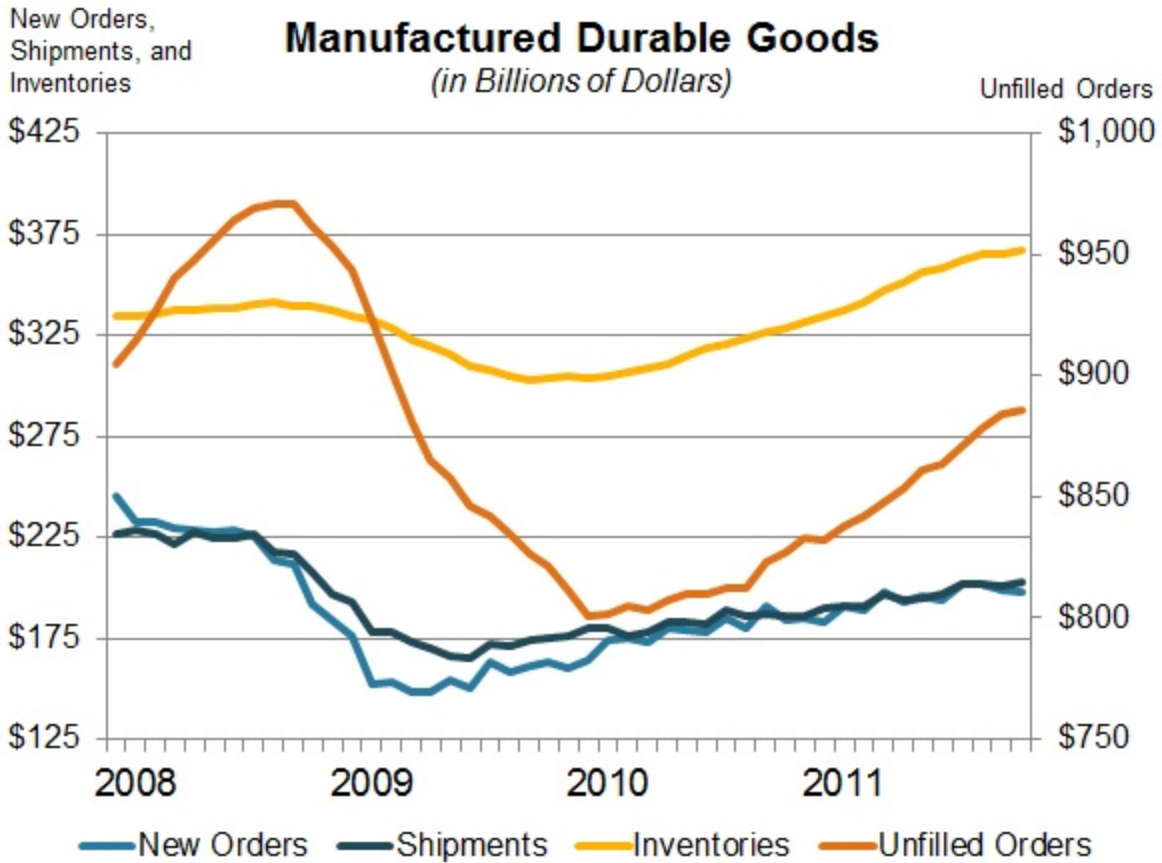




MONDAY ECONOMIC REPORT



November 28, 2011

There continues to be a split between domestic manufacturing activity and other economic variables. Much of the talk last week centered on the failure of the so-called Super Committee to tackle the nation's fiscal deficit challenges and Europe's continued financial problems. Rising borrowing costs are pushing many European nations — including some which were once considered "safe" — to grapple with credit and financial issues. Meanwhile, U.S. policymakers must once again attempt to deal with our soaring debt in the midst of a political stalemate and the threat of large cuts to federal spending on the horizon. Both of them will provide significant headwinds to

economic growth in the coming months.

