewise, respondents anticipate an annualized 4.66% increase in costs six months from now, up from 3.78% in the prior survey and the most since February 2020.

- **State Employment Report**: California created the most net new manufacturing jobs in February, adding 8,900 workers. Other states with notable employment growth for the month included Indiana (up 2,500), Iowa (up 2,200), Georgia (up 2,000) and Michigan (up 1,800). Nationally, manufacturing employment remained down 561,000 year-over-year in February. Only two states have had net employment gains over the past 12 months: Utah (up 2,400) and Idaho (up 100). The largest year-over-year declines remained in big states: California (down 76,800), Texas (down 53,900), Michigan (down 43,700), Ohio (down 36,600), Illinois (down 34,100), New York (down 33,500), Pennsylvania (down 33,200) and Washington (down 32,700).

The national unemployment rate was 6.2% in February, and the unemployment rate fell in 23 states and the District of Columbia in the latest data. Hawaii had the highest unemployment rate in the country at 9.2%, followed closely by New York (8.9%), Connecticut (8.5%), California (8.5%), New Mexico (8.3%) and Nevada (8.3%). At the other end of the spectrum, the lowest unemployment rates in the United States in February occurred in South Dakota (2.9%), Utah (3.0%), Nebraska (3.1%), Vermont (3.1%) and Kansas (3.2%).

- **University of Michigan Consumer Sentiment (Revision)**: Consumer confidence rose from 76.8 in February, a six-month low, to 84.9 in March, a 12-month high, according to final data from the University of Michigan and Thomson Reuters. This was a nice improvement from the preliminary reading, which was 83.0 in March. With more Americans getting vaccinated and stimulus checks distributed as part of the American Rescue Plan, consumers felt more upbeat about both current and future economic conditions. The release further adds, "The data clearly point toward robust increases in consumer spending. The ultimate strength and duration of the spending surge will depend on the rate of draw-downs in savings since consumers anticipate a slower pace of income growth."

  Despite such gains, it is also clear that improvements have not been as broad-based as might be preferred, with many households continuing to worry about finances. For instance, in the February data, the University of Michigan noted that households with incomes below $75,000 tended to be more concerned about economic prospects.

- **Weekly Initial Unemployment Claims**: Initial unemployment claims totaled 684,000 for the week ending March 20, down from 781,000 for the week ending March 13 and the lowest since the week ending March 14, 2020. Meanwhile, continuing claims declined from 4,134,000 for the week ending March 6 to 3,870,000 for the week ending March 13. Although this figure represents the lowest level since the week ending March 21, 2020, it is still too high and consistent with 2.7% of the workforce.

  At the same time, 18,952,795 Americans received some form of unemployment insurance benefit (including state and federal programs) for the week ending March 6. That figure ticked up from 18,218,933 for the week ending Feb. 27 and reflects sizable increases in pandemic assistance claims.

Take Action

- The Manufacturing Institute will host a webinar, "Connecting Manufacturers with the Future: How 5G Will Transform Your Business," on Tuesday, April 6, at 2:00 p.m. EDT in conjunction with the release of a new study on the topic. Avrio Institute President Shawn DuBravac will walk through the results of the MI study. Other panelists include Qualcomm Senior Vice President and General Manager of 5G Durga Malladi and Deere & Company Manager of Enterprise Manufacturing Technologies Casey Kann.

Click here for more information and to register.

- The MI and Deloitte will host a webinar, “Beyond Reskilling in Manufacturing: Creating Pathways for Tomorrow’s Workforce Today,” on Friday, April 16, at 12:00 p.m. EDT in conjunction with an updated release of the skills gap study. Deloitte Human Capital Practice Managing Director Victor Reyes will join MI Executive Director Carolyn Lee for a discussion of the highlights of the report and current and future labor force conditions for manufacturers. Chad Moutray, the MI’s director for the Center for Manufacturing Research, will also provide a quick economic overview. Click here for more information and to register.

Questions or comments? Email NAM Chief Economist Chad Moutray at cmoutray@nam.org.