Economic Analysis

Industrial Production Continues to Disappoint

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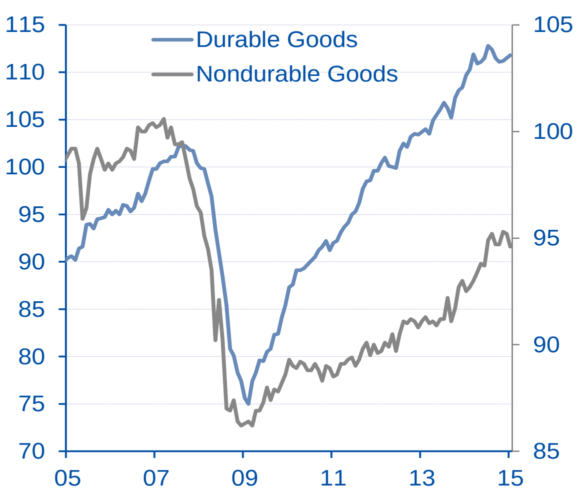
- **Total industrial production declined 0.2% MoM in May following a 0.5% drop in April**
- **Manufacturing declined 0.2% MoM, but auto production held strong**
- **Mining dropped for the fifth consecutive month alongside ongoing sector weakness**

In May, the industrial production reading was negative for the fourth time in six months. Declining 0.2% MoM, May's reading was well below expectations, and offers little relief after the weak first quarter. In fact, 2015 thus far has been far weaker than any other year in the recovery. Industrial production has failed to increase in the last six months, and April's industrial production reading was revised down to -0.5% MoM from an initial -0.3% MoM. Capacity utilization fell to 78.1%–its lowest level since January 2014. This continuing softness is a testament to weak global demand and the strong U.S. dollar which appear to be stifling output, particularly in the manufacturing sector.

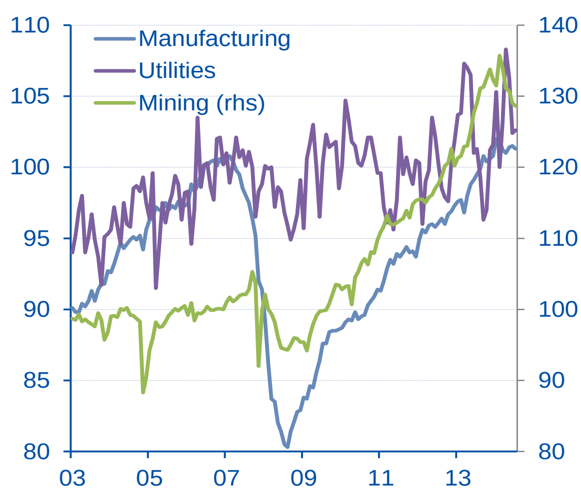
Manufacturing and mining were the hardest-hit components of industrial production, falling 0.2% MoM and 0.3% MoM, respectively. Manufacturing's decline was largely due to the strong dollar, which especially impacted consumer goods and construction supplies. Auto production was the shining star of the manufacturing component, rising 1.7% MoM, backing up May's strong auto sales report indicating greater consumer demand. Mining dropped for the fifth consecutive month, but weakness in the sector could be easing as this month's MoM decline was the smallest since the beginning of the year. Mining's weak output was primarily in oil and gas well drilling and servicing, while crude oil extraction actually increased. After two large consecutive declines, utility output was slightly up, rising 0.2% MoM.

Chart 1
Manufacturing Production
SA, 2007=100



Source: BBVA Research & FRB

Chart 2
Industrial Production Components
SA, 2007=100



Source: BBVA Research & FRB

Although recent retail sales and employment reports could warrant expectations for a stronger 2015, May's decline in industrial production does nothing to inflate those hopes. Our expectation for a later increase in the Fed funds rate is substantiated by this release. However, the eventual increase in rates could be detrimental to U.S. producers, as they compete against companies in Europe and Asia whose central banks continue offering low interest rates. Nevertheless, given strong consumption and hiring, we continue to expect a pick-up in the upcoming months, and do not intend to revise down our GDP forecast based solely on this negative report.