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MONDAY ECONOMIC REPORT

NAM Survey: 63% of Manufacturers Expect a Recession in 2022 or 2023

By Chad Moutray – September 26, 2022

The Weekly Toplines

- In the Q3 Manufacturers' Outlook Survey, 75.6% of respondents felt either somewhat or very positive about their company outlook, down from 82.6% in the second quarter. It was the weakest reading since the fourth quarter of 2020, with growth slowing notably across the board. Indeed, sentiment was just marginally above the historical average, which was 75.2%, illustrating just how much manufacturing activity has stalled year to date.

- At the same time, 63.3% of manufacturing leaders believed that the U.S. economy would officially slip into a recession in either 2022 or 2023.

- Meanwhile, supply chain challenges topped the list of primary business challenges in the third quarter, cited by 78.3% of respondents. Just 10.8% anticipate these disruptions improving by the end of 2022, with 60.7% expecting some abatement in 2023. The other leading concerns included attracting and retaining a quality workforce (76.1%), increased raw material costs (76.1%) and transportation and logistics costs (65.9%).

- The S&P Global Flash U.S. Manufacturing PMI ticked slightly higher, up from 51.5 in August, which was a 25-month low, to 51.8 in September. As such, the sector continued to expand, but at a lukewarm pace and with the underlying data mixed.

- Manufacturing activity expanded at the slowest pace since July 2020 in the Kansas City Federal Reserve Bank's district, with new orders contracting for the fourth straight month. Respondents cited soaring costs, supply chain issues and workforce challenges in their comments.

- The Federal Open Market Committee has increased the federal funds rate by 75 basis points, as expected, to 3.00% to 3.25%. In the economic projections, FOMC participants suggested that the federal funds target rate could increase to 4.25% to 4.50% by year's end. This would seem to imply another 75-basis-point hike at the Nov. 1–2 meeting, followed by a 50-basis-point increase at its Dec. 13–14 meeting.

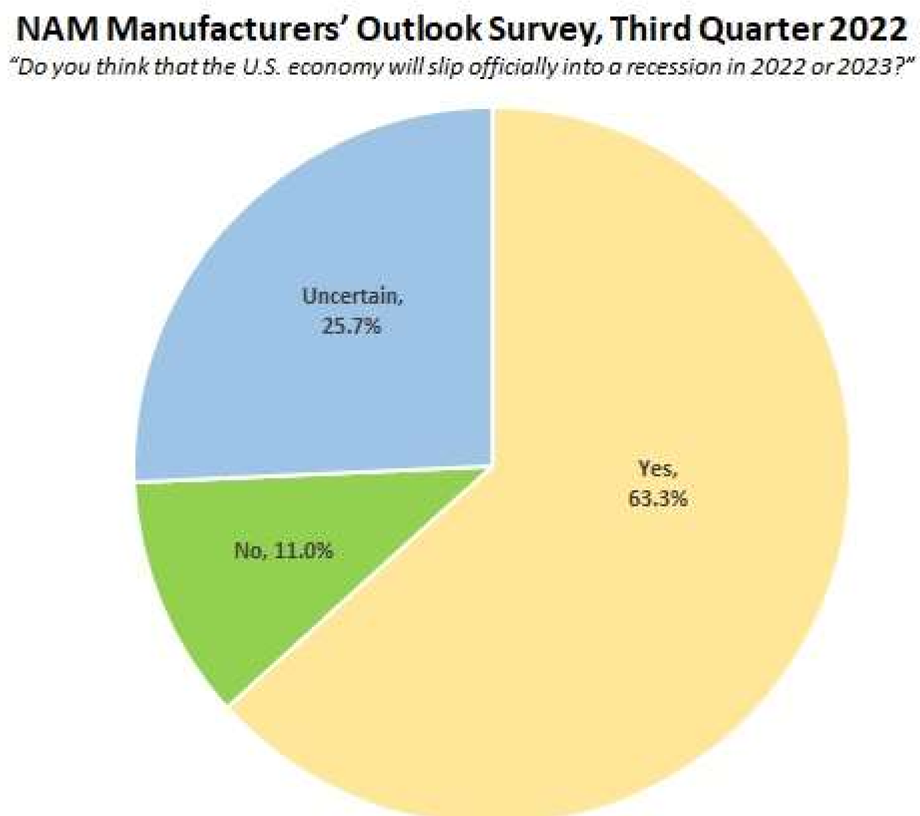
- It also predicts another 25-basis-point increase in early 2023 before holding, with the federal funds rate not declining until 2024. This would suggest a very aggressive stance on the part of the Federal Reserve and a strong statement of the FOMC's intentions to tackle inflation at any cost. With that said, future monetary policy actions will hinge on incoming data.

