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MONDAY ECONOMIC REPORT

Essential Takes on Leading Economic Indicators

By Chad Moutray, Ph.D., CBE – December 23, 2019 – SHARE

Manufacturing Outlook Steadied in the Fourth Quarter, but Remained Soft

The Weekly Toplines

- In the latest NAM Manufacturersâ€™ Outlook Survey, 67.6% of manufacturing respondents reported a positive outlook for their company. Manufacturing confidence has remained largely steady since the third quarter, yet optimism continues to be well below the 89.5% positive reading in March. Large businesses felt notably less upbeat in their outlook relative to other firm sizes.

- Passage of the United Statesâ€“Mexicoâ€“Canada Agreement, securing a trade deal with China and reauthorizing the Export-Import Bank could each make an immediate difference for manufacturers in the United States to allow them to continue growing their operations and creating well-paying jobs.

- The inability to find talent remained the top concern in the NAM Outlook Survey for the ninth straight quarter. Along those lines, job openings continued to be highly elevated in the manufacturing sector, with 477,000 in October and with an average of 483,500 per month year to date.

- After declining 0.7% in both September and October, manufacturing production rebounded, rising 1.1% in November and buoyed by stronger auto output. The sector continues to see signs of stabilization, but it is clearly not out of the woods yet. Production has fallen 0.8% over the past 12 months, declining on a year-over-year basis for the fifth consecutive month.

- Manufacturers in the New York and Philadelphia Federal Reserve Bank districts reported slight expansions once again in December, but activity contracted for the sixth consecutive month in the Kansas City Fedâ€™s region, pulled lower by global challenges, especially in the energy sector, and ongoing struggles in finding talent. The outlook for each region is cautiously positive.

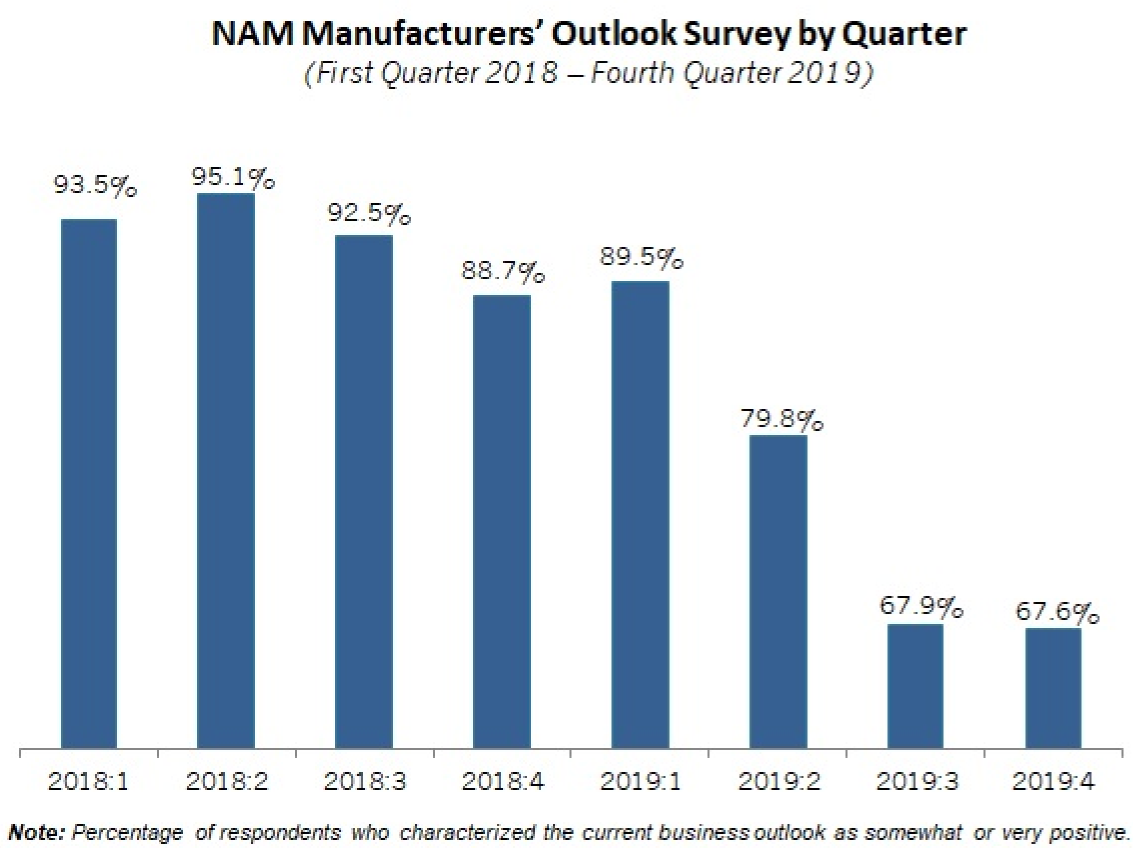
- According to IHS Markit, manufacturing in the United States continued to expand somewhat modestly in December, with respondents remaining optimistic about production in the first half of 2020. In contrast, Eurozone activity has now contracted for 11 straight months, led by lingering weaknesses in Germany.Â

