MONDAY ECONOMIC REPORT

Manufacturing Output: Strongest Since January 2019 Despite Slowing in August

By Chad Moutray – September 20, 2021

The Weekly Toplines

- Manufacturing production slowed significantly in August, edging up 0.1% for the month after rising by 1.6% in July. Much like the larger economy, manufacturing production has softened likely due to supply chain disruptions, workforce shortages and rising raw material costs. Still, manufacturing production has increased 5.9% over the past 12 months, or 3.2% year to date, with output in the sector the strongest since January 2019.

- Similarly, manufacturing capacity utilization edged up from 76.6% in July to 76.7% in August, also the best reading since January 2019. Looking at annual average growth rates, I would expect that manufacturing production will have risen by 6.8% in 2021, with 4.2% growth in 2022.

- Regional surveys from the New York and Philadelphia Federal Reserve Banks reflected stronger manufacturing expansions in September, with a positive outlook for the next six months. The forecast for capital spending in the Empire State release was the best since January 2018, with technology spending seen rising at a record pace. Yet, delivery times and pricing pressures remained significant challenges in both districts.

- Retail sales rose 0.7% in August, rebounding from the 1.8% decline seen in July and continuing the seesaw pattern seen over the past five months. Motor vehicle and parts dealers reported 3.6% fewer sales in August, with the chip shortage and supply chain issues hindering spending in that category. Excluding motor automobiles, retail spending increased 1.8% for the month.

- Spending at retailers was boosted by very robust growth at non-store retailers (up 5.3%), among others. Spending at food services and drinking places was flat in August, slowing from the 1.3% gain seen in July and likely dampened by rising delta variant cases of COVID-19 in some markets around the country.

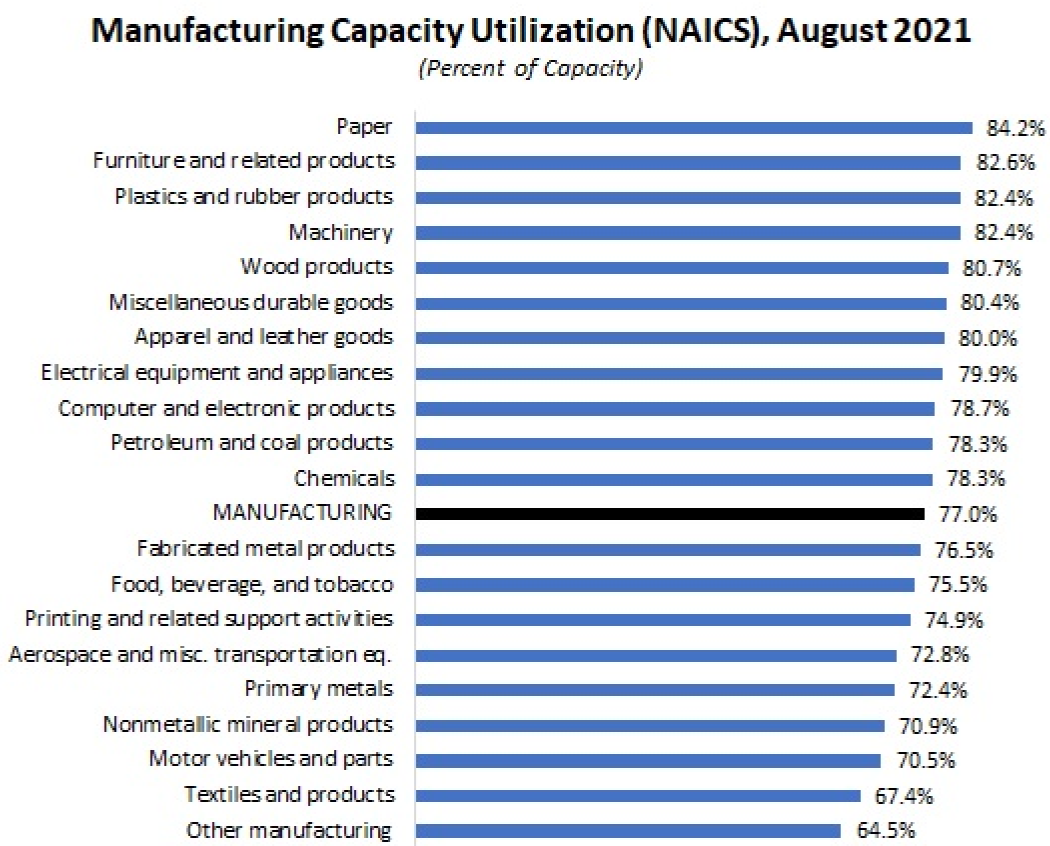
- Consumer prices rose 0.3% in August, the slowest monthly increase since January. Excluding food and energy, core consumer prices edged up 0.1% in August, the weakest pace since February. Prices for used cars and trucks and transportation services, both of which soared sharply earlier in the year, declined in August. New vehicle prices were higher.

