



BUSINESS OUTLOOK SURVEY

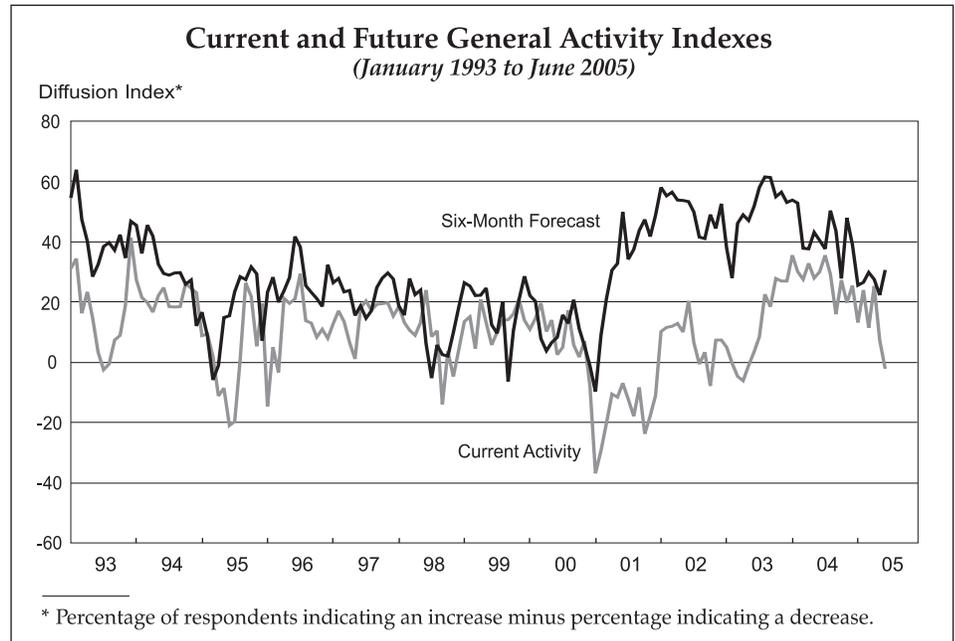
June 2005

Activity in the region's manufacturing sector weakened in June, according to firms surveyed for this month's *Business Outlook Survey*. This represents a decline from the moderate performance in May. Indexes for general activity, new orders, and shipments fell from their readings in May, and most indicators have weakened over the past two months. Firms continued to report a rise in prices for inputs and for their finished goods, although the survey's price indexes fell again this month. Overall employment was reported slightly higher, and average work hours also improved. Despite the weakness in current conditions, expectations for growth over the next six months improved somewhat this month.

Conditions Weaken This Month

The diffusion index of current activity, the broadest measure of manufacturing conditions, fell from 7.3 in May to -2.2 this month. This is the index's first negative reading in 25 months (see Chart). The portion of firms reporting decreases in activity (21 percent) was slightly greater than the portion reporting increases (19 percent). The current new orders index fell 13 points this month, and the shipments index fell eight points. Both indexes remained positive but suggest little or no growth in June. Indicators for unfilled orders and delivery times were negative and provide corroborating evidence of weakness: the unfilled orders index fell 19 points, and the delivery times index fell 14 points.

Despite the weakening in broad indicators, the survey's employment index was slightly higher this month. The current employment index rose from 5.4 in May (the lowest reading since November 2004) to 7.1 this month. More firms reported higher employment than lower (18 percent versus 11 percent); 71 percent reported no change.



Price Pressures Moderate Again

Although firms continue to report higher production costs, the index for input prices fell notably this month. The diffusion index for prices paid declined from 30.9 in May to 23.5. The index has generally trended down since its high reading of 66.1 in January and is now at its lowest point in 21 months.

Firms continued to report higher prices for their own manufactured goods, though price increases were less widespread (17 percent reported higher prices; 9 percent reported lower prices). The diffusion index for prices received fell eight points and is now at its lowest reading in 18 months.