- The U.S. economy grew 2.1% at the annual rate in the third quarter, unchanged from the previous estimate. For the year, the U.S. economy should increase by 2.3% in 2019, with 1.8% growth forecasted for 2020. Fourth quarter 2019 growth is currently hovering around 2.2%.

- Housing starts rose 3.2% in November, jumping 13.6% year-over-year, led by strength in single-family activity. Permits rose to the fastest pace since May 2007, with homebuilder optimism increasing to the best reading since June 1999.

- Personal income and spending rose 0.5% and 0.4% in November, respectively, with 4.9% and 3.9% growth for those two measures over the past 12 months. While consumers have tended to save more this year than last, spending remains a bright spot. Consumer sentiment rose to the best reading since May, according to the University of Michigan and Thomson Reuters.

P.S.: Due to the holidays, the Monday Economic Report will not be published on Monday, Dec. 30. The next issue will be released on Monday, Jan. 6.



Economic Indicators

Last Week's Indicators:
(Summaries Appear Below)

Monday, December 16
IHS Markit Flash U.S. Manufacturing PMI
NAHB Housing Market Index
New York Fed Manufacturing Survey

Tuesday, December 17
Housing Starts and Permits
Industrial Production
Job Openings and Labor Turnover Survey

Wednesday, December 18
NAM Manufacturersâ€™ Outlook Survey

Thursday, December 19
Conference Board Leading Indicators
Existing Home Sales
Philadelphia Fed Manufacturing Survey

Friday, December 20
Gross Domestic Product (Second Revision)
Kansas City Fed Manufacturing Survey
Personal Consumption Expenditures Deflator
Personal Income and Spending
State Employment Report
University of Michigan Consumer Sentiment (Revision)

This Week's Indicators:

Monday, December 23
Chicago Fed National Activity Index
New Home Sales

Tuesday, December 24
Durable Goods Orders and Shipments
Richmond Fed Manufacturing Survey

Wednesday, December 25
CHRISTMAS DAY HOLIDAY

Thursday, December 26
None

Friday, December 27
None

Deeper Dive

- **Conference Board Leading Indicators:** The Leading Economic Index was flat in November, an improvement after declining 0.2% in each of the three prior months. Moreover, the headline index has been relatively stagnant over the past six months, which would seem to indicate that economic growth should remain soft in early 2020. New orders for manufactured goods continued to be a drag on the LEI, with the average workweek of production workers also negatively impacting activity in November. In contrast, building permits, consumer confidence, the interest rate spread, lending conditions and stock prices were bright spots.

  Meanwhile, the Coincident Economic Index rose 0.4% in November, rebounding strongly at the best pace in three months. The CEI was buoyed by a solid bounce-back in industrial production, as described below. The other components (manufacturing and trade sales, nonfarm payrolls and personal income) also contributed positively to current economic growth conditions for the month.