- The consumer price index has risen 5.2% year-over-year, pulled back from 5.3% in June and July, which was the fastest year-over-year pace since September 2008.

Likewise, core inflation increased 4.0% year-over-year in August, decelerating for the second straight month from 4.5% in June, the highest since November 1991.

- Small business owners continue to experience record-level challenges with prices and employment, according to the National Federation of Independent Business. Half of all respondents in the August survey said that they had job openings that they were unable to fill, with 60% saying that there were few or no qualified applicants, also an all-time high.

- Kentucky created the most net new manufacturing jobs in August, adding 5,700 workers. Post-pandemic onset, Utah has generated the most employment in the sector, adding 8,100 workers over the past 18 months. Nebraska had the lowest unemployment rate (2.2%).



Economic Indicators

Last Week's Indicators:
(Summaries Appear Below)

Monday, September 13
None

Tuesday, September 14
Consumer Price Index
NFIB Small Business Survey

This Week's Indicators:

Monday, September 20
NAHB Housing Market Index

Tuesday, September 21
Housing Starts and Permits

Wednesday, September 22

Wednesday, September 15
Industrial Production
New York Fed Manufacturing Survey

Thursday, September 16
Philadelphia Fed Manufacturing Survey
Retail Sales
Weekly Initial Unemployment Claims

Friday, September 17
State Employment Report
University of Michigan Consumer Sentiment (Preliminary)

Existing Home Sales
FOMC Monetary Policy Statement

Thursday, September 23
Chicago Fed National Activity Index
Conference Board Leading Indicators
IHS Markit Flash U.S. Manufacturing PMI
Kansas City Fed Manufacturing Survey
Weekly Initial Unemployment Claims

Friday, September 24
New Home Sales

Deeper Dive

- **Consumer Price Index:** Consumer prices rose 0.3% in August, easing from the 9% and 5% gains seen in June and July, respectively, and the slowest monthly increase since January. Food and energy costs rose 0.4% and 2.0%, respectively, for the month, with gasoline prices up 2.8%. Excluding food and energy, core consumer prices edged up 0.1% in August, the weakest pace since February and down sharply from the 0.9% growth rate seen in June (which, along with April's reading, was the strongest pace since April 1982).

  After very sharp increases earlier in the year, including a 10.5% gain in June, used car and truck prices fell 1.5% in August. Even with some easing in the latest data, used car and truck prices remain 29.4% higher today than in February. Likewise, the cost of transportation services, which was also strong in the spring and early summer, declined for the second straight month, down 2.3% in August but remaining up 4.2% since February. Meanwhile, the price of new vehicles rose 1.2% in August, with 7.2% growth over the past six months.

The consumer price index has risen 5.2% over the past 12 months, pulling back slightly from the 5.3% year-over-year pace seen in both June and July, which was the fastest since September 2008. At the same time, core inflation (which excludes food and energy) increased by 4.0% year-over-year in August, decelerating from the 4.5% and 4.2% year-over-year gains seen in June and July, respectively. Core inflation in June was the highest since November 1991, with some moderation in the two months since.

Overall, price pressures have eased for consumers in the latest data, which is encouraging. The longer-term trend continues to reflect elevated price growth year to date, especially for cars and trucks and transportation services. Yet, consumer price growth has stabilized somewhat in the past month or two. That should give some credence to the notion that at least some of the recent cost increases were transitory, even if inflationary pressures are likely to remain more elevated than we have become accustomed to in recent years.

- **Industrial Production:** Manufacturing production slowed significantly in August, edging up 0.1% for the month after rising by 1.6% in July. Durable and nondurable goods production also inched up by 0.1% each in August. The underlying data provided mixed results, including for motor vehicles and parts. This broad category has struggled with supply chain and chip shortage issues for most of this year, with output down 5.6% since January. Motor vehicle production pulled back 0.3% in August after rebounding in July, but motor vehicle parts output rose by 0.4%.

  Much like the larger economy, manufacturing production has softened likely due to supply chain disruptions, workforce shortages and rising raw material costs. Even with weaker-than-desired growth, manufacturing capacity utilization edged up from 76.6% in July to 76.7% in August, the best reading since January 2019.

  Manufacturing production has increased 5.9% over the past 12 months, or 3.2% year to date, with output in the sector the strongest since January 2019 (similar to the capacity utilization data). Looking at annual average growth rates, I would expect that manufacturing production will have risen by 6.8% in 2021, with 4.2% growth in 2022.

