Daiwa Capital Markets

U.S. Data Review

- ISM nonmanufacturing: noticeable declines in orders, employment, business activity
- International trade: increase in imports in May exceeds advance in exports; wider deficit
- Factory orders: aircraft-led drop in durables; petroleum-led drop in nondurables

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ISM Nonmanufacturing Index

The ISM nonmanufacturing index slipped 1.8 percentage points in June to 55.1 percent, a larger decline than the expected shift of -0.9 percentage point. The new reading trailed by a sizeable margin the average of 58.9 percent in 2018 and it moved to its lowest level since October 2016 (54.4 percent; July 2017 matched the current reading of 55.1 percent).

Only one of the four major components posted an increase in June, and the gain was hardly a sign of strength, as the supplier delivery component moved from a sub-50 percent reading to a still-low 51.5 percent. The other three major components -- new orders, employment, and business activity -- all posted declines of approximately three percentage points. These measures remained comfortably above the critical value of 50 percent (see table), but they all were noticeably below observations in late 2018 or early 2019. The shift in new orders was the most disappointing, as the current reading of 55.8 percent was more than five percentage points below the average of 61.3 percent from last year.

ISM Nonmanufacturing -- Monthly Indexes

	Feb-19	Mar-19	Apr-19	May-19	Jun-19
ISM Nonmfg. Composite	59.7	56.1	55.5	56.9	55.1
Business activity	64.7	57.4	59.5	61.2	58.2
New orders	65.2	59.0	58.1	58.6	55.8
Employment	55.2	55.9	53.7	58.1	55.0
Supplier deliveries*	53.5	52.0	50.5	49.5	51.5
Prices	54.4	58.7	55.7	55.4	58.9

** The supplier deliveries index is not seasonally adjusted. The index differs from the other components of the composite measure (business activity, new orders, employment) in interpretation. An index above 50 percent indicates slower deliveries and readings below 50 percent indicate faster deliveries.*

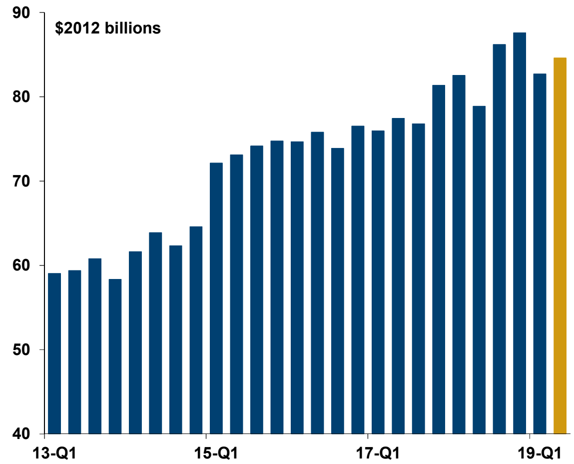
Source: Institute for Supply Management via Haver Analytics

International Trade

Both exports and imports rose in May, but the shift in imports was larger (3.3 percent versus 2.0 percent for exports), and the trade deficit widened as a result (shortfall of $55.5 billion versus $51.2 billion in April, revised from $50.8 billion). Analysts were looking for slippage in the deficit, but the deterioration of $4.3 billion was more pronounced than the expected widening of $3.2 billion.

The picture for trade in goods after adjusting for price changes was largely the same as shifts in nominal values noted above: both exports and imports rose, with the larger change in imports leading to a wider deficit. Results for real goods trade so far in the second quarter show a wider deficit than in Q1, suggesting a drag from net exports on GDP growth (chart; next page, left). If results for June were to match the average for April and May, net exports would subtract approximately one-half percentage point from GDP growth.

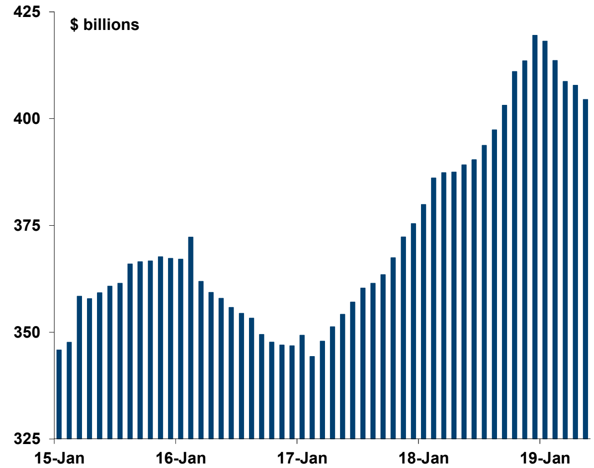
Real Goods Trade Deficit*



* Quarterly averages of monthly data. The reading for 2019-Q2 is the average of results for April and May.

Source: Bureau of Economic Analysis via Haver Analytics; Daiwa Capital Markets America

U.S. Trade Deficit with China*



* U.S. merchandise trade deficit with China. 12-month moving totals of not-seasonally-adjusted data.

Source: Bureau of Economic Analysis via Haver Analytics

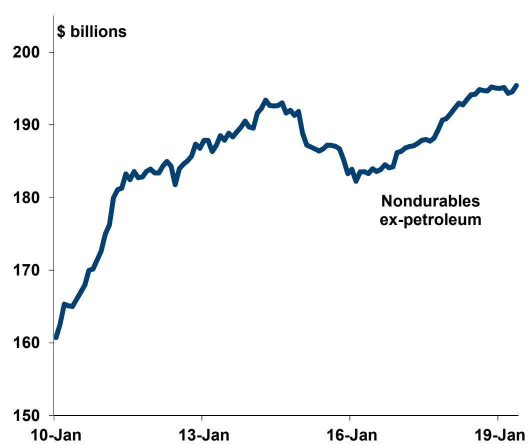
Trade with China merits close attention because of the tensions that have emerged. Both exports and imports have moved lower in recent months, with exports showing the larger change in percentage terms. The 12-month moving total of exports is down 18.8 percent from its peak in July of last year, while imports are off 4.7 percent from their peak in October. (We use 12-month moving totals to remove seasonal variation in these not seasonally adjusted figures.) Given the large difference in the value of exports and imports, these percent changes translate to a larger decline in imports in dollar terms and a slight narrowing in the trade deficit. The 12-month shortfall in the goods deficit narrowed from $419.5 billion last December to $404.5 billion in May (chart, above right).

Factory Orders

The report on factory orders was about in line with expectations (off 0.7 percent versus a consensus estimate of -0.6 percent), although close inspection shows some mildly favorable surprises. The already reported change in durable orders was unrevised at -1.3 percent, but it was adjusted slightly higher (less negative) if calculated with more precision (-1.262 percent versus -1.349 percent). In addition, about half of the revision occurred in nondefense capital goods excluding aircraft, mildly encouraging for capital spending (although this series is still tilting downward). The drop in durable orders in May was concentrated in the aircraft component, not surprising given the problems at Boeing. Excluding transportation, durable orders rose 0.4 percent, revised from an initial estimate of 0.3 percent published last week.

Orders for nondurable goods fell 0.2 percent, softer than the implied expectation of no change. However, a decline of 2.4 percent in orders for petroleum and coal products dominated the retreat, and this drop was at least partially the result of lower prices. Nondurable orders excluding petroleum and coal rose 0.4 percent from a slightly upwardly revised reading in April. Nondurable orders excluding petroleum and coal had been moving sideways since last summer, but the new figures showed a slight pickup (chart). The shift was far from strong, but it did inch out of the recent range.

Manufacturers' New Orders*



* Bookings for nondurable goods excluding petroleum and coal products.

Source: U.S. Census Bureau via Haver Analytics