- **Existing Home Sales:** The National Association of Realtors reported that existing home sales declined 1.7% from an annualized 5.44 million units in October to 5.35 million units in November. Sales improved in the Midwest and Northeast but weakened somewhat in the South and West, with single-family and condominium and co-op activity down 1.2% and 5.1% in November, respectively. NAR Chief Economist Lawrence Yun noted low inventories of existing homes for sale, but also overall strength in the economy.

  With that said, existing home sales have risen a modest 2.7% over the past 12 months, up from 5.21 million units in November 2018. Single-family sales have increased 3.5% year-over-year, but condominium and co-op sales have fallen 3.4% over that time frame. The median sales price for existing homes has increased 5.4% year-over-year, up to $274,000 in November.

- **Gross Domestic Product (Second Revision):** The U.S. economy grew 2.1% at the annual rate in the third quarter, unchanged from the previous estimate. The updated figures were largely similar, but with upward revisions to service-sector spending essentially offsetting weaker inventory spending relative to the estimates in the prior release.

  Consumer spending, government expenditures and the housing market were bright spots, contributing 2.58% to real GDP growth for the quarter, but that was weighed down by net exports, nonresidential fixed investment and inventories, which subtracted 0.48%. For the year, the U.S. economy should increase by 2.3% in 2019, with 1.8% growth forecasted for 2020. Fourth quarter 2019 growth is currently hovering around 2.2%.

- **Housing Starts and Permits:** New residential construction rose 3.2%, up from an annualized 1,323,000 units in October to 1,365,000 units in November. Activity increased in November for both single-family (up from 916,000 units to 938,000 units) and multifamily (up from 407,000 units to 427,000 units) construction, with single-family starts having the best reading since January. Over the past 12 months, new residential construction has increased 13.6%, with single-family housing starts jumping 16.7% since November 2018.

  This suggests that homebuyers continue to respond positively to lower mortgage rates, with the overall housing market bouncing back after being in the doldrums over much of the past year. Homebuilder optimism also reflects that positivity, rising to a 20-year high (see below).

  Indeed, housing permits rose 1.4% in the latest report, up from 1,461,000 units at the annual rate in October to 1,482,000 units in November, the fastest pace since May 2007. The headline number was buoyed by growth in single-family permitting, up from 911,000 units to 918,000 units, a rate not seen since July

2007. Permits for multifamily units also increased, up from 550,000 units to 564,000 units, the best reading since June 2015. Overall, new residential construction permits have soared 11.1% year-over-year, which should signal healthy growth for the housing sector moving forward.

- **IHS Markit Flash U.S. Manufacturing PMI:** Manufacturing activity in the United States continued to expand somewhat modestly in December, albeit with a very slight easing. The main index edged down from 52.6 in November to 52.5 in December. The previous survey's results were the best since April, and the latest release mostly sustains those improvements. (In contrast, the competing ISMÂ® Manufacturing Purchasing Managers' IndexÂ® contracted for the fourth straight month.) IHS Markit reports progress for new orders and future output, but with some deceleration in the growth rates for output, exports and employment. Respondents remain optimistic about production in the first half of 2020.

  Meanwhile, the IHS Markit Flash Eurozone Manufacturing PMI remained challenged, dropping from 46.9 in November to 45.9 in December. The headline index has contracted for 11 straight months, with the current reading just shy of the 45.7 recorded in September, which was the lowest since October 2012. With that said, respondents felt cautiously positive for modest growth in output over the next six months, and exports had the best reading since May despite continuing to contract. The data continued to be pulled lower by weaknesses in Germany, which contracted in every month of 2019, albeit with some improvement from the 10-year low in September. At the same time, manufacturing slowed in France to just above neutral on decreasing demand and decelerating production, even as activity expanded for the fifth consecutive month.

