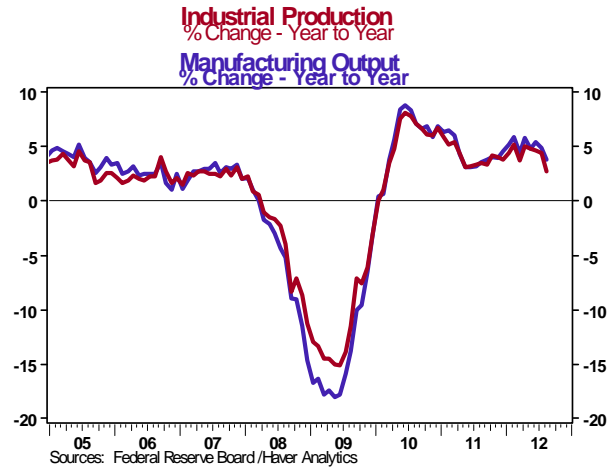


## August Industrial Production / Capacity Utilization

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- Industrial production fell 1.2% in August coming in way below the consensus expected no change. Production is still up 2.8% in the past year.
- Manufacturing, which excludes mining/utilities, declined 0.7% in August (-0.9% including slight downward revisions to prior months). Auto production fell 4.0% in August while non-auto manufacturing slipped 0.4%. Auto production is up 18.5% versus a year ago while non-auto manufacturing is up 2.6%.
- The production of high-tech equipment declined 1.2% in August and is down 1.8% versus a year ago.
- Overall capacity utilization moved down to 78.2% in August from 79.2% in July. Manufacturing capacity use declined to 77.0% in August from 77.7% in July.

**Implications:** Ugly report today on industrial production in August, with output falling 1.2%, the largest monthly decline since the recession. However, there are some extenuating circumstances that suggest a rebound next month. Output at utilities and mines, which are volatile from month to month, declined 3.7% and 1.9%, respectively. Auto production, which is also very volatile, fell 4%, the largest drop in 16 months. Even so, manufacturing outside the auto sector – what we like to follow to reduce “statistical noise” – declined 0.4%. However, it’s not abnormal for even this category of production to decline three or four times a year even during periods of overall economic expansion. Moreover, the Federal Reserve, which generates these data, says Hurricane Isaac temporarily reduced production in the Gulf region. If so, this should generate a rebound in September. Manufacturing remains up 4% from a year ago, including a booming 18.5% in the auto sector and a respectable 2.6% ex-autos. Given relatively low inventories in the auto sector, we expect overall production to bounce back soon. Capacity utilization fell to 78.2%, but still remains higher than the 20 year average of 77.7%. This means companies have an increasing incentive to build out plant and equipment. Meanwhile, corporate profits and cash on the balance sheet show they have the ability to make these investments. The bottom line is that sometimes we have to absorb bad numbers even during economic expansions. The plow horse economy lives on. Today’s data do not signal a recession.



<b>Industrial Production</b> <b>Capacity Utilization</b> <i>All Data Seasonally Adjusted</i>	<b>Aug-12</b>	<b>Jul-12</b>	<b>Jun-12</b>	<b>3-mo % Ch</b> <b>annualized</b>	<b>6-mo % Ch.</b> <b>annualized</b>	<b>Yr to Yr</b> <b>% Change</b>
<b>Industrial Production</b>	<b>-1.2%</b>	0.5%	0.1%	-2.0%	-0.6%	2.8%
<b>Manufacturing</b>	<b>-0.7%</b>	0.3%	0.5%	0.4%	-0.8%	4.0%
<b>Motor Vehicles and Parts</b>	<b>-4.0%</b>	2.7%	1.9%	2.0%	7.3%	18.5%
<b>Ex Motor Vehicles and Parts</b>	<b>-0.4%</b>	0.2%	0.3%	0.4%	-1.7%	2.6%
<b>Mining</b>	<b>-1.9%</b>	1.0%	0.5%	-1.4%	0.2%	3.0%
<b>Utilities</b>	<b>-3.7%</b>	1.3%	-2.7%	-18.8%	3.4%	-4.7%
<b>Business Equipment</b>	<b>-0.2%</b>	0.1%	1.9%	7.6%	7.7%	11.4%
<b>Consumer Goods</b>	<b>-1.3%</b>	0.4%	-0.1%	-3.8%	-1.3%	0.2%
<b>High-Tech Equipment</b>	<b>-1.2%</b>	0.8%	1.0%	2.4%	2.4%	-1.8%
<b>Total Ex. High-Tech Equipment</b>	<b>-1.1%</b>	0.5%	0.1%	-2.1%	-0.6%	3.0%
				<b>3-mo Average</b>	<b>6-mo Average</b>	<b>12-mo Average</b>
<b>Cap Utilization (Total)</b>	<b>78.2</b>	79.2	78.9	78.8	78.8	78.4
<b>Manufacturing</b>	<b>77.0</b>	77.7	77.5	77.4	77.5	77.0

Source: Federal Reserve Board