- New residential construction activity rebounded, jumping 12.2% in August. The uptick in housing starts in August likely stemmed from a pullback in mortgage rates from July highs, stimulating more activity in the housing market. With that said, the average 30-

year fixed-rate mortgage was 6.29% last week (the highest since Oct. 30, 2008), suggesting that new residential construction activity will weaken again in upcoming data.

- Single-family housing starts have plummeted 14.6% over the past 12 months, and builder sentiment was negative for the second straight month in September on affordability issues. Along those lines, new housing permits—which are a proxy of future residential construction—fell 10.0% in August to the lowest level since June 2020.

- Existing home sales inched down 0.4% to 4.80 million units at the annual rate in August, declining for the seventh straight month to the slowest pace since June 2020. On a year-over-year basis, existing home sales plummeted 19.9% from 5.99 million units in August 2021.



Economic Indicators

Last Week's Indicators:
(Summaries Appear Below)

Monday, Sept. 19
NAHB Housing Market Index
NAM Manufacturers' Outlook Survey

Tuesday, Sept. 20

This Week's Indicators:

Monday, Sept. 26
Chicago Fed National Activity Index
Dallas Fed Manufacturing Survey

Tuesday, Sept. 27
Conference Board Consumer Confidence

Housing Starts and Permits

Wednesday, Sept. 21
Existing Home Sales
FOMC Monetary Policy Statement

Thursday, Sept. 22
Conference Board Leading Indicators
Kansas City Fed Manufacturing Survey
Weekly Initial Unemployment Claims

Friday, Sept. 23
S&P Global Flash U.S. Manufacturing PMI

Durable Goods Orders and Shipments
New Home Sales
Richmond Fed Manufacturing Survey

Wednesday, Sept. 28
International Trade in Goods (Preliminary)

Thursday, Sept. 29
Gross Domestic Product (Second Revision)
Real GDP by Industry
Weekly Initial Unemployment Claims

Friday, Sept. 30
Personal Consumption Expenditures Deflator
Personal Income and Spending
University of Michigan Consumer Sentiment (Revision)

Deeper Dive

- **Conference Board Leading Indicators:** The Leading Economic Index decreased 0.3% in August, falling for the sixth straight month. Over the past six months, the LEI declined 2.7%, suggesting weaker growth over the coming months as firms grapple with supply chain, workforce and inflationary challenges and renewed economic uncertainties. The release notes that this is a reversal from the 1.7% gain in the prior six-month period, and the data suggest a higher risk of recession. Meanwhile, the Coincident Economic Index edged up 0.1% in August, slowing from the 0.5% gain in July. The CEI increased just 0.6% over the past six months.

- **Existing Home Sales:** Existing home sales inched down 0.4% from 4.82 million units at the annual rate in July to 4.80 million units in August, declining for the seventh straight month to the slowest pace since June 2020, according to the National Association of Realtors. Affordability has become a big challenge for potential homebuyers, with soaring costs and higher mortgage rates dampening demand. In August, existing home sales weakened in the Midwest but strengthened in the Northeast and West. Single-family sales decreased 0.9% from 4.32 million units to 4.28 million units, but condominium and co-op sales rose 4.0% from 500,000 units to 520,000 units. On a year-over-year basis, existing home sales plummeted 19.9% from 5.99 million units in August 2021.