- **Industrial Production:** After declining 0.7% in both September and October, manufacturing production rebounded, rising 1.1% in November. This was largely expected, with a fair share of the recent weakness stemming from an auto strike. Indeed, motor vehicles and parts production soared 12.4% in November after dropping in the three prior months. Excluding motor vehicles and parts, manufacturing production increased 0.2% in November.

  Overall, the data suggest that manufacturers are seeing some signs of stabilization, mirroring other indicators, but with the sector continuing to be weaker than desired. Along those lines, manufacturing production has fallen 0.8% over the past 12 months, declining on a year-over-year basis for the fifth consecutive month but improving from a decrease of 1.7% year-over-year in October. At the same time, manufacturing capacity utilization jumped from 74.5% in October to 75.2% in November, a three-month high.

  In November, durable and nondurable goods production rose 2.2% and 0.1%, respectively. Thirteen of the 19 major sectors experienced better output for the month, with most of those bouncing back from softness in the previous release. In addition to motor vehicles and parts, sizable increases in production in November occurred for computer and electronic products, plastics and rubber products and primary metals, among others. In contrast, the six sectors with declining output were apparel and leather products, chemicals, furniture and related products, machinery, nonmetallic mineral products and petroleum and coal products.

Meanwhile, total industrial production also bounced back, up 1.1% in November after dropping in the two previous months. In addition to stronger manufacturing output, production also rose for utilities (up 2.9%), but mining production decreased 0.2%, falling for the third straight month. Industrial production has fallen 0.8% over the past 12 months, declining on a year-over-year basis for the third straight month. Total capacity utilization increased from 76.6%, the lowest since September 2017, to 77.3%.

- **Job Openings and Labor Turnover Survey:** Job openings in the manufacturing sector increased, up from 462,000 in September to 477,000 in October. Overall, manufacturing job postings have remained elevated, averaging 483,500 per month year to date, including the all-time high reached in June (515,000). In the latest report, job openings increased for durable goods manufacturers, up from 292,000 to 342,000, a new record level. This was partially offset, however, by a decrease in job postings for nondurable goods firms, which declined from 170,000 to 134,000, nearly a three-year low.

  In the larger economy, nonfarm business job openings rose from 7,032,000 in September to 7,267,000 in October. From the manufacturing perspective, firms continue to cite the inability to find talent as a top concern. Indeed, for the 20th straight month, the U.S. economy reported more nonfarm job openings than the number of people looking for work (5,855,000 in October). That statistic suggests there were 1,412,000 more job postings than there were unemployed people to fill them.

  With that said, net hiring in the manufacturing sector has been softer than desired. Manufacturers hired 319,000 workers in October, down from 338,000 in September and the slowest pace since February 2017. At the same time, separations also decreased, down from 349,000 to 313,000, the lowest level since August 2017. As a result, net hiring (or hires minus separations) increased by 6,000 employees in October, an improvement from the decline of 11,000 in September.

- **Kansas City Fed Manufacturing Survey:** Manufacturing activity in the district contracted for the sixth consecutive month, with the composite index dropping from -3 in November to -8 in December, the fastest pace of decline since February 2016. New orders, production, shipments, employment, the average employee workweek and exports all deteriorated further in the latest survey. The sample comments reflect overall manufacturing business challenges, with frustrations about trade uncertainties and the continuing difficulties with finding talent. In addition, respondents cited weaknesses in the energy sector.

  Nonetheless, manufacturers remained cautiously positive about activity over the next six months. At least 42% of manufacturing firms in the region predict increased orders, production and shipments in the coming months, with 37% and 36% expecting higher employment and capital spending, respectively. Yet, firms also see the backlog of orders and the average employee workweek narrowing over the coming months.

