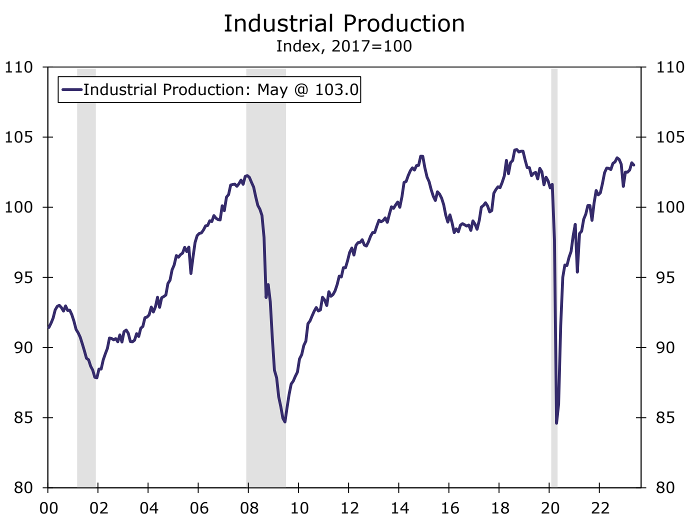
Economic Indicator — June 15, 2023

Modest Gain at Factories Offset by Production Cuts at Utilities & Mines

Summary

Industrial production fell 0.2% in May owing to a sharp drop in utilities output and a more modest dip in mining activity which swamped a scant 0.1% gain in production in the much larger manufacturing category. Meanwhile, mixed signals from regional Fed surveys muddy the outlook.



Source: Federal Reserve Board and Wells Fargo Economics

Economist(s)

Tim Quinlan
Senior Economist | Wells Fargo Economics
Tim.Quinlan@wellsfargo.com | 704-410-3283

Shannon Seery
Economist | Wells Fargo Economics
Shannon.Seery@wellsfargo.com | 332-204-0693

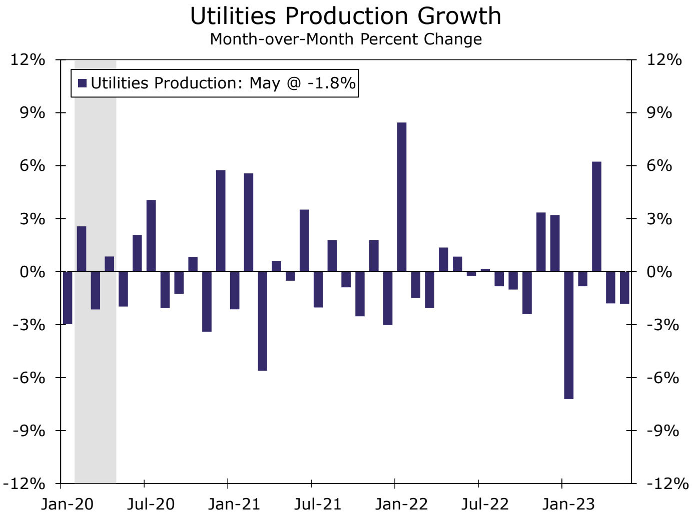
Nicole Cervi
Economic Analyst | Wells Fargo Economics
Nicole.Cervi@wellsfargo.com | 704-410-3059

Making Sense of the Crosscurrents

Industrial production fell 0.2% in May (chart). Manufacturing production, which comprises roughly three quarters of all output, actually eked out a scant gain of 0.1%. The headline decline was a result of a steep decline of 1.8% in utilities production as well as a more modest drop of 0.4% in mining activity (chart).

There are most definitely cross-currents in today's manufacturing sector and that was on full display in this morning's batch of economic data which started with the release of regional Fed surveys just before the industrial production report. The Empire Manufacturing Index rose to 6.6 in June, an unexpected rebound after coming in at -31.8 the prior month. New orders climbed back above breakeven, indicating manufacturing orders across New York State have edged higher. Down I-95, the Philadelphia Fed Business Outlook Survey index slipped further into contraction territory coming in at -13.7 in June, but current shipments and expectations for new orders both broke above zero.

The conflicting storylines in today's data make a little more sense when you dig into the details of the industrial production report. The parts of manufacturing tied to consumer and business equipment spending are evidently under pressure. The production of consumer goods and business equipment both declined. But amid government-supported construction of new factories to support the domestic production of semiconductors as well as ongoing infrastructure spending, construction output posted the largest gain of any major market group.



