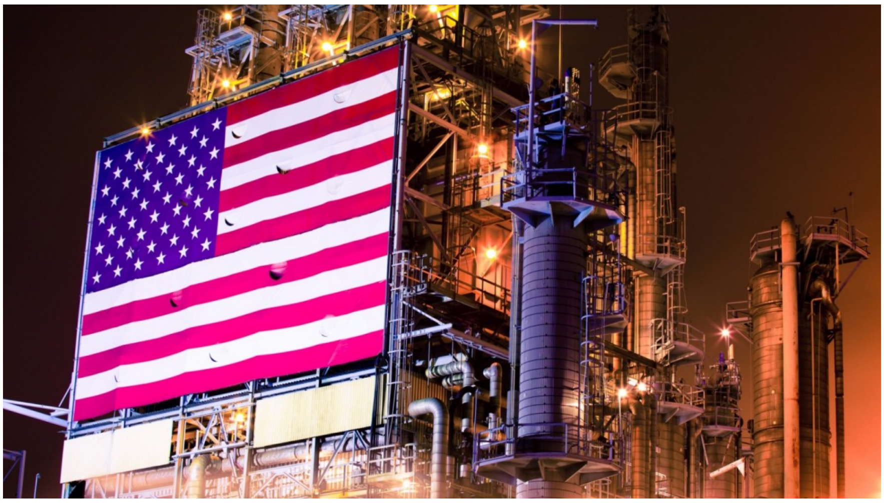
US: Manufacturing dip is just the start

The headline ISM index fell less than feared, but the underlying components painted a darker picture. With business and consumer sentiment falling sharply, lay-offs spiking and movement restrictions spreading across the country the April report will be much weaker

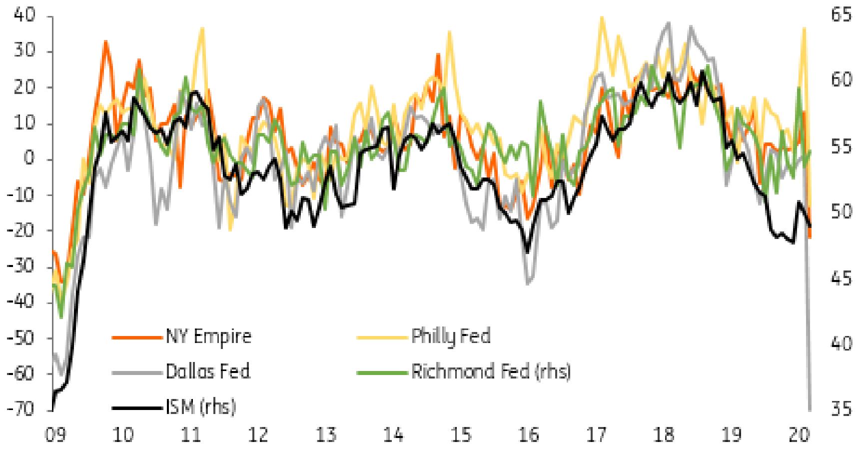


Source: iStockphoto

The good news is that the ISM headline index for the manufacturing sector hasn't collapsed in the wake of the Covid-19 crisis. It dipped marginally to 49.1 from 50.1 versus the 44.5 consensus with production holding up relatively well at 47.7 - it was actually lower in December at the height of the US-China trade tension fallout.

Of course, as the chart below shows, different regions are facing different situations with the Dallas Fed region obviously hit by the double whammy of the collapse in the oil price in addition to the economic dislocation relating to containment measures surrounding Covid-19.

Headline ISM versus regional manufacturing surveys

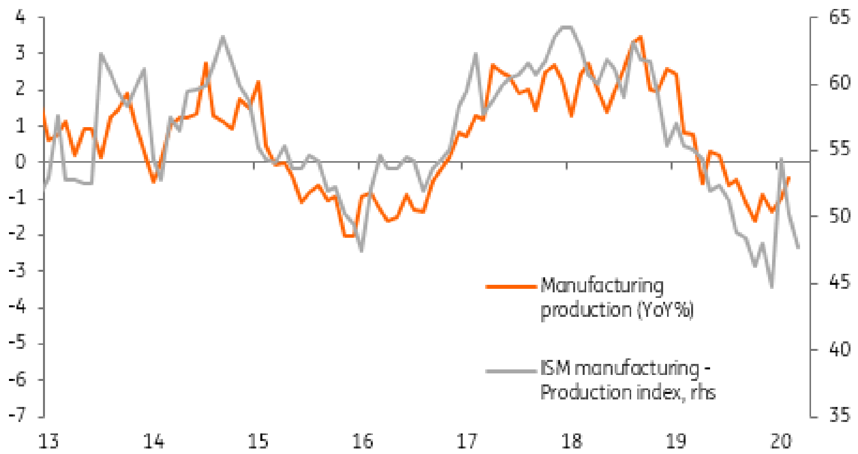


Source: Bloomberg, ING

New orders were understandably weaker, as was employment, both of which fell to their lowest levels since the global financial crisis in 2009.

Coupled with the tightening restrictions on working practices, which are now extended to the end of the month with stricter measures spreading across more and more states, the production component will fall much more sharply in April. In combination with the obvious plunge in consumer spending, this reinforces our fears about a potential 10% decline in economic activity - equivalent to an annualised 40% decline in GDP for the second quarter.

ISM production index versus manufacturing production



Source: Macrobond, ING

Why you should ignore the headline reading....

The headline index is being artificially boosted by a surge in the supplier delivery times component of the report. Normally, when delivery times are longer this reflects demand outstripping supply – a good situation.

However today delivery times are extended because of the supply shock relating to Covid-19 with firms struggling to get inputs from China and increasingly from domestic suppliers because of company shutdowns, which is clearly a bad situation. As such, the ISM headline is painting an overly rosy picture right now and this helps to explain why non-manufacturing surveys are performing far worse than the manufacturing equivalents around the world.

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