

Economics Group

Tim Quinlan, Senior Economist
tim.quinlan@wellsfargo.com • (704) 410-3283
 Sarah House, Economist
sarah.house@wellsfargo.com • (704) 410-3282

Crummy Details Underneath Industrial Production's Gain

Industrial production rose 0.5 percent in March, but the gain was entirely driven by a surge in utilities. Manufacturing declined 0.4 percent, although we believe fundamentals still support the sector's expansion.

Utilities Whipsaw

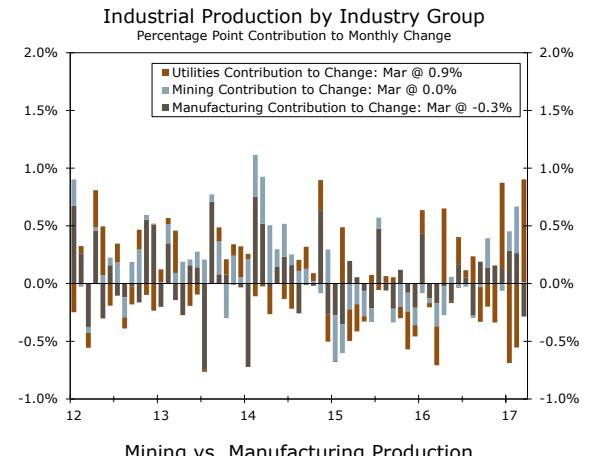
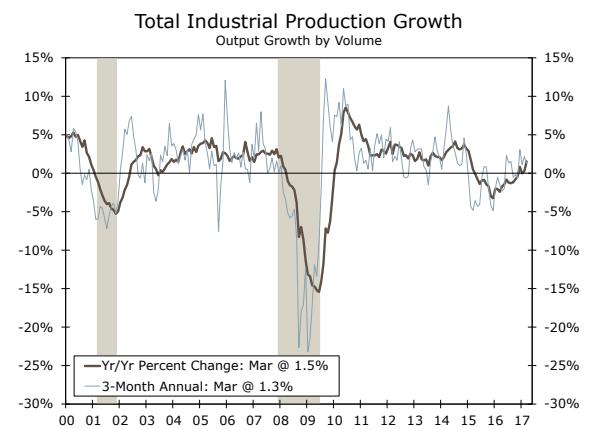
At first glance, the 0.5 percent rise in industrial production looks pretty solid, notching the second largest increase for the series in more than a year. However, a surge in utilities output accounted for nearly the entirety of the gains. After the second warmest February on record led to a 5.8 percent decline in utilities production, temperatures in the lower-48 returned to more seasonal norms in March. A late season snow storm in the Northeast and above-average temperatures in the Southwest drove utilities output up 8.6 percent. At about 11 percent of total index, utilities alone boosted the headline by 0.9 percentage points.

Mining output was virtually unchanged over the month, inching up just 0.1 percent. The oil and gas industry continued to make a comeback despite oil prices wobbling over the month. Output for oil and gas extraction was up 0.7 percent in March and drilling for oil and gas wells rose nearly 8 percent, which was just enough to offset sizeable drops in coal (down 14 percent month-over-month) and nonmetallic mineral mining (down 3.6 percent).

Malaise Returns to Manufacturing?

Hiding underneath the headline's apparent strength was a 0.4 percent decline in manufacturing production. The retreat follows six straight months of gains, but leaves factory output up 1.0 percent over the past year. Notable within the manufacturing sector was a 3.0 percent decline in motor vehicle and parts output. The pullback in autos production coincides with a sharp drop-off in sales in March. Already inventories were elevated heading into the month (the inventory-to-sales ratio at motor vehicles and parts dealers jumped to the second highest level since the recession in February). As a result, the decline in production should at least alleviate the growing inventory glut and help restrain the industry's use of incentives to drive sales. Excluding autos, however, manufacturing output still slipped 0.2 percent with declines across most durable and nondurable sub-industries.

The factory sector has been one area where the relationship between "hard" and "soft" survey data has held up relatively well in recent months, with both pointing to upward momentum. While today's industrial production figures and latest PMI readings from the ISM and Empire State Manufacturing Survey suggest some cooling, we still look for manufacturing output to expand in the coming months. The export environment for U.S. producers has improved with a pickup in global growth and relatively stable value of the dollar (at least compared to 2014-2015), while rising profits and wage pressures should help to revive business investment.