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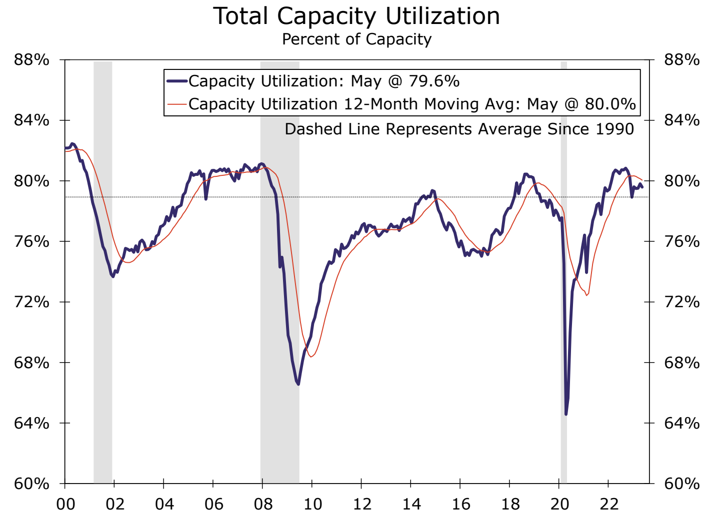

Source: Federal Reserve Board and Wells Fargo Economics

The outturn in today's industrial production report broadly aligns with the trends we have seen in the ISM manufacturing index. Improving supply chains have allowed production to post the occasional gain, even as the pipeline of new orders has significantly thinned over the past year. In May, the production component of the ISM edged back into expansionary territory for the first time since November 2022, mirroring the 0.1% rise in manufacturing production.

The ISM's gauge of new orders signaled contraction for the ninth straight month in May, yet purchasing manager indices from some regional Federal Reserve banks suggest demand may be stabilizing. In a separate report earlier this week, small business plans to increase capital expenditures jumped six percentage points in May to its highest since August 2022. That is a welcome development after a year of wobbly activity. Industrial production has been down in five of the past 12 months. For the Federal Reserve, the modest firming in activity may not be met with immediate inflationary pressure. Capacity utilization, a traditional leading indicator of inflation, edged lower 0.2 percentage points to 79.6% in May (chart). The slip signals that manufacturers have some excess capacity to produce, which should come as welcome news to monetary policymakers in their effort to get inflation in check.

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Economics Group

Jay H. Bryson, Ph.D.	Chief Economist	704-410-3274	Jay.Bryson@wellsfargo.com
Sam Bullard	Senior Economist	704-410-3280	Sam.Bullard@wellsfargo.com
Nick Bennenbroek	International Economist	212-214-5636	Nicholas.Bennenbroek@wellsfargo.com
Tim Quinlan	Senior Economist	704-410-3283	Tim.Quinlan@wellsfargo.com
Sarah House	Senior Economist	704-410-3282	Sarah.House@wellsfargo.com
Azhar Iqbal	Econometrician	212-214-2029	Azhar.Iqbal@wellsfargo.com
Charlie Dougherty	Senior Economist	212-214-8984	Charles.Dougherty@wellsfargo.com
Michael Pugliese	Senior Economist	212-214-5058	Michael.D.Pugliese@wellsfargo.com
Brendan McKenna	International Economist	212-214-5637	Brendan.Mckenna@wellsfargo.com
Jackie Benson	Economist	704-410-4468	Jackie.Benson@wellsfargo.com
Shannon Seery	Economist	332-204-0693	Shannon.Seery@wellsfargo.com
Nicole Cervi	Economic Analyst	704-410-3059	Nicole.Cervi@wellsfargo.com
Jessica Guo	Economic Analyst	212-214-1063	Jessica.Guo@wellsfargo.com
Karl Vesely	Economic Analyst	704-410-2911	Karl.Vesely@wellsfargo.com
Patrick Barley	Economic Analyst	704-410-1232	Patrick.Barley@wellsfargo.com
Jeremiah Kohl	Economic Analyst	704-410-1437	Jeremiah.J.Kohl@wellsfargo.com
Coren Burton	Administrative Assistant	704-410-6010	Coren.Burton@wellsfargo.com

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