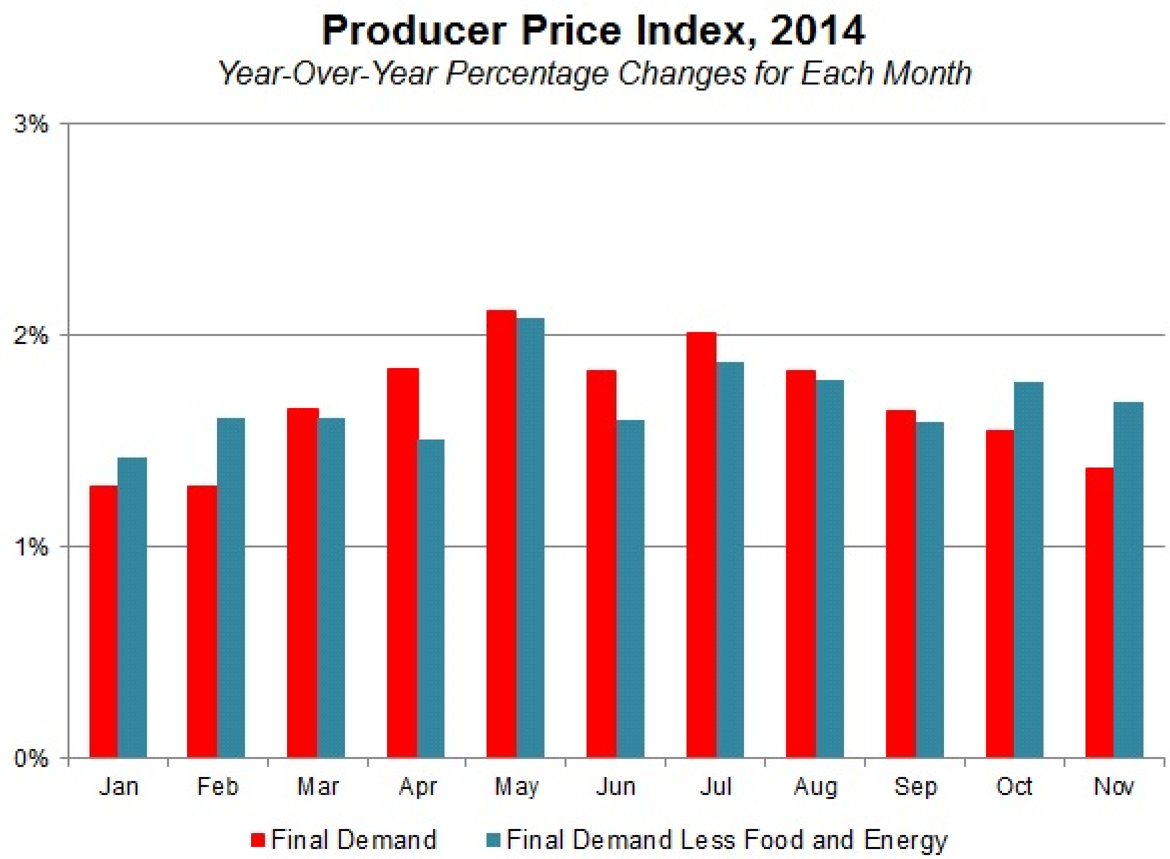
A Publication of the National Association of Manufacturers

Monday Economic Report

December 15, 2014



The biggest domestic economic news story last week was actually a global one: The price of petroleum continued to plummet. Since peaking at $107.95 per barrel on June 20, the price of West Texas Intermediate crude has fallen dramatically, down to $57.49 a barrel on Friday. There are a number of factors at play here, including increased North American energy production, excess supply worldwide, a stronger U.S. dollar and a slowing global economy. It is this latter point that has spooked financial markets, on fear that the weakened global demand for petroleum might be a harbinger of larger challenges. Indeed, as discussed in the most recent *Global Manufacturing Economic Update*, North America's economy appears to be a bright spot in an otherwise sluggish international economic climate.

Of course, reduced petroleum costs also provide benefits to the larger macroeconomy. Producer prices fell 0.2 percent in November, with lower energy prices reducing overall inflationary pressures in the U.S. economy. In fact, producer prices for final demand energy goods have fallen 8.8 percent since June, and core inflation, which excludes food and energy costs, has now remained below 2 percent for six consecutive months, which is the Federal Reserve's stated goal.

