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February ISM Manufacturing Index: Solid Follow-Through As New Threats Emerge

- › The ISM Manufacturing Index fell to 52.4 percent in February from 52.6 percent in January
- › The new orders index fell to 55.8 percent, the production index fell to 55.8 percent, and the employment index rose to 48.8 percent

When the ISM Manufacturing Index jumped to 52.6 percent in January from 47.9 percent in December, handily beating expectations, many were quick to dismiss that as little more than start-of-the year "window dressing," such as firms placing orders to help shore up inventories, as opposed to there having been any meaningful improvement in conditions in the manufacturing sector. We took the other side of that argument, as the details of the ISM's January survey firmly supported the jump in the headline index, and we noted that the jump in January put the ISM index in line with other indicators such as the S&P Global Manufacturing PMI and the monthly data on core capital goods orders. That said, we did expect some payback in the ISM's February survey, at least in part due to what would be less favorable seasonal adjustment. As it turns out, there was less payback, particularly in the new orders index, than we anticipated. So, while the headline index fell to 52.4 percent in February, that modest dip was less pronounced than what we and the consensus expected. Moreover, as was the case in January, the details of the February survey are firmly supportive of the headline index. We have for months been pointing to strong and increasingly broad based growth in orders for core capital goods which, combined with firms not necessarily liking but at least learning to navigate the trade policy landscape and firming growth abroad was, in our view, brightening the outlook for the manufacturing sector. While by no means were we projecting rip roaring growth, we did at least think the ISM Manufacturing Index would hold above the 50.0 break between contraction and expansion over coming months. That said, ongoing developments in the Middle East, which have led to rapid increases in energy prices and threats to global shipping channels, pose new hurdles for the manufacturing sector. It is far too soon to be able to draw any meaningful conclusions as to the ultimate impacts, but it does seem that the manufacturing sector is set to face these newly emerging challenges with momentum on its side.

Twelve of the eighteen broad industry groups included in the ISM survey reported growth in February, the most in any month since June 2022, while five reported contraction. Additionally, comments from survey respondents relayed by ISM are more mixed than had been the case over the prior several months when the tone had been overwhelmingly

negative. While some respondents continue to point to the adverse effects of tariffs, others point to improving demand and growing backlogs of unfilled orders. Cost pressures, in part from higher tariff rates, are commonly cited, consistent with the jump in the prices paid index.

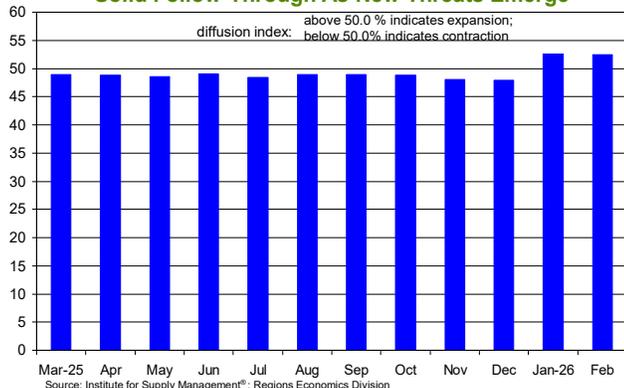
The index of new orders slipped to 55.8 percent in February from 57.1 percent in January, besting our forecast of 53.8 percent. As noted above, we did expect some payback from January, when the new orders index came in higher than at any time since February 2022, but there was less payback than we anticipated. Twelve of the eighteen broad industry groups reported growth in new orders in January, the most since June 2022. Moreover, ISM notes that for every negative panelist comment on new orders, there were two positive comments about near-term demand, which was also the case in January, and the firm level details show a pronounced decline in the percentage of firms reporting lower orders since the end of 2025. The production index slipped to 53.5 percent from 55.9 percent in January, with nine of the eighteen broad industry groups reporting higher output and four reporting lower output. The employment index remained below the 50.0 percent break but nonetheless rose to 48.8 percent from 48.1 percent in January.

After January saw the first incidence of rising order backlogs since September 2022, order backlogs grew further in February, with eleven of the eighteen broad industry groups reported higher backlogs. Though slowing supplier delivery times would seem to align with the premise of rising demand and increasing levels of manufacturing activity, it is unclear whether, or to what extent, unusually harsh winter weather impaired deliveries as ISM offers no comments along these lines. Either way, rising new orders, growing order backlogs, and firms continuing to assess customer inventory levels as being too low should be supportive of employment and output growth in the months ahead.

One troubling element of the February survey is the jump in the prices paid index, which rose to 70.5 percent, the highest reading since June 2022. While higher steel and aluminum prices continue to infiltrate the supply chain, price increases have become much more broadly based, which is clear in the firm level splits. This is consistent with our argument that there is further to run for goods price inflation.



Solid Follow-Through As New Threats Emerge



Firmer Order Books In Line With Other Indicators

