ISM Manufacturing Index Not Cause For Panic

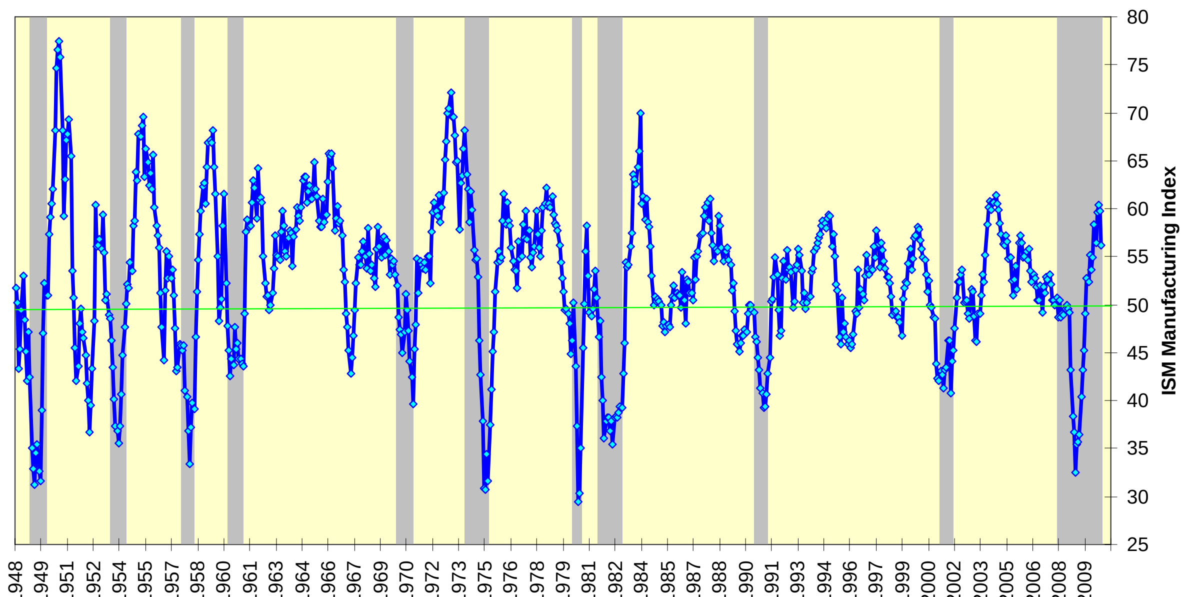
Of all of mankind's urges, the compulsion to be the first to forecast the next recession during an expansion and its anti-twin, the first to forecast a recession's end, surely rank high. They are somewhat similar to those who must be bullish during a selloff and then start calling a market sold on two consecutive hours of price gains. Twitchy, twitchy.

What makes the recent spate of negative economic data so amusing in this context is our good friends at the National Bureau of Economic Research, who only recently confirmed that Constantinople's fall in 1453 has something to do with the Byzantine Empire's otherwise puzzling silence in world affairs, has yet to define an end to the recession it says began in December 2007. Most of us went through 2009 feeling those very special feelings you get when you believe an economic expansion is at-hand. Could this be the first recession to start inside of another recession without ever giving us a proper expansion?

ISM Manufacturing Index

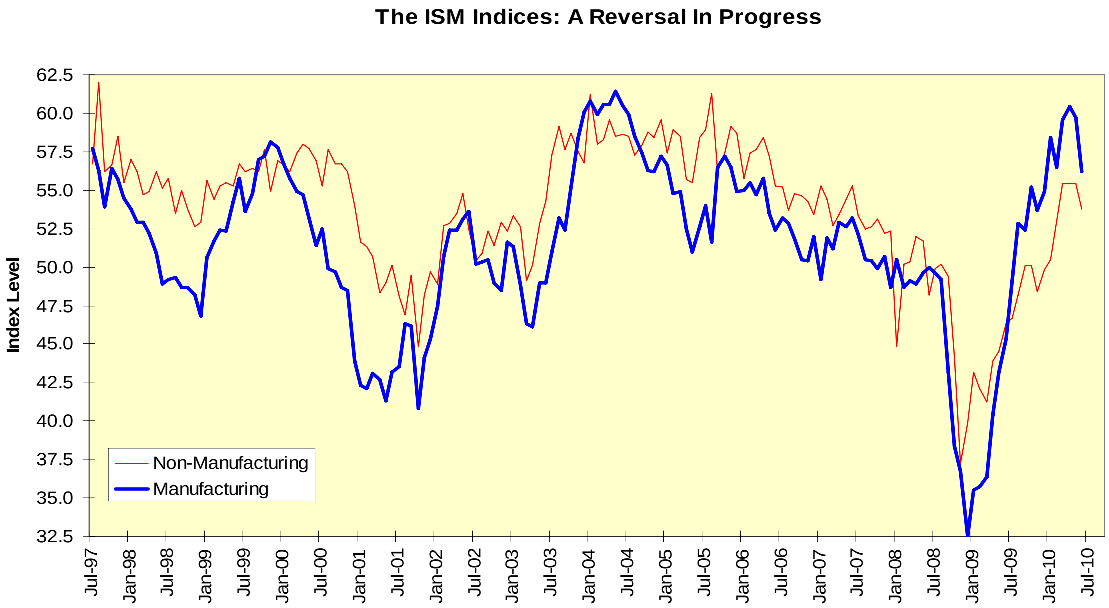
The Institute of Supply Management (they will always be the National Association of Purchasing Managers in my heart) manufacturing index is one of those indicators turning lower at the moment. Should you find a tall building where the windows still open and do the honorable thing? No, if we take this index back to the Truman administration and map its dips and doodles against the NBER's list of recessions, we find the end of a recession is an excellent indicator for an upturn in the ISM index and a downturn in the ISM index often occurs during expansions, most recently from May 2004 to November 2007. As there are five and one-half months left in 2010, your chances of finding something more useful than this index approach 100%.

ISM Manufacturing Index Not Much Of A Recession Predictor



Non-Manufacturing Index

The ISM's non-manufacturing index began in July 1997, and as can be expected for an economy decreasingly dependent on manufacturing, has been out of phase with the manufacturing index. It resisted downturns in the manufacturing index between November 1999 and November 2000, and again between June 2002 and February 2003.



What should we do with this information? First, we can observe the manufacturing index has a large number of V-shaped reversals. A factory can be stopped and restarted far more abruptly than can most service industries, and one of the consequences of vastly improved global supply chain management is a small drop in final demand can rattle through the production sector very quickly. Call it a flash-crash for real stuff. Second, watch developments in credit markets and in the financial services industry more closely than anything involving a punch press, a brake press, a straightening press or a de-burring machine (I have operated them all, thank you very much). Recessions used to be inventory-cycle affairs; now they are bubble-popping affairs. This passes for progress in 21st Century America.

The proverbial bottom line is pay attention to the ISM indices; nothing good will happen if either falls out of bed. However, neither one is going to give you the single one-stop shopping answer to the macro puzzle craved by us all.