The Bureau of Economic Analysis downgraded third-quarter growth from 2.5 percent, as estimated a few weeks ago, to 2.0 percent. The consumer continued to be the largest driver of this growth; however, spending was less than originally estimated. There were also downward revisions for business inventories and investment. Over the course of the last year, the U.S. economy has grown 1.5 percent, which is well below where it should be at this point in the recovery. Nonetheless, the outlook for 2012 is somewhat brighter, [with the National Association for Business Economics estimating 2.4 percent growth next year in its most recent survey](#).

The National Activity Index from the Chicago Fed noted upgrades in many economic indicators including manufacturing which have helped to reduce the risk of recession. This observation was based on better-than-expected recent industrial production numbers. In addition, manufacturing activity picked up around the country. The Richmond Federal Reserve Bank's latest survey showed that production has stopped contracting. Moreover, respondents are very optimistic about new orders, shipments, capital expenditures and employment moving into 2012. The Kansas City Fed's survey echoed the upbeat expectations regarding the next six months even as its current numbers indicate slower growth than last month.

Personal income rose at its fastest pace since March, helping to boost the savings rate to 3.5 percent. Spending also grew, albeit at a slower rate than in September, and the University of Michigan observed greater consumer confidence in current and future economic expectations. Rounding out the better news, existing homes sales picked up and most states reported lower unemployment in October. Weaknesses still persist in housing and employment, and it is safe to assume that consumers are cautiously optimistic moving forward.

This week, we will hope to see more improvements in manufacturing employment and production. The Institute for Supply Management will release its purchasing managers' index on Thursday, and the government will detail November employment conditions on Friday. New productivity data should also confirm the tremendous gains made by manufacturers recently. In addition, regional production information from Chicago and Dallas will foreshadow the Federal Reserve Board's Beige Book release on Wednesday.

Chad Moutray
Chief Economist
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P.S. I hope you will take a moment to fill out the latest NAM/IndustryWeek Survey of Manufacturers. This [15-question survey](#) should take just a few minutes to complete. It is important for us to get a sense of how NAM members gauge the current business climate. The results will be published in IndustryWeek in early December.

Economic Indicators

Last Week's Indicators: (Summaries Appear Below)

Monday, November 21

Chicago Fed National Activity Index
Existing Home Sales

Tuesday, November 22

GDP (Revision)
Regional and State Employment
Richmond Fed Manufacturing Survey

Wednesday, November 23

Durable Goods
Kansas City Fed Manufacturing Survey
Personal Income
University of Michigan Consumer Sentiment

Thursday, November 24

None

Friday, November 25

None

This Week's Indicators:

Monday, November 28

New Home Sales
Texas Manufacturing Outlook Survey

Tuesday, November 29

Conference Board Consumer Confidence

Wednesday, November 30

ADP Employment Report
Beige Book
ISM-Chicago
Productivity and Costs

Thursday, December 1

Construction Spending
ISM Manufacturing Index

Friday, December 2

BLS Employment Situation

Summaries of Last Week's Economic Indicators

Chicago Fed National Activity Index (October)

[The Chicago Federal Reserve Bank's National Activity Index rose from -0.20 in September to -0.13 in October.](#) This suggests that the national economy continues to operate below its historical trend, yet there were some improvements from the previous month. Specifically, better-than-expected industrial production numbers and increased employment helped to bring the index higher. Housing continued to provide a drag on the macroeconomy.

Three-month moving average values below -0.70 are associated with the increased likelihood of a recession. Currently, the 3-month moving average is -0.27. While lower than the month before, this figure remains comfortably away from the -0.70 threshold suggesting that the risk of recession has diminished since the summer. (The 3-month moving average in June was -0.54.) Nonetheless, significant weaknesses remain, preventing the economy from growing at its potential.

Durable Goods (October)

[The Census Bureau reported that new orders for durable manufactured goods fell 0.7 percent in October](#), but the decline was mostly attributable to nondefense aircraft. (All percentages are in annual terms.) Airplane orders are sporadic, creating a lot of volatility in these numbers. (Note that [Boeing just received an order for 230 planes](#) from Lion Air, which will show up in the November shipments data.) Outside of aircraft, the transportation sector had stronger gains, with new orders for motor vehicles rising 6.2 percent. When transportation is excluded from the durable goods numbers, new orders rose 0.7 percent.

