ECONOMIC UPDATE
REGIONS
September 15, 2017

August Industrial Production: Output Down Across The Board

- Industrial production fell by 0.9 percent in August, with manufacturing output down by 0.3 percent.
- The overall capacity utilization rate fell to 76.1 percent, while the utilization rate in manufacturing fell to 75.3 percent.
- On a year-over-year basis, total industrial production was up by 1.5 percent in August, with manufacturing output up by 1.5 percent.

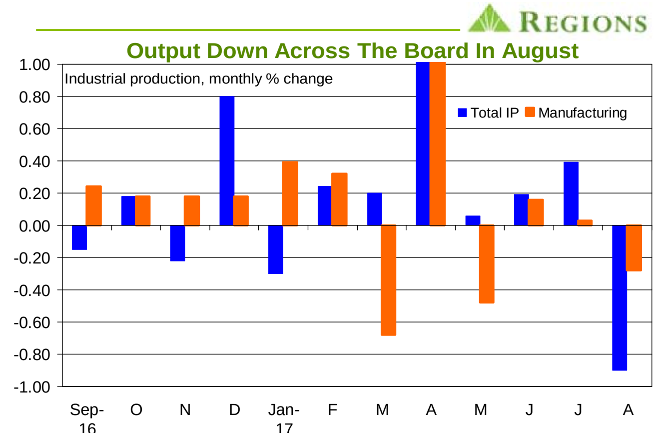
Total output amongst the nation's factories, mines, and utilities fell by 0.9 percent in August, with output down in each of the three broad sectors, manufacturing, mining, and utilities. Estimates by the Federal Reserve, which produces the monthly industrial production data and reports, show Hurricane Harvey lowered growth in total industrial output by 0.75 percentage points in August, with particularly large drags on mining and manufacturing output. While we had expected to see some effects of Harvey in the August data, we are a bit surprised the impact was this pronounced. Manufacturing output fell by 0.3 percent in August despite a modest bounce back in motor vehicle assemblies. Year-on-year, total industrial production and manufacturing output were both up 1.5 percent in August.

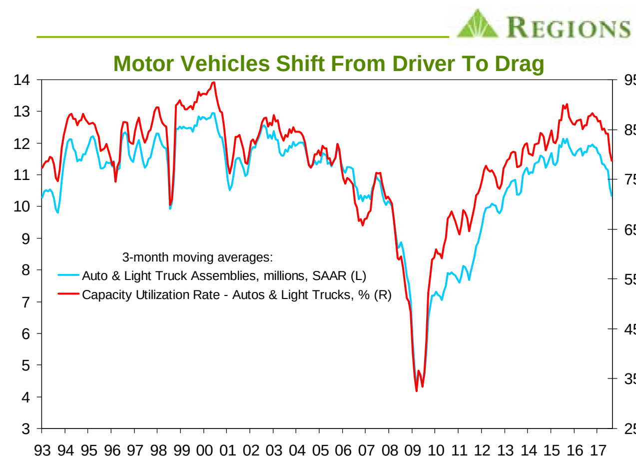
After having slipped to a four-year low of 9.857 million units in July, assemblies of autos and light trucks rebounded to 10.397 million units in August (these are annualized rates). There is likely a considerable degree of noise in the assembly data over recent months. While July is the traditional seasonal shutdown for retooling ahead of the new model year, this year saw extended breaks in many factories while others have cut shifts entirely and laid off workers in the face of bloated inventories – mainly in the form of smaller, fuel efficient automobiles that have fallen out of favor after a prolonged period of low gasoline prices. As can be seen in our middle chart, motor vehicle production has fallen sharply over recent months and, as unit sales continue to recede from their cyclical peak, is likely to fall further over coming months. While some have argued replacing vehicles damaged or destroyed by Hurricanes Harvey and Irma will provide support for motor vehicle manufacturing, we're not so sure. As noted above, inventories remain notably high, and if consumers are provided blue book, as opposed to new vehicle replacement, value in insurance settlements, then sales of used vehicles could see the most pronounced effects from replacements. Moreover, in light on an ongoing decline in the trend rate of sales, any such lift to new production would be transitory.

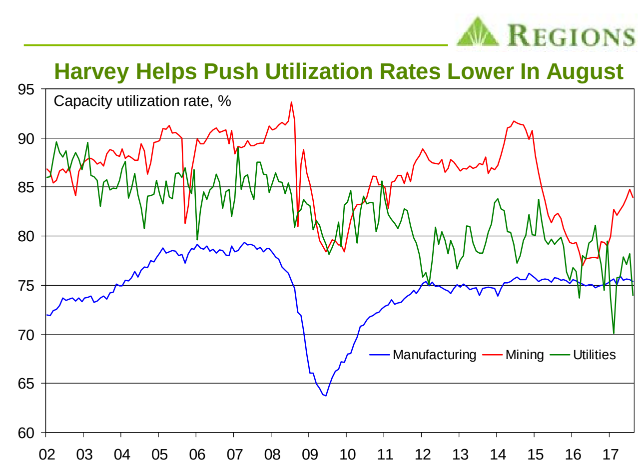
Manufacturing output excluding motor vehicles fell by 0.5 percent in August. One surprise here is that production of industrial machinery fell by 1.4 percent, which includes a 2.5 percent decline in production of electrical equipment. Given steady, if still somewhat sluggish, growth in core capital goods orders over recent months, the August data seem more like a one-off drop than an ominous sign of weakness over coming months, and the August industrial production data are also at odds with the ongoing strength seen in the ISM Manufacturing Index. Petroleum and coal output fell by 1.6 percent in August, which to a large extent reflects the impact of Harvey on refinery activity, and this should persist into the September data. The effects of Harvey are also seen in the 0.8 percent decline in mining output, which reflects lower oil and gas extraction as well as diminished drilling of new oil and gas wells due to the hurricane. Utilities output plummeted in August, falling 5.5 percent. While some of this decline can be attributed to Hurricane Harvey, as it would have weighed on demand in those areas impacted by the storm, the bigger factor is what in many parts of the U.S. were below-normal temperatures in August the held down usage of air conditioning.

Utilization rates were pushed lower in August, which in the mining and manufacturing sectors reflects the impacts of Hurricane Harvey. This could be more pronounced in the September data, but the bigger picture here shows what remains a fairly high degree of idle capacity in the manufacturing sector, which will constrain price pressures even as global demand for goods and services continues to expand at a somewhat faster pace.

As with many other series, the industrial production data will be very noisy for the next few months. In light of this, it is helpful to remain mindful of what had been steadily improving conditions in the industrial sector prior to the hurricanes.







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