  There were 3.2 months of unsold inventory of existing homes for sale on the market in August, the same pace as in July and trending higher after hitting a record low of 1.6 months in January. For perspective, there were 3.9, 3.1 and 2.3 months of supply on average in 2019, 2020 and 2021, respectively. The median sales price was $389,500 in August, up 7.7% over the past year.

- **FOMC Monetary Policy Statement:** The Federal Open Market Committee has increased the federal funds rate by 75 basis points, as expected, to 3.00% to 3.25%. In making this decision, the Federal Reserve stated, “Inflation remains elevated, reflecting supply and demand imbalances related to the pandemic, higher food and energy prices, and broader price pressures.” At the same time, the Federal Reserve noted strength in the labor market, with "modest growth in spending and production."

In the economic projections that were also released, FOMC participants suggested that the federal funds target rate could increase to 4.25% to 4.50% by year's end. This would seem to imply another 75-basis-point hike at the Nov. 1–2 meeting, followed by a 50-basis-point increase at its Dec. 13–14 meeting. It also predicts another 25-basis-point increase in early 2023 before holding, with the federal funds rate not declining until 2024. This would suggest a very aggressive stance on the part of the Federal Reserve and a strong statement of the FOMC's intentions to tackle inflation at any cost. With that said, future monetary policy actions will hinge on incoming data.

The Federal Reserve expects real GDP growth of just 0.2% in 2022, down sharply from an estimate of 1.7% growth in its June forecast. It also sees the U.S. economy expanding 1.2% and 1.7% in 2023 and 2024, respectively. The unemployment rate is anticipated to rise to 3.8% later this year, rising to 4.4% in both 2023 and 2024. On the inflation front, the core PCE inflation should moderate to 4.5% by year's end and to 3.1% and 2.3% in 2023 and 2024, respectively.

In addition to increases in the federal funds rate, the FOMC will continue to reduce the size of its balance sheet, which had ballooned to nearly $9 trillion before starting to ease. Starting in June, the Federal Reserve has reduced its holdings of Treasury securities by up to $30 billion each month and of mortgage-backed securities by up to $17.5 billion each month. As of this meeting, the FOMC stepped up those reductions to $60 billion and $35 billion each month, respectively.

- **Housing Starts and Permits**: New residential construction activity rebounded, jumping 12.2% in August after falling 10.9% in July. There were 1,575,000 new housing starts at the annual rate in August, returning to the level in June. Single-family housing starts rose 3.4% from 904,000 units in July, the slowest pace since June 2020, to 935,000 units in August. At the same time, multifamily activity, which can be highly volatile from month to month, soared 28.0% from 500,000 units to 640,000 units. On a year-over-year basis, new housing starts edged down 0.1% from 1,576,000 units in August 2021, but with single-family construction activity plummeting 14.6% over the past 12 months.

  The uptick in housing starts in August likely stemmed from a pullback in mortgage rates from July highs, stimulating more activity in the housing market. With that said, the average 30-year fixed-rate mortgage was 6.29% last week, suggesting that new residential construction activity will weaken again in upcoming data. Indeed, builder sentiment was negative for the second straight month in September on affordability issues, according to the National Association of Home Builders. (See below.)

  Along those lines, new housing permits—which are a proxy for future residential construction—fell 10.0% from an annualized 1,685,000 units in July to 1,517,000 units in August, the lowest reading since June 2020. Single-family permits declined 3.5% from 932,000 units to 899,000 units, also a 26-month low. Likewise, multifamily activity decreased 17.9% from 753,000 units to 618,000 units. On a year-over-year basis, housing permits have dropped 10.0% from 1,772,000 units in August 2021, with single-family permits declining 15.3% over the past 12 months from 1,061,000 units one year ago.

- **Kansas City Fed Manufacturing Survey**: Manufacturing activity expanded at the slowest pace since July 2020 in the Kansas City Federal Reserve Bank's district, with the composite index declining from 3 in August to 1 in September. New orders contracted for the fourth straight month, with exports also negative once again. Production and the average employee workweek rebounded in September, and shipments stabilized. Hiring growth was unchanged. The index for raw material costs rose from 38 to 41, with elevated growth in input prices despite decelerating from faster paces earlier in the year. Manufacturers cited soaring costs, supply chain issues and workforce challenges in their comments.