  In August, the largest manufacturing production increases for the month occurred in other manufacturing (up 2.4%), furniture and related products (up 2.1%), computer and electronic products (up 1.2%), paper (up 1.1%) and fabricated metal products (up 0.7%). At the same time, production declined for the month for electrical equipment and appliances (down 1.2%), machinery (down 0.8%), printing and related products (down 0.8%), textiles and products (down 0.8%) and chemicals (down 0.5%).

  Nine of the major manufacturing sectors have experienced increased production since February 2020, or since the COVID-19 pandemic began. This included sizable gains in output over the past 18 months in aerospace and miscellaneous transportation equipment (up 12.7%), computer and electronic products (up 11.3%), chemicals (up 5.3%), miscellaneous durable goods (up 5.0%) apparel and leather goods (up 4.9%) and machinery (up 4.7%). At the other end of the spectrum, still-sizable declines in output since February 2000 occurred in other manufacturing (down 15.1%), printing and related support activities (down 6.6%), nonmetallic mineral products (down 5.7%), motor vehicles and parts (down 5.6%) and furniture and related products (down 5.5%).

Meanwhile, total industrial production rose 0.4% in August to the best reading since December 2019, but growth eased after rising by 0.8% in July. Utilities production jumped 3.3% in August on warmer temperatures, but mining output fell by 0.6%. On a year-over-year basis, industrial production has soared 5.9%. Total capacity utilization rose from 76.2% in July to 76.4% in August, also the highest since December 2019.

- **New York Fed Manufacturing Survey:** Manufacturing activity strengthened in September after slowing somewhat in August, according to the Empire State Manufacturing Survey, with the composite index rising from 18.3 in August to 34.3 in September. The underlying data improved across the board, including for new orders, shipments, inventories, employment and the average workweek. Supply chain issues remained, however, with the index for delivery times soaring to a new high. Input costs pulled back for the fourth straight month from May's record growth rates but remained not far from that pace, with 76.5% of respondents continuing to cite rising raw material costs for the month. At the same time, the index for selling prices jumped to another record in September.

  Manufacturers in the region remained very upbeat about growth over the next six months, with the forward-looking composite index rising from 46.5 in August to 48.4 in September, the strongest reading since January 2018. More than 60% of respondents predict increased new orders and shipments moving forward, with 46.1% and 40.9% forecasting more hiring and capital spending, respectively. The forecast for capital expenditures was the best since January 2018, with technology spending seen rising at a record pace. Respondents expected input and product prices to remain highly elevated and not far from recent records.

- **NFIB Small Business Survey:** The National Federation of Independent Business reported that the Small Business Optimism Index edged up from 99.7 in July to 100.1 in August. Overall, small business owners remain anxious, and inflation is a challenge. But strong hiring and capital spending expectations point to overall optimism in the outlook. The percentage of respondents saying that the next three months would be a "good time to expand" eased from 13% to 11%, and the net percentage reporting greater sales over the next three months was negative for the second straight report despite inching up from -4% to -2%.

  As with other surveys, pricing pressures remain very elevated. In August, the net percentage of respondents reporting higher prices today than three months ago rose from 46% to 49%, a new record. In addition, the net percentage planning a price increase over the next three months remained at an all-time high of 44% for the third straight survey.

  The labor market remained challenging. The percentage of respondents suggesting they had job openings they were unable to fill inched up from 49% to 50%, a new record, and the percentage of respondents saying there were few or no qualified applicants for job openings rose from 57% to a record 60%. At the same time, the percentage of respondents planning to increase hiring over the next three months rose from 27% to 32%, a new all-time high. Respondents once again cited difficulties in obtaining qualified labor as the top "single most important problem."

  Regarding capital spending, 55% of small firms have made an investment over the past six months, the same pace as in the previous survey. In addition, the percentage of respondents planning to make a capital investment over the next three to six months rose from 26% to 30%, the best reading since November 2019.

- **Philadelphia Fed Manufacturing Survey:** Manufacturers in the Philadelphia Federal Reserve Bank's district reported accelerating growth in September, with activity bouncing back to a three-month high. The composite index rose from 19.4 in August to 30.7 in September, led by stronger growth in shipments and the average workweek. New orders and employment softened somewhat in September but remained solid overall, and inventory growth was strongly positive after contracting in both July and August. The index for prices paid has continued to decelerate a little since peaking in June (at the highest reading since October 1980) but remained highly elevated. Likewise, the index for prices received edged down from August's reading, which had been the fastest since May 1974 but was not far from that level.

