



Economics Group

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

Slump Continues for Industrial Production

You can blame warm weather for another drop in utilities, but mining output fell for a fourth straight month and manufacturing output edged lower.

More Than Just a Soft Patch

The 2.0 percent drop in utilities output was broadly expected, and the 0.8 percent drop in mining should also come as little surprise in the context of the steep declines in energy prices. What is more disappointing, in our view, is that manufacturing output declined. This component, which comprises roughly three quarters of all industrial production, has been a stalwart notching modest gains even as other measures have declined. That changed in today's report. Not only did manufacturing slip 0.1 percent in December, last month's slight increase was revised to a scant 0.1 percent decline. Small as these declines might be, on the razor's edge between growth and contraction, even small declines take on additional significance. In a special report earlier this week, we argued that the manufacturing sector, while battered and bruised, is not yet in recession. We are not retracting that call now, but part of our justification just got revised away. Until this report hit the wire, the data affirmed that manufacturing output was growing; now it is not.

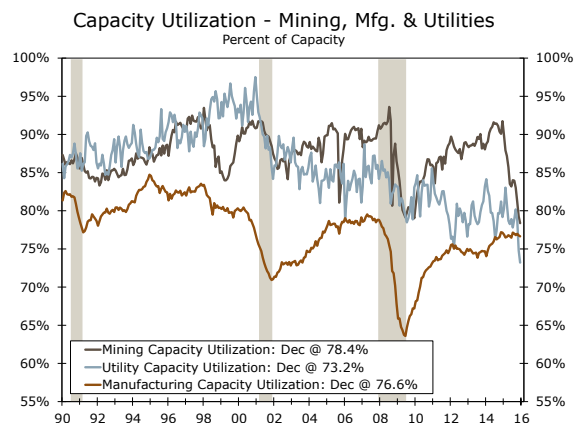
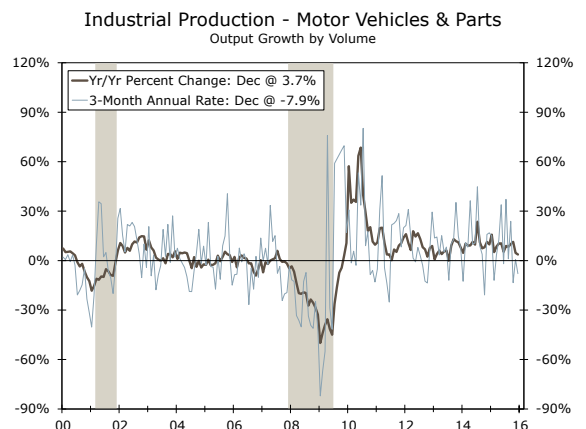
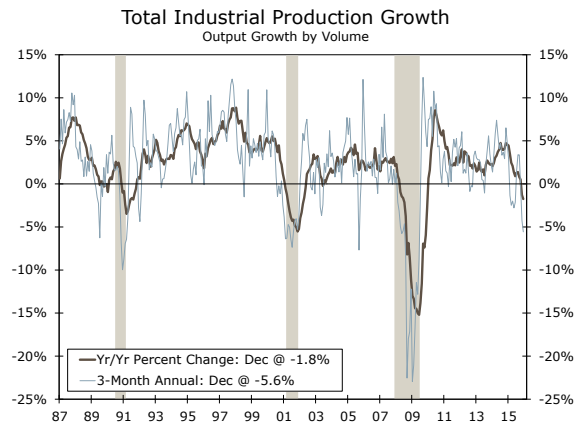
All that said, we are not throwing in the towel yet. A lot of the recent weakness in manufacturing is concentrated in motor vehicle and parts production. After consecutive monthly declines, this category fell at a 7.9 percent annualized rate over the past three months. Stripping away this notoriously volatile category, manufacturing production was up in December and still growing at a 1.3 percent annualized rate. Production of business equipment as well as construction supplies was also positive in December.

An Exceptionally Warm and Soggy Ending to a Warm Year

According to the National Weather Service, it was the warmest and wettest December on record and it put an exclamation point on 2015, which was the second-warmest year on record for the contiguous United States. Not surprisingly, utilities output fell 2.0 percent. This marks the third-straight monthly decline for utilities production, which puts the three-month annualized rate of decline at a stunning 30.1 percent. With utilities production index so low, a return to more seasonal wintry weather would mean this category would become a help rather than a hindrance.

Unused Capacity Makes Job Harder for FOMC

If the Federal Reserve is actually going to deliver on the four rate hikes that are implied in its latest dot-plot forecast, there will need to be some firming in inflation measures. Today's report did not help on that front. Capacity utilization fell in 10 out of the 12 months in 2015 to finish the year at levels last seen in 2013. Granted, a lot of the available capacity is opening up in the mining sector, but utilization in manufacturing and utilities is down as well. During each of the past three Fed tightening cycles, capacity utilization averaged numbers north of 80 percent.



Wells Fargo Securities, LLC 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
Eugenio J. Alemán, Ph.D.	Senior Economist	(704) 410-3273	eugenio.j.aleman@wellsfargo.com
Anika R. Khan	Senior Economist	(704) 410-3271	anika.khan@wellsfargo.com
Azhar Iqbal	Econometrician	(704) 410-3270	azhar.iqbal@wellsfargo.com
Tim Quinlan	Economist	(704) 410-3283	tim.quinlan@wellsfargo.com
Eric Viloría, CFA	Currency Strategist	(212) 214-5637	eric.viloría@wellsfargo.com
Sarah House	Economist	(704) 410-3282	sarah.house@wellsfargo.com
Michael A. Brown	Economist	(704) 410-3278	michael.a.brown@wellsfargo.com
Erik Nelson	Economic Analyst	(704) 410-3267	erik.f.nelson@wellsfargo.com
Alex Moehring	Economic Analyst	(704) 410-3247	alex.v.moehring@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
Donna LaFleur	Executive Assistant	(704) 410-3279	donna.lafleur@wellsfargo.com

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