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December ISM Non-Manufacturing Index

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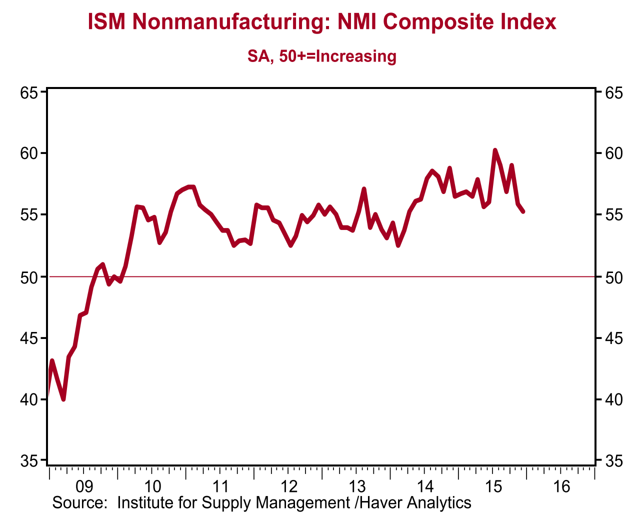
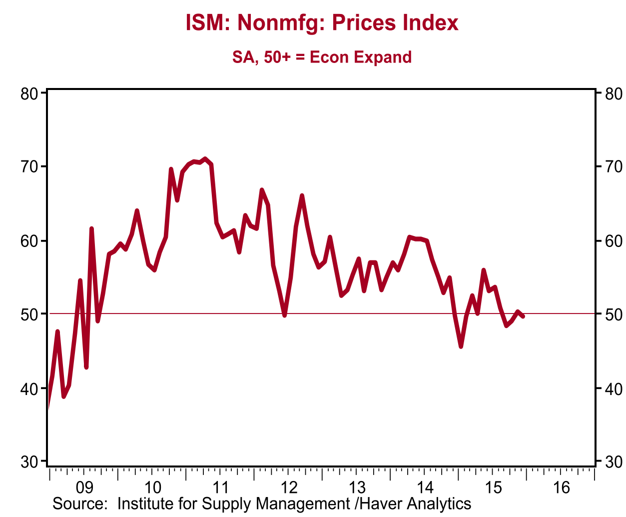
- The ISM non-manufacturing index declined to 55.3 in December from 55.9 in November, coming in below the consensus expected 56.0. (Levels above 50 signal expansion; levels below 50 signal contraction.)
- Despite the decline in the headline number, the major measures of activity were mostly higher in December. The new orders index rose to 58.2 from 57.5 while the employment index moved higher to 55.7 from 55.0 in November. The business activity index increased to 58.7 from 58.2. The supplier deliveries index fell to 48.5 from 53.0.
- The prices paid index fell to 49.7 in December from 50.3 in November.

Implications: Today's report from the Institute for Supply Management shows why looking at the details is so important. While the decline in the headline number represents a slight slowdown in the pace of growth (remember, levels above 50 signal expansion, so Decembers reading represents continued growth, but at a slower rate than in recent months), the underlying details show that activity is rising where it matters most. Both the business activity and new orders indexes, the most forward looking measures in the report, suggest that service sector activity should remain healthy in the coming months. This marks a stark contrast from the manufacturing sector, where recent readings are being compared to 2009. And, as the Fed certainly knows, the service sector represents a much larger portion of the economy. So ignore the calls from the pouting pundits of pessimism suggesting that the manufacturing slowdown is reason to hold off on (or reverse) rate hikes in 2016. Service sector strength continues to move the economy forward, and adds to the reasons we remain positive about 2016. The employment index is also painting a positive picture. Despite some monthly volatility, the average reading of 56.1 in 2015 represents the best annual level since the series began in the late 1990's. On the inflation front, the prices paid index inched back below 50 in December, with respondents reporting that continued declines in energy are leading to reduced costs from vendors. Taken as a whole, today's reports shows why the Fed was comfortable raising rates in December (after manufacturing began showing declines), and why Fed Vice Chairman Stanley Fischer, just this morning, suggested that the Fed's dot plot projection of four rate hikes in 2016 still looks "in the ballpark". That's above the two 25 basis point rate hikes the market is currently pricing in, but total hikes of 100 basis points in 2016 sounds about right to us.





Non-Manufacturing ISM Index *Seasonally Adjusted Unless Noted*	Dec-15	Nov-15	Oct-15	3-month *moving avg*	6-month *moving avg*	Year-ago *level*
Composite Index	**55.3**	55.9	59.1	56.8	57.8	56.5
Business Activity	**58.7**	58.2	63.0	60.0	61.5	58.6
New Orders	**58.2**	57.5	62.0	59.2	60.3	59.2
Employment	**55.7**	55.0	59.2	56.6	57.3	55.7
Supplier Deliveries (NSA)	**48.5**	53.0	52.0	51.2	51.9	52.5
Prices	**49.7**	50.3	49.1	49.7	50.3	49.8

Source: Institute for Supply Management