Americans are spending less to fill their gas tanks, with the Energy Information Administration reporting that regular gasoline sold for $2.68 a gallon on average last week. This should help boost consumer spending in other categories, and, in fact, retail sales grew strongly in November, up 0.7 percent for the month and 5.1 percent year-over-year. Such healthy gains should help to erase anxieties about holiday spending, as this was a strong number. Moreover, consumer confidence soared to its highest level since January 2007, according to the University of Michigan and Thomson Reuters. Lower energy costs and an improved economic outlook likely contributed to the increased perceptions.

Other recent surveys have also highlighted the better outlook for the U.S. economy. As noted in last week's report, the NAM/*IndustryWeek* Survey of Manufacturers found that respondents were mostly upbeat about their own company's outlook, with sales and employment expected to grow relatively strongly over the next 12 months. Exports were anticipated to slow somewhat due to the softer global economy, however, and manufacturers continued to express frustrations with Washington. The top policy objective noted in the survey was a desire to reduce regulatory burdens, cited by 82.8 percent of manufacturers. Rising health care costs were once again listed as the top business challenge, with an average premium increase for 2015 of 9.5 percent, with smaller manufacturers experiencing even larger cost increases.

The most recent McGladrey Manufacturing & Distribution Monitor Report was equally encouraging about the current state of the sector, with 36 percent of executives surveyed saying that their firms were "thriving." Meanwhile, small business owners were also more upbeat in the latest National Federation of Independent Business survey. The Small Business Optimism Index rose to its highest level since February 2007, with better sales expectations helping to explain much of that rise. Hiring plans also improved. Yet, even with the better data, small firms continue to suggest that earnings remain soft. In addition, taxes and regulations are the most cited problems. For their part, respondents to the National Association for Business Economics survey were more positive in their forecasts than three months ago. Economists expect the U.S. economy to grow 2.9 percent on average in 2015, with industrial production expanding by 3.5 percent.

This morning, we will get new industrial production data for November, and it is expected to show an increase of around 0.5 percent for November. In addition, manufacturing sentiment surveys from the Kansas City, New York and Philadelphia Federal Reserve Banks will provide regional perspectives on activity, and Markit will release Flash Manufacturing Purchasing Managers' Index data for China, the Eurozone, Japan and the United States for a global view. As such, we will get a better sense on the health of the manufacturing sector this week. In addition, the latest housing starts and consumer price index data will be reported. Beyond those data points, the Federal Open Market Committee will meet, releasing a new policy statement on Wednesday. The Federal Reserve is expected to maintain its current monetary policy stances, with conventional wisdom holding that short-term interest rates will begin to rise in mid-2015.

Chad Moutray
Chief Economist
National Association of Manufacturers

Share The Monday Economic Report with your social network:

Economic Indicators

Last Week's Indicators:
(Summaries Appear Below)

Monday, December 8
NABE Outlook Survey
NAM/IndustryWeek Survey of Manufacturers

Tuesday, December 9
Job Openings and Labor Turnover Survey
NFIB Small Business Survey

Wednesday, December 10
None

Thursday, December 11
Retail Sales

Friday, December 12
Producer Price Index
University of Michigan Consumer Sentiment

This Week's Indicators:

Monday, December 15
Industrial Production
NAHB Housing Market Index
NY Fed Empire State Manufacturing Survey

Tuesday, December 16
Housing Starts and Permits
Markit Flash Manufacturing PMIs for China, the Eurozone, Japan and the United States

Wednesday, December 17
Consumer Price Index
FOMC Monetary Policy Statement

Thursday, December 18
Conference Board Leading Indicators
Philadelphia Fed Manufacturing Survey

Friday, December 19
Kansas City Fed Manufacturing Survey
State Employment Report

Summaries for Last Week`s Economic Indicators

Job Openings and Labor Turnover Survey

The Bureau of Labor Statistics reported that manufacturing job openings eased slightly, down from 293,000 in September to 290,000 in October. Nonetheless, the sector has seen improvements in the pace of job postings, with an average of 294,000 over the past six months (May through October). This represents progress since February's rate of 258,000, the low point of 2014 so far. In October, job openings for durable goods firms were up from 179,000 to 190,000, whereas postings for nondurable goods businesses dropped from 115,000 to 100,000.