Manufacturers in the district felt less positive about growth over the next six months, with the forward-looking composite index edging down from 10 to 9, the weakest reading since June 2020. Expectations for new orders, production, shipments, employment and capital expenditures eased in September. Manufacturers expected exports to decline slightly moving forward, likely a reaction to slowing global growth, with that measure turning negative for the first time in 25 months.

- **NAHB Housing Market Index:** Homebuilders were negative in their assessments of the housing market for the second consecutive month, with the Housing Market Index declining from 49 in August to 46 in September, according to the NAHB and Wells Fargo. It was the lowest value since May 2020. Readings below 50 are consistent with more builders being negative than positive in their views of the housing market. Indeed, residential activity has weakened dramatically year to date, with higher mortgage rates and affordability being top of mind for builders and potential homebuyers. With mortgage rates exceeding 6% for the first time since November 2008, NAHB Chief Economist Robert Dietz said that the “housing recession” shows “no sign of abating,” and builders are using incentives to try to stimulate demand.

  Beyond the headline number, the index of current activity for single-family homes dropped from 57 to 54, and the index for the traffic of potential buyers deteriorated further from 32 to 31. Meanwhile, the index for expected single-family sales in the next six months edged down from 47 to 46. Each were also the weakest readings since May 2020.

- **NAM Manufacturers’ Outlook Survey:** In the Q3 Manufacturers’ Outlook Survey, 75.6% of respondents felt either somewhat or very positive about their company outlook, down from 82.6% in the second quarter. It was the weakest reading since the fourth quarter of 2020, with growth slowing notably across the board. Indeed, sentiment was just marginally above the historical average, which was 75.2%, illustrating just how much manufacturing activity has stalled year to date. Small manufacturers (those with fewer than 50 employees) remained less upbeat in their outlook, with 71.0% positive, than their medium (50 to 499 employees) and large (500 or more employees) manufacturing counterparts.

  In addition, 63.3% of manufacturing leaders believed that the U.S. economy would officially slip into a recession in either 2022 or 2023. Because of worries about slowing U.S. and global economic growth, 34.6% of respondents had reduced their company’s outlook for sales growth, with 31.2% and 27.8% suggesting that their capital spending and hiring plans had also slowed, respectively. At the same time, nearly 40% noted that their outlook had not changed, with 8.5% being uncertain.

  Meanwhile, supply chain challenges topped the list of primary business challenges in the third quarter, cited by 78.3% of respondents. For the fourth straight quarter, those completing the survey were asked when they expect supply chain disruptions to abate. Just 10.8% anticipate these disruptions improving by the end of 2022, with 60.7% expecting some abatement in 2023. As such, more respondents expect supply chain issues to drag on longer than in previous surveys. For instance, in the Q2 survey in June, 53.1% expected supply chain issues would improve in 2023, with 14.6% suggesting that bottlenecks had either already improved or would do so by the end of 2022.

On the list of primary business challenges, attracting and retaining a quality workforce (76.1%), increased raw material costs (76.1%) and transportation and logistics costs (65.9%) were not far behind supply chain challenges as the biggest problems faced by manufacturers. More than 40% of manufacturers felt inflationary pressures were worse today than six months ago, with 53.7% noting that higher prices were making it harder to compete and remain profitable. For firms that have had to raise prices, the top sources of inflation were increased raw material prices (95.2%), freight and transportation costs (85.4%), wages and salaries (81.7%), energy costs (54.4%) and health care and other benefits costs (49.0%). Roughly 21% cited the war in Ukraine and global instability as a source of higher prices, with 16.3% noting production stoppages.

For the past nine quarters, manufacturers were asked about production, employment and capital spending in the current quarter relative to the previous one. This information can be expressed as purchasing managers' indices. The data were consistent with notably slower—but still decent—growth in manufacturing activity in the third quarter relative to the second quarter. For instance, the percentage reporting higher production decelerated from 51.1% in the second quarter to 36.8% in the third quarter, with those citing declining output rising from 12.8% to 20.9%. More than 42% stated that production had not changed in the third quarter, up from 36.2% in the previous survey. There were similar trends for employment and capital spending.