Other sectors with strong new order gains for the month included primary metals (up 3 percent), machinery (up 1.6 percent) and all other durable goods (up 1.2 percent). In addition to transportation, other areas with the largest weaknesses for new orders were capital goods (down 6.2 percent), electrical equipment (down 5.2 percent) and communications equipment (down 1.6 percent).

New orders are a good proxy for future production, but this report also noted current activity. Shipments of durable goods increased 1.3 percent in October, reversing the September decline of 0.5 percent. In this case, the transportation sector led the pack with 5.2 percent higher shipments than the previous month, including 6.4 percent and 8.6 percent gains in motor vehicles and nondefense aircraft shipments, respectively.

Unfilled orders and inventories grew 0.2 percent and 0.5 percent, respectively, in October, continuing a long streak for both of them.

Overall, this report is more positive than the headline number suggests, yet the lower capital goods figures reflect weaknesses in the sector. Excluding aircraft, new orders and shipments for capital goods were down 1.8 percent and 1.1 percent, respectively. Moving forward, a stronger recovery will hinge on those numbers turning around.

Existing Home Sales (October)

[The National Association of Realtors \(NAR\) found that existing home sales increased 1.4 percent in October to an annualized 4.97 million units](#). This reversed the decline experienced in September. Each region saw gains, with the exception of a modest decline in the Northeast.

There are currently 8 months of supply on the market, which is down significantly from the 9.5 months observed in July. The current median home price for existing homes is \$162,500.

Despite these improvements, NAR Chief Economist Lawrence Yun said that a high percentage of potential buyers are unable to achieve credit to purchase a home, hampering improvements in the market. He said, "Contract failures reported by NAR members jumped to 33 percent in October from 18 percent in September ." This figure was 8 percent last year.

Gross Domestic Product (Third-Quarter Revision)

[The Bureau of Economic Analysis revised its third-quarter 2011 estimate for real GDP growth to 2 percent](#), down from its earlier estimate of [2.5 percent growth](#). The downward revisions were mainly due to lower inventories, business investment and consumer spending than originally thought.

The largest contributor to real GDP growth in the third quarter was consumption, adding 1.63 percentage points. The consumption of durable goods contributed 0.41 percentage points, rebounding from the negative contribution in the second quarter. Nondurable goods consumption subtracted 0.11 percentage points in the third quarter, with many sectors still showing weaknesses. There is more recent evidence, though, that these weaknesses are beginning to subside.

Net exports were another positive influence on economic growth in the third quarter, adding 0.49 percentage points to the final figure. Goods exports accounted for 0.48 percentage points of that number, with goods imports subtracting 0.04 percentage points. In essence, the growth of real exports significantly outpaced increases in real imports (up 4.3 percent versus 0.5 percent from the previous quarter).

The business investment picture was mixed, with large increases in fixed capital and residential investment being offset by reductions in nonfarm business inventories. As a whole, these provided a slight drag on real GDP. Similarly, government spending provided a negative contribution to growth, mainly from reduced expenditures in nondefense spending at the federal level and continued declines in state and local spending.

Overall, these numbers suggest that the U.S. economy has grown just 1.5 percent over the past year. The economy should grow by at least one percentage point more than that in 2012, yet it is clear that the economic recovery has been subpar. These rates of growth will not generate sufficient net new employment. We desperately need pro-growth policies from Washington that will allow manufacturers to grow and help boost the rest of the economy to create jobs.

Kansas City Fed Manufacturing Survey (November)

[The Kansas City Federal Reserve Bank observed a slower pace of growth in manufacturing activity in its region in November](#). The composite index fell from 8 in October to 5 in November, and it has been in single digits for six of the past seven months. This suggests modest growth among manufacturers in the district. Perhaps worrisome is the fact that the volume of new orders, the average employee workweek and new export orders declined from slight growth to a slight contraction. Other components mostly suggested little change from October, including no change in production or shipments and modestly higher employment.