Net hiring was also somewhat lower in October. Manufacturers hired 275,000 workers in October, down from 279,000 in September. This was still more than earlier in the year, with 234,000 in February. At the same time, total separations, including layoffs, quits and retirements, were up from 256,000 in September to 260,000 in October. As a result, net hiring (or hires minus separations) fell from 23,000 in September to 15,000 in October. Yet, the average over the past six months was 17,333 for manufacturers, a relatively healthy pace.

In the larger economy, nonfarm job openings rose from 4,685,000 to 4,834,000 for the month. There were pickups in postings for construction; health care; leisure and hospitality; and trade, transportation and utilities. Net hiring was off slightly, down from 266,000 to 231,000. However, net hiring remains strong overall, mirroring larger job trends in recent employment data.

NABE Outlook Survey

The National Association for Business Economics provided an encouraging economic outlook in its latest survey. Business economists anticipate 2.7 percent growth in real GDP in the current (or fourth) quarter, with an average of 2.9 percent expected in 2015. There were slight upticks in the forecast in the December survey relative to responses noted in September. In particular, respondents were somewhat more upbeat about nonresidential fixed investment growth, including for structures, equipment and software and intellectual property products.

Industrial production is seen expanding by 4.0 percent in 2014, with 3.5 percent growth in 2015. Along those lines, light vehicles sales are predicted to increase from an average of 16.4 million units in 2014 to 16.8 million in 2015, and housing starts are expected to grow from 1.00 million annualized units this year to 1.15 million next year. In terms of the labor market, nonfarm payrolls are forecasted to increase by 217,000 each month in 2015, with the unemployment rate falling to 5.6 percent by year's end. (My own forecast has the unemployment rate declining to 5.4 percent, with faster monthly job growth.)

Business economists were asked when they anticipate the Federal Reserve beginning to raise the federal funds rate, and roughly three-quarters expect this to occur in the second or third quarters of 2015. Inflation should remain near the 2 percent goal stated by the Federal Reserve, with 10-year Treasury note yields rising from 2.50 percent on average in 2014 to 3.20 percent in 2015. Meanwhile, the U.S. dollar is expected to continue its recent strength.

NAM/IndustryWeek Survey of Manufacturers
In the latest NAM/*IndustryWeek* Survey of Manufacturers, business leaders continue to reflect optimism about the coming months. Overall, 91.2 percent of survey respondents said they are either somewhat or very positive about their own company's outlook. Moreover, manufacturers predict growth of 4.5 percent in sales and 2.1 percent in employment over the next 12 months, with both experiencing the strongest pace in at least two years.

In addition, the NAM/*IndustryWeek* survey noted that the expected pace of exports decelerated once again, mirroring the slow growth in manufactured goods exports. The survey also found that manufacturers remain frustrated with Washington, particularly regarding rising health care costs and regulatory burdens. At the same time, nearly 65 percent were more optimistic that policymakers would address our long-term challenges in light of the midterm election results.

NFIB Small Business Survey
The National Federation of Independent Business reported that small business sentiment reached a pre-recessionary high in December. The Small Business Optimism Index rose from 96.1 in October to 98.1 in November, its highest level since February 2007. This is a significant milestone, particularly given the fact that smaller firms have struggled much longer than their larger counterparts to see progress in terms of activity and outlook. Along those lines, the index remains below 100, a level that would indicate strong growth in the sector. Still, the latest data suggest movement in the right direction.

Smaller firm owners were more upbeat about sales in November, helping to explain the bump in optimism. The net percentage of respondents expecting sales to increase over the next three months rose from 9 percent to 14 percent. Moreover, employment plans were also higher. The percentage planning to hire in the next three months increased from 10 percent to 11 percent. In addition, the percentage suggesting the next three months were a good time to expand remained unchanged at 11 percent.

However, small businesses still have challenges. Earnings remain soft, and economic conditions continue to be the top reason for those suggesting it was not a good time for expansion. In addition, government actions remain an issue. Small business owners cited taxes (23 percent) and regulations (22 percent) as their top problems in November.