- **NAHB Housing Market Index:** The National Association of Home Builders and Wells Fargo reported that confidence jumped to the best reading since June 1999. The Housing Market Index rose from 70 in November to 76 in December, with sentiment boosted by reduced inventories of existing homes, the strong labor market and lower mortgage rates. Indeed, the index for expected single-family sales six months from now increased from 78 to 79, the best reading since February 2018. With that said, the NAHB cites slowing economic growth and ongoing supply issues as challenges, including the shortage of skilled labor, a lack of buildable lots and rising costs that hurt affordability for would-be homebuyers.

- **NAM Manufacturers' Outlook Survey:** In the fourth quarter of 2019, 67.6% of manufacturing respondents reported a positive outlook for their company. Manufacturing confidence has remained largely steady since the third quarter, yet optimism continues to be well below the 89.5% positive reading in March. It was the second straight quarter with below-average activityâ€"a phenomenon that last occurred in the second and third quarters of 2016.

  Large manufacturers (i.e., those with 500 or more employees) felt less upbeat in their outlook than their small and medium-sized counterparts. This is likely because larger manufacturers are more likely to be engaged globally, and hence, those firms appear to be more sensitive to slowing growth and trade uncertainties. Just 55.8% of respondents from larger companies felt positive in their outlook, compared to 73.3% for small manufacturers (i.e., those with fewer than 50 employees) and 72.3% for medium-sized firms (i.e., those with 50 to 499 employees).

  Passage of the United Statesâ€"Mexicoâ€"Canada Agreement, securing a trade deal with China and reauthorizing the Export-Import Bank could each make an immediate difference for manufacturers in the United States to allow them to continue growing their operations and creating well-paying jobs.

  Along those lines, in a special question, 58.3% of large manufacturing respondents said that the downturn in the sector had impacted their economic outlook negatively, compared to 37.3% for small firms. Likewise, 47.1% of large companies said that the downturn had impacted hiring negatively versus one-quarter of small businesses. Business leaders from large companies expect full-time employment to decrease 0.6% over the next 12 months, with small and medium-sized respondents anticipating 1.3% growth.

  Another longstanding concern manufacturers continue to grapple with is finding enough workers. The inability to attract and retain a quality workforce remained respondents' top concern for the ninth consecutive survey, noted as the top concern by 63.8% of respondents.

Other top primary challenges in the fourth quarter included rising health care and insurance costs (52.3%) and a weaker domestic economy (51.9%).

- **New York Fed Manufacturing Survey:** Manufacturing activity in the New York Federal Reserve Bank's district expanded slightly for the sixth straight month in December. The headline index inched up from 2.9 in November to 3.5 in December, which has essentially been the average across the second half of 2019. The underlying data provided mixed results, with shipments improving somewhat but new orders and the average employee workweek slowing. Hiring continued to expand modestly at the same pace as in the prior survey. Inventories rebounded in December after falling in November.

  Meanwhile, respondents to the Empire State Manufacturing Survey remain positive in their outlook for the next six months. The forward-looking index for business conditions increased from 19.4 in November to 29.8 in December, the best reading since July, with stronger growth expected for new orders, shipments, the average employee workweek and capital expenditures, including technology spending. Respondents predicted hiring to expand at roughly the same modest pace despite easing marginally in this report.

- **Personal Consumption Expenditures Deflator:** The PCE deflator rose 0.2% in November for the second straight month. Energy costs increased 0.8% in November, slowing from 2.6% growth in October, but food prices were flat. The core PCE deflator, which excludes food and energy prices, inched up 0.1% in November for the fourth consecutive month. Over the past 12 months, the PCE deflator has risen 1.5%, up slightly from 1.4% growth in October. At the same time, core inflation registered 1.6% in November, off slightly from 1.7% year-over-year in October. For 11 consecutive months, or in every month so far in 2019, the core PCE deflator has remained below the Federal Reserve's stated goal of 2.0% core inflation.

  As such, the pricing data have provided some comfort to the Federal Open Market Committee, allowing participants the luxury of being more "dovish" in setting monetary policy. The Federal Reserve has reduced short-term rates three times in 2019, with the most recent move coming at its October meeting. Policymakers are more concerned with keeping the economic recovery moving at this point than with inflationary pressures. With that said, the FOMC is likely to wait for incoming data on economic growth before changing policy again.