- **S&P Global Flash U.S. Manufacturing PMI:** The S&P Global Flash U.S. Manufacturing PMI ticked slightly higher, up from 51.5 in August, which was a 25-month low, to 51.8 in September. As such, the sector continued to expand, but at a lukewarm pace and with the underlying data mixed. New orders (up from 48.8 to 50.9) rebounded in September, expanding for the first time since May, and hiring (up from 51.1 to 53.4) strengthened. At the same time, output (up from 49.2 to 49.5) stabilized slightly but contracted for the third straight month, and exports (down from 47.2 to 46.5) deteriorated further. The index for future output (down from 66.9 to 66.0) slipped a little in the month but continued to reflect cautious optimism for production growth over the next six months. Raw material costs (down from 68.1 to 64.1) grew in September at the slowest pace since November 2020 but remained highly elevated.

  Meanwhile, the S&P Global Flash Eurozone Manufacturing PMI contracted for the third straight month, declining from 49.6 in August to 48.5 in September, the lowest reading since June 2020. The deterioration of manufacturing activity stems from negative impacts from the Russian invasion of Ukraine and soaring costs, especially for energy. In September, sharp decreases occurred in new orders and exports, resulting in post-pandemic lows for both, with output also weakening. The index for future output dropped from 52.7 to 45.1, the lowest since May 2020 and a sign that manufacturers in the Eurozone are becoming more pessimistic about production over the next six months. On the other hand, employment softened but remained somewhat positive. Input prices continued to be highly elevated, strengthening slightly from the previous month but down from recent highs.

  Manufacturing production also weakened in France and Germany on sharp declines in demand, with each country's sector contracting at paces not seen since May 2020 and June 2020, respectively. Outside the Eurozone, the decline in sentiment improved somewhat in the United Kingdom, but manufacturing activity contracted for the second straight month.

- **Weekly Initial Unemployment Claims:** The week ending Sept. 17 saw 213,000 initial unemployment claims, up from 208,000 for the week ending Sept. 10, which was the lowest since the end of May. In contrast, the week ending Sept. 10 saw 1,379,000 continuing claims, down from 1,401,000 for the week ending Sept. 3 and an eight-week low.

Take Action

- **SHRM Webinar on Compensation in a Tight Labor Market**
  On Thursday, Sept. 29, from 12:00 p.m. to 1:00 p.m. EDT, the Society for Human Resource Management will host a webinar focusing on how companies have competed for talent in a very tight labor market, highlighting the findings of a recent paper from The Manufacturing Institute— the workforce development and education partner of the NAM—and Colonial Life. Manufacturers continue to recount the difficulties they are having with attracting and retaining workers, and compensation practices have needed to adapt. In addition, companies have had to differentiate themselves from other competitors for workers. Speakers include NAM Chief Economist Chad Moutray and Colonial Life's Michelle White McLaughlin and Patrick McCullough. For more information and to register, click here.

- **MFG Day Kickoff Event at SAS Headquarters**
  The NAM and MI are planning to celebrate MFG Day at a kickoff event at SAS headquarters in Cary, North Carolina, on Wednesday, Oct. 5, from 9:30 a.m. to 1:30 p.m. EDT. This live, in-person event will include an executive panel on how technology and analytics are transforming the industry and its workforce, a creators' panel spotlighting the many paths students can take into exciting, high-tech manufacturing careers and interactive exhibits of the latest analytics-driven innovations in manufacturing. If you are interested in attending, click here.

- **Be Part of Manufacturing's Premier Workforce Event**
  The MI invites you to its inaugural Workforce Summit on Oct. 18–20 at the Hyatt Regency in Cincinnati, Ohio, where manufacturers, thought leaders, educators, business association leaders and human resource and workforce development professionals will convene to discuss innovations in workforce development and the future of manufacturing. Click here for more information and to register.

Questions or comments? Email NAM Chief Economist Chad Moutray at cmoutray@nam.org.

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