Producer Price Index
The Bureau of Labor Statistics reported that producer prices for final demand goods and services declined 0.2 percent in November. Producer prices for final demand goods fell for the fifth straight month, down 0.7

percent, or 1.7 percent since June. Much of that decline, as you might expect, stemmed from reduced energy costs, which have decreased 8.8 percent since June and were off 3.1 percent in November. Of course, petroleum prices have continued to fall since then, with West Texas Intermediate crude selling for $57.49 a barrel on Friday, a level last seen in mid-2009. This has helped to reduce overall pricing pressures in the economy.

At the same time, food prices were also lower in November, down 0.2 percent. Despite the easing for the month, final demand food costs have risen 4.6 percent so far in 2014. In November, there was some relief in many areas that have grown the most this year, including cooking oils, dairy products, eggs, meats and vegetables. Yet, prices for grains and bakery products were up sharply in November.

Excluding food and energy, producer prices for final demand goods decreased 0.1 percent. There were reduced prices for cosmetics, industrial chemicals, light motor trucks, metal forming machines, mining machinery and transformers and power regulators, among others. These were slightly offset, however, by higher costs for jewelry, paper industry machinery, pharmaceutical preparations, pumps and compressors and sporting goods.

On a year-over-year basis, producer prices for final demand goods and services have risen 1.4 percent, down from 2.1 percent in May and 1.6 percent in October. Core inflation, which excludes food and energy costs, was up 1.7 percent over the past 12 months, or the sixth consecutive month with core prices below the Federal Reserve’s stated goal of 2 percent.

As such, pricing pressures appear to be under control, at least for now, assisted more recently by lower energy costs. This has given the Federal Reserve a freer hand to pursue accommodative policies without worry of excessive inflation. Regardless, conventional wisdom holds that the Federal Reserve will start raising short-term rates in mid-2015, with improved economic growth necessitating the moves toward normalization.

Retail Sales
The Census Bureau provided encouraging news about retail sales growth in November. Retail spending was 0.7 percent in November, extending the revised 0.5 percent growth seen in October. This is noteworthy because it will help to erase anxieties about holiday spending seen in prior estimates. On a year-over-year basis, retail spending has increased 5.1 percent, a relatively healthy pace, up from 4.5 percent in October.

Gasoline sales were lower, down 0.8 percent, driven by reduced energy costs. Indeed, the Energy Information Administration says that the average price of regular gasoline fell from $2.99 per gallon on November 3 to $2.68 on December 8. Such pocketbook savings have the potential to boost consumer spending in other categories, acting as a stimulus for economic growth.

Outside of gasoline, consumer spending was mostly higher, beating expectations. Areas with the fastest growth included motor vehicles and parts (up 1.7 percent), building materials and supplies (up 1.4 percent), clothing and accessories (up 1.2 percent), department stores (up 1.0 percent), non-store retailers (up 1.0 percent) and electronics and appliances (up 0.9 percent). Many of these categories speak to strong holiday sales. In addition, Americans have also started to eat out more, with spending at food services and drinking places up 0.7 percent in November.

Over the past 12 months, the categories with the most growth were non-store retailers (up 8.7 percent), motor vehicles and parts (up 8.6 percent), building materials and supplies (up 7.8 percent), electronics and appliances (up 6.9 percent), health and personal care items (up 6.8 percent) and food services and drinking places (up 6.7 percent). Excluding autos, the year-over-year pace for retail sales was 4.3 percent, up from 3.5 percent the month before.

University of Michigan Consumer Sentiment
Preliminary consumer confidence numbers soared to their highest level since January 2007, according to the

University of Michigan and Thomson Reuters. The Consumer Sentiment Index rose from 88.8 in November to 93.8 in December. Measures for the current (up from 102.7 to 105.7) and forward-looking (up from 79.9 to 86.1) economic outlook were both higher for the month. The data suggest that Americans were more upbeat in their assessments of the economy, perhaps boosted by improvements in the labor market and by cheaper gasoline prices.

At least in this report, challenges in global markets or worries about income growth were downplayed. A similar survey from the Conference Board, on the other hand, fell in November, largely on persistent anxieties about those issues. We will get final numbers on the University of Michigan's consumer confidence data on December 23, with the Conference Board releasing its latest report on December 30.

Connect with the Manufacturers

Questions or comments?

Contact Chief Economist Chad Moutray at cmoutray@nam.org.

.