Pricing pressures have eased considerably. The index for raw material prices fell from 72 in March to 12 in November. The ability to pass these costs on to the consumer also declined, though, with its index standing at 1.

Expectations are positive for the next six months, with respondents' sentiments virtually identical to their responses in October. The composite index for expectations was 12 in November, down from 13 in October. New orders, production, employment and capital expenditures are expected to grow moving forward, which is a positive sign. This optimism is consistent with other regional surveys, as well.

Personal Income (October)

[The Bureau of Economic Analysis found that personal income rose 0.4 percent in October, its fastest pace since March, with personal consumption up 0.1 percent.](#)

Consumer spending grew 0.8 percent for durable goods items, building on the 2.9 percent increase in September. Spending on nondurable goods, though, dropped 0.2 percent. Consumption is up 4.7 percent since October 2010. Wages and salaries for manufacturing workers totaled \$709 billion in October, up \$6.3 billion from September.

Personal disposable income rose 0.3 percent in October, both in nominal and real terms. The inflation rate, as determined by the personal consumption expenditure deflator, is currently 2.7 percent for all items or 1.7 percent when food and energy costs are excluded (with the latter being the "core" inflation rate).

The savings rate is now 3.5 percent, which is slightly higher than the 3.3 percent rate observed last month but still lower than the 5 percent found in June. The downward trend in recent months has been a function of consumer spending growth outstripping the increases in personal income. This month's stronger growth in personal income helped to lift the savings rate by 0.2 percentage points.

Regional and State Employment (October)

[The Bureau of Labor Statistics reported that regional and state employment numbers fell in most states in October.](#) Nevada had the highest unemployment rate at 13.4 percent, with North Dakota's 3.5 percent the lowest in the nation. The U.S. unemployment rate, [as reported earlier in the month](#), was 9.0 percent. Illinois and California had the largest monthly increases in nonfarm employment with 30,000 and 25,000 net new jobs, respectively.

States with the fastest growth in manufacturing employment were Michigan (up 3,600), Kentucky (up 2,900) and Mississippi (up 2,000). Breaking it down between durable and nondurable goods jobs, Pennsylvania (up 2,000), Washington (up 1,700) and Michigan (up 1,500) had the largest monthly gains in durable goods employment. Meanwhile, Michigan (up 2,100), Illinois (up 1,400) and Louisiana had the biggest increases in nondurable goods employment.

Richmond Fed Manufacturing Survey (November)

The composite index in the [Richmond Federal Reserve Bank's manufacturing survey](#) contracted five of the six months between May and October. In light of that, the zero reading for November seems positive in that manufacturing activity has stopped

contracting, at least for now.

Much of this report highlights that conditions were unchanged from October, with little change in shipments, employment and the average workweek. The index for new orders was -2 in November, an improvement from the -17 reading of September and -5 for October. Some modest upticks in supplier delivery time and wages were observed.

In terms of pricing pressures, respondents reported that raw material prices grew 3.42 percent on average at annual rates, which was higher than the 2.20 percent observed last month. Finished goods prices rose 2.64 percent for the month. This also was above last month's average price increase of 1.75 percent. Manufacturers will continue to see elevated pricing pressures over the next six months.

As we have seen in many of these regional sentiment surveys, manufacturers in the Richmond district are significantly more upbeat about future activity, with the composite index up from 28 in October to 36 in November. Respondents anticipate faster growth in new orders, shipments, capital expenditures and employment moving forward.

University of Michigan Consumer Sentiment (November)

[The University of Michigan and Thomson Reuters observed higher consumer sentiment in November, with its index rising from 60.9 in October to 64.1 in November.](#) According to its press release, consumers anticipate "a slowly improving economy, and more importantly, slow gains in employment." Measures for present conditions as well as future expectations both increased slightly, but it was the growth in anticipated economic conditions that led the gain. It increased from 51.8 to 55.4.

It is important to keep in mind that these numbers still reflect an anxious American consumer. The index is still relatively low even with this month's gain. It remains 10 points lower than six months ago, and well below where it stood pre-recession.

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Questions or Comments?
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