

US manufacturing woes mount

US manufacturing output has now contracted in six of the first nine months of 2019. With the economic slowdown spreading to other parts of the US economy, the Federal Reserve will likely have to respond with several more rate cuts



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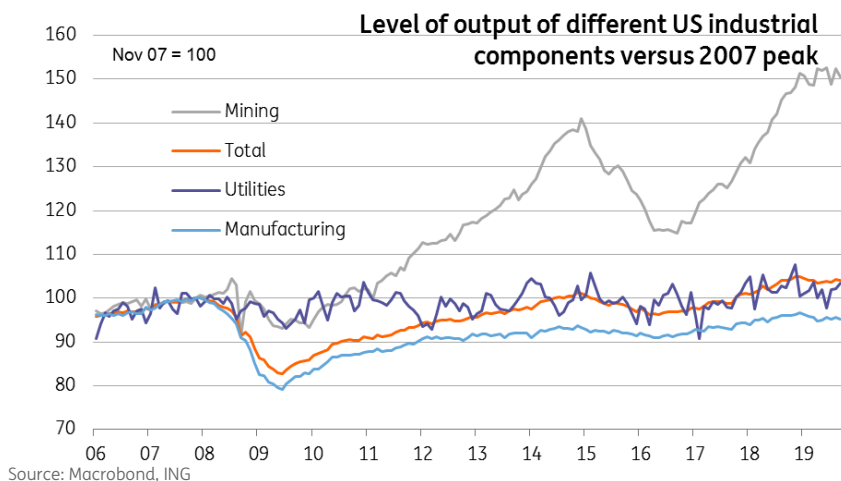
Well, it is another grim day for US economic data with industrial production and manufacturing output both falling more than expected in September, although we do acknowledge this follows on from a surprisingly robust set of numbers in August. With business surveys hinting at a deepening recession for US manufacturing, the case for additional Federal Reserve rate cuts remains very strong.

Manufacturing remains the weak link

US industrial output fell 0.4% in September versus expectations of a 0.2% drop, although August's output was revised up two-tenths of a percentage point to a 0.8% month-on-month gain. This leaves year-on-year growth at -0.1%, which is the worst annual rate of growth since November 2016. The details show that manufacturing continues to be the main drag, falling -0.5% MoM/-0.9% YoY, which is clearly not helped by the United Auto Workers' strike at GM – vehicle and parts output fell 4.2% MoM. This component should rebound next month given the apparent agreement with the union, but in general the manufacturing sector remains very weak.

Manufacturing output overall is still down 4.8% from the pre-global financial crisis peak while employment in the sector is down 10%. Mining continues to be the clear success story given the shale oil and gas revolution, although output fell 1.3% in September. Utilities output was the only component to post a gain in September, rising 1.4% MoM.

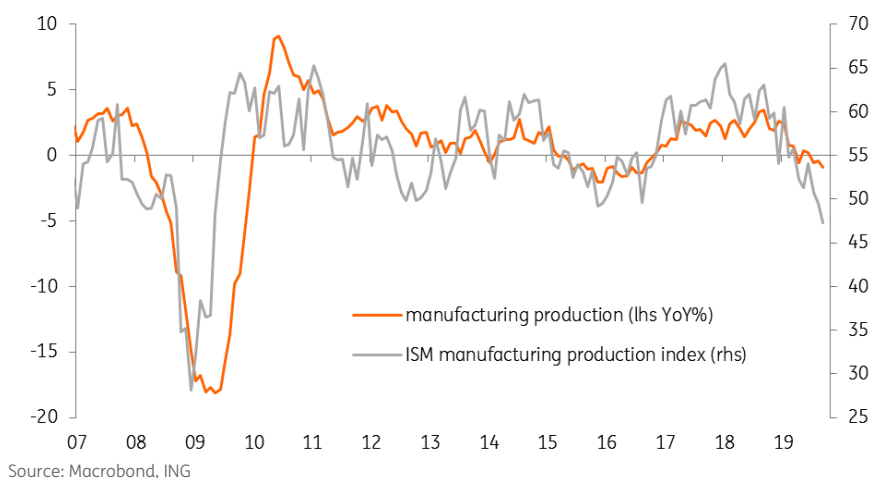
Level of US industrial output by sector



Further pain is coming

Looking ahead the outlook for manufacturing remains poor. Global economic weakness is hurting business sentiment and is resulting in weaker export growth. The strength of the dollar is compounding the problem and then when we add in the lingering negatives from the US-China trade war there is seemingly little to be optimistic about right now. Indeed, the ISM manufacturing index is currently at levels consistent with manufacturing growth contracting at a -5% YoY rate versus the current -0.9% rate.

ISM index points to much more downside potential for manufacturing



The Fed has more work to do

Given the weakness in manufacturing is seemingly spreading to the service sector and consumer spending based on the recent non-manufacturing ISM and retail sales readings it looks as though our fears of a major US slowdown are materializing. We are forecasting GDP growth of just 1.3% next year versus the 1.8% consensus forecast and as such look for the Fed to continue responding with rate cuts. We look for moves in October and December, and in January 2020.

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