Wells Fargo Securities Economics Group

Diane Schumaker-Krieg	Global Head of Research, Economics & Strategy	(704) 410-1801 (212) 214-5070	diane.schumaker@wellsfargo.com
John E. Silvia, Ph.D.	Chief Economist	(704) 410-3275	john.silvia@wellsfargo.com
Mark Vitner	Senior Economist	(704) 410-3277	mark.vitner@wellsfargo.com
Jay H. Bryson, Ph.D.	Global Economist	(704) 410-3274	jay.bryson@wellsfargo.com
Sam Bullard	Senior Economist	(704) 410-3280	sam.bullard@wellsfargo.com
Nick Bennenbroek	Currency Strategist	(212) 214-5636	nicholas.bennenbroek@wellsfargo.com
Anika R. Khan	Senior Economist	(212) 214-8543	anika.khan@wellsfargo.com
Eugenio J. Alemán, Ph.D.	Senior Economist	(704) 410-3273	eugenio.j.aleman@wellsfargo.com
Azhar Iqbal	Econometrician	(704) 410-3270	azhar.iqbal@wellsfargo.com
Tim Quinlan	Senior Economist	(704) 410-3283	tim.quinlan@wellsfargo.com
Eric Viloria, CFA	Currency Strategist	(212) 214-5637	eric.viloria@wellsfargo.com
Sarah House	Economist	(704) 410-3282	sarah.house@wellsfargo.com
Michael A. Brown	Economist	(704) 410-3278	michael.a.brown@wellsfargo.com
Jamie Feik	Economist	(704) 410-3291	jamie.feik@wellsfargo.com
Erik Nelson	Currency Strategist	(212) 214-5652	erik.f.nelson@wellsfargo.com
Misa Batcheller	Economic Analyst	(704) 410-3060	misa.n.batcheller@wellsfargo.com
Michael Pugliese	Economic Analyst	(704) 410-3156	michael.d.pugliese@wellsfargo.com
Julianne Causey	Economic Analyst	(704) 410-3281	julianne.causey@wellsfargo.com
E. Harry Pershing	Economic Analyst	(704) 410-3034	edward.h.pershing@wellsfargo.com
Donna LaFleur	Executive Assistant	(704) 410-3279	donna.lafleur@wellsfargo.com
Dawne Howes	Administrative Assistant	(704) 410-3272	dawne.howes@wellsfargo.com

Wells Fargo Securities Economics Group publications are produced by Wells Fargo Securities, LLC, a U.S. broker-dealer registered with the U.S. Securities and Exchange Commission, the Financial Industry Regulatory Authority, and the Securities Investor Protection Corp. Wells Fargo Securities, LLC, distributes these publications directly and through subsidiaries including, but not limited to, Wells Fargo & Company, Wells Fargo Bank N.A., Wells Fargo Advisors, LLC, Wells Fargo Securities International Limited, Wells Fargo Securities Asia Limited and Wells Fargo Securities (Japan) Co. Limited. Wells Fargo Securities, LLC, is registered with the Commodities Futures Trading Commission as a futures commission merchant and is a member in good standing of the National Futures Association. Wells Fargo Bank, N.A. is registered with the Commodities Futures Trading Commission as a swap dealer and is a member in good standing of the National Futures Association. Wells Fargo Securities, LLC. and Wells Fargo Bank, N.A. are generally engaged in the trading of futures and derivative products, any of which may be discussed within this publication. Wells Fargo Securities, LLC does not compensate its research analysts based on specific investment banking transactions. Wells Fargo Securities, LLC's research analysts receive compensation that is based upon and impacted by the overall profitability and revenue of the firm which includes, but is not limited to investment banking revenue. The information and opinions herein are for general information use only. Wells Fargo Securities, LLC does not guarantee their accuracy or completeness, nor does Wells Fargo Securities, LLC assume any liability for any loss that may result from the reliance by any person upon any such information or opinions. Such information and opinions are subject to change without notice, are for general information only and are not intended as an offer or solicitation with respect to the purchase or sales of any security or as personalized investment advice. Wells Fargo Securities, LLC is a separate legal entity and distinct from affiliated banks and is a wholly owned subsidiary of Wells Fargo & Company. © 2017 Wells Fargo Securities, LLC.

Important Information for Non-U.S. Recipients

For recipients in the EEA, this report is distributed by Wells Fargo Securities International Limited ("WFSIL"). WFSIL is a U.K. incorporated investment firm authorized and regulated by the Financial Conduct Authority. The content of this report has been approved by WFSIL a regulated person under the Act. For purposes of the U.K. Financial Conduct Authority's rules, this report constitutes impartial investment research. WFSIL does not deal with retail clients as defined in the Markets in Financial Instruments Directive 2007. The FCA rules made under the Financial Services and Markets Act 2000 for the protection of retail clients will therefore not apply, nor will the Financial Services Compensation Scheme be available. This report is not intended for, and should not be relied upon by, retail clients. This document and any other materials accompanying this document (collectively, the "Materials") are provided for general informational purposes only.

SECURITIES: NOT FDIC-INSURED/NOT BANK-GUARANTEED/MAY LOSE VALUE



SECURITIES