  While the forward-looking composite index fell from 33.7 in August to 20.0 in September, the lowest since February 2016, manufacturers in the district remained positive in their outlook for the coming months. Nearly 49% of respondents predict increased orders over the next six months, with 56.0% expecting more shipments. In addition, 44.4% and 33.3% anticipate higher employment and capital spending in their outlook, respectively. Pricing pressures are not expected to let up, even with the expected prices received index easing slightly from the highest reading since September 1981.

  In special questions, 70.0% of manufacturers in the Philly Fed region report higher production in the third quarter relative to the second quarter, with 17.5% noting declines. The median capacity utilization rate shifted up to 70–80% in Q3 2021 relative to 60–70% in Q3 2020, with supply chain issues (87.2%) and labor issues (74.4%) serving as the largest impediments to having greater capacity.

- **Retail Sales:** Retail sales rose 0.7% in August, rebounding from the 1.8% decline seen in July and continuing the seesaw pattern seen over the past five months. Motor vehicle and parts dealers reported 3.6% fewer sales in August, with the chip shortage and supply chain issues hindering spending in that category. Excluding motor automobiles, retail spending increased 1.8% for the month—an encouraging sign that consumers continue to make purchases at a solid pace despite weaknesses in motor vehicles and parts.

  In August, retail sales were mostly higher, led by strong growth for non-store retailers (up 5.3%), furniture and home furnishings stores (up 3.7%), general merchandise stores (up 3.5%), food and beverage stores (up 1.8%) and miscellaneous store retailers (up 1.4%), among others. Spending at food services and drinking places was flat in August, slowing from the 1.3% gain seen in July and likely dampened by rising delta variant cases of COVID-19 in some markets around the country. In addition to motor vehicles and parts, retail spending was also lower for electronics and appliance stores (down 3.1%) and sporting goods and hobby stores (down 2.7%).

  Overall, retail spending has soared 15.1% over the past 12 months, with retail sales excluding automobiles and gasoline rising 13.6% year-over-year. There is optimism that consumers will continue to increase spending moving forward as the economy continues to rebound, especially given elevated savings rates, but this could hinge on supply chains stabilizing. There are also sizable risks in the outlook related to the spread of the delta variant, which could continue to dampen activity in the coming months.

- **State Employment Report:** Kentucky created the most net new manufacturing jobs in August, adding 5,700 workers. Other states with notable employment growth for the month included Missouri (up 4,500), Illinois (up 3,900), Kansas (up 3,300), Tennessee (up 3,200) and Pennsylvania (up 3,100). Just eight states have notched increased manufacturing employment since February 2020, or in the 18 months since the pandemic began. Those states were Utah (up 8,100), Nebraska (up 1,500), Nevada (up 700), Kentucky (up 200) and Montana, Rhode Island, South Dakota and Vermont (each up 100). In contrast, the largest declines over that time occurred in big states, such as California (down 69,200), Michigan (down 46,600), Ohio (down 31,400), Washington (down 30,300), Texas (down 29,600) and Illinois (down 28,900).

  The national unemployment rate was 5.2% in August, and the rate fell in 15 states and the District of Columbia in the latest data. Nevada had the highest unemployment rate in the country at 7.7%, followed by California (7.5%), New York (7.4%), and Connecticut, New Jersey and New Mexico (each with 7.2%). At the other end of the spectrum, the lowest unemployment rates in the United States in July occurred in Nebraska (2.2%), Utah (2.6%), Idaho (2.9%) and South Dakota (2.9%).

- **University of Michigan Consumer Sentiment (Preliminary):** After plummeting to the lowest level since December 2011 in August, consumer confidence edged higher in September but remained weaker than desired, according to the University of Michigan and Thomson Reuters. The Index of Consumer Sentiment rose from 70.3 in August to 71.0 in September. The headline index has averaged 80.0 year to date in 2021, down from 96.0 and 81.5 in 2019 and 2020, respectively. In the latest figures, Americans were slightly more upbeat in the outlook for the future but were less confident about current conditions. Inflation remains a worry for many of the respondents and, in the short term, that has also corresponded to reduced buying intentions for homes, vehicles, and household durables in the survey.

- **Weekly Initial Unemployment Claims:** Initial unemployment claims totaled 332,000 for the week ending Sept. 11, up from the post-pandemic low of 312,000 for the week ending Sept. 4. Meanwhile, continuing claims declined from 2,852,000 for the week ending Aug. 28 to 2,665,000 for the week ending Sept. 4, the lowest figure since the COVID-19 pandemic began. Continuing claims were consistent with 1.9% of the workforce, down from 2.1% in the previous report.

  At the same time, 12,106,727 Americans received some form of unemployment insurance benefit (including state and federal programs) for the week ending Aug. 28. That figure was up from 11,927,790 for the week ending Aug. 21. The increase stemmed from additional pandemic unemployment assistance, which was enough to offset reduced state and extended benefits assistance.

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