- **Personal Income and Spending:** Personal consumption expenditures rose 0.4% in November, extending the 0.3% gain in October. Goods spending increased 0.5% for the month, with durable and nondurable goods spending up 1.0% and 0.2%, respectively. On a year-over-year basis, personal spending has risen 3.9%, with durable and nondurable goods sales up 3.5% and 2.7% since November 2018, respectively.

  Personal income jumped 0.5% in November, the best monthly reading since August. Over the past 12 months, personal income has risen by a solid 4.9%, up from 4.5% in the previous release and the fastest year-over-year rate since

December 2018. In addition, manufacturing wages and salaries were $927.9 billion in November, up from $921.2 billion in October and rising 4.2% over the past 12 months.

The saving rate edged up from 7.8% in October to 7.9% in November. In general, Americans have saved somewhat more this year than last, with the saving rate averaging 8.0% year to date in 2019, up from 7.6% through the first 11 months of 2018.

- **Philadelphia Fed Manufacturing Survey:** Manufacturing activity stagnated in December, expanding ever so slightly at the slowest pace in six months. The composite index of general business activity dropped from 10.4 in November to 0.3 in December. Despite the decline in the headline index, new orders, shipments and the average employee workweek improved for the month, with each growing modestly in December. Hiring eased somewhat but continued to expand at a solid pace.

  Meanwhile, manufacturers in the district remain very positive in their outlook for the next six months, albeit with some slight easing. The forward-looking composite index edged down from 35.8 in November to 35.2 in December. Roughly half of respondents expect new orders to rise in the coming months, with 40.6% and 34.1% predicting increases in employment and capital expenditures, respectively. At the same time, respondents predict input costs to accelerate once again, with the index for prices paid rising from 43.2 to 50.9, a one-year high.

  In special questions, manufacturers in the Philadelphia Fed's district anticipate wage growth of 2.6% in 2020, with health benefits rising 4.9%.

- **State Employment Report:** Michigan created the most net new manufacturing jobs in November, adding 19,600 workers, largely on a solid rebound in the aftermath of the auto strike in October. Other states with positive manufacturing employment growth for the month included Texas (up 6,300), Virginia (up 4,400), Tennessee (up 3,200), New York (up 3,000) and Missouri (up 2,700). At the same time, Vermont had the lowest unemployment rate in the nation in November at 2.3%. Â

  Texas saw the greatest job gains in the sector over the past 12 months, with manufacturing employment in the state up 21,700 since November 2018. California (up 11,400), Florida (up 7,400), Oregon (up 6,900), Arizona (up 6,800) and South Carolina (up 6,700) also experienced solid growth in manufacturing employment year-over-year.

- **University of Michigan Consumer Sentiment:** The Index of Consumer Sentiment improved to the best reading since May, according to the University of Michigan and Thomson Reuters. The headline measure jumped from 96.8 in November to 99.3 in December, slightly better than the 99.2 estimate seen two weeks prior. Americans felt more upbeat in their assessments of both current and future economic conditions. Surveys of Consumers Chief Economist

Richard Curtin noted that respondents with higher incomes accounted for the bulk of the increase in December, likely on recent gains in the stock market.

Overall, consumer confidence remains strong, even as perceptions have slipped a bit this year relative to last. The Index of Consumer Sentiment averaged 96.0 in 2019, off from 96.8 and 98.4 in 2017 and 2018, respectively.

Take Action

- The Manufacturing Leadership Council is partnering with The Manufacturing Instituteâ€"the workforce and education partner of the NAMâ€"to examine what skills are most in demand, both in current operations and for expected roles on the shop floor over the coming years. If you have not already done so, please take a moment to complete this short 10-question survey by **Wednesday, Jan. 8, 2020,** at 5:00 p.m. EST. All responses will be kept confidential, and the results will be posted online soon.

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