Outlook Remains Favorable

Despite the weakness in current activity, expectations for future growth improved this month. The index for future activity increased from 22.3 in May to 30.6, its highest reading in six months (see Chart). The portion of firms anticipating improve-

ment in business conditions over the next six months (47 percent) continues to exceed the portion expecting deterioration (16 percent) by a significant margin. Other future indicators improved. The future new orders index increased 19 points, and the future shipments index rose 16 points. The future employment index also increased notably, from 7.0 in May to 21.4 this month. The future workweek index paralleled the increase in the future employment index. The future capital spending index edged up four points.

In special questions this month, firms were asked about their expectations for spending on new plant and equipment over the next six to 12 months, relative to actual spending during the past six to 12 months (see Special Questions). Nearly 40 percent of the firms indicated that they plan to increase spending; 13 percent said they planned a decrease. There was a slight decline in the percentage of firms expect-

ing increases compared to January when the same question was posed to the survey participants. The most frequently cited reasons for planned increases in spending were expected sales growth, the need to replace capital goods, and a high current capacity utilization rate.

Firms were also asked about their anticipated employment increases in the same six- to 12-month period. Forty-three percent of the firms expect increases over that period, and 11 percent expect decreases. Nearly 22 percent of firms expect an increase of up to 3 percent, and about 14 percent of the firms expect increases of between 4 and 6 percent. About 8 percent said they expect employment increases of more than 7 percent.

Summary

Overall manufacturing conditions in the region weakened this month, as indicators of current performance fell from their May readings. Indexes for general activity, new orders, and shipments dropped to their lowest readings in two years and suggest little or no growth for the month. Firms continued to report higher prices for inputs and their own manufactured goods, but the survey's price indicators fell again this month. Although current conditions were reported weaker this month, manufacturers were more optimistic about growth in manufacturing over the next six months.

Special Questions (June 2005)

1. Do you expect your firm's spending on new plant and equipment over the next 6 to 12 months to increase, decrease, or remain more or less unchanged relative to your actual spending over the past 6 to 12 months?

	June 2005 (%)	January 2005 (%)	January 2004 (%)
Increase	39.8	43.8	58.2
Decrease	13.3	15.7	12.7
No Change	47.0	40.4	29.1

2. What are the major factors behind your plan to increase capital spending? (Top five chosen)*

	June 2005 (%)
Expected growth of sales is high	58.8
Need to replace non-IT capital goods	44.1
Capacity utilization is currently high	35.3
Firm's cash flow or balance sheet position has improved	26.5
Need to replace information technology (IT) equipment	23.5

3. What are the major factors behind your plans not to increase capital spending? (Top five chosen)*

	June 2005 (%)
Limited need to replace non-IT capital goods	38.3
Expected growth of sales is low	27.7
Capacity utilization is currently low	27.7
Limited need to replace information technology (IT) equipment	23.4
Firm's cash flow or balance sheet position has not improved	17.0

4. What percentage change in employment is anticipated over the next six to 12 months?

	%	%	%	%	
Increase of 0-3%	21.5	Decrease of 0-3%	5.1		
Increase of 4-6%	13.9	Decrease of 4-6%	0.0		
Increase of 7-9%	6.3	Decrease of 7-9%	2.5		
Increase of 10% or more	1.3	Decrease of 10% or more	3.8		
Stay at current levels	45.6	Total Increase	43.0	Total Decrease	11.4

*Percentages may add to greater than 100 because firms were asked to indicate more than one factor if applicable.

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Summary of Returns

June 2005

	Previous Diffusion Index	June vs. May			Diffusion Index	Previous Diffusion Index	Six Months from Now vs. June			Diffusion Index
		Increase	No Change	Decrease			Increase	No Change	Decrease	
What is your evaluation of the level of general business activity?	7.3	18.8	58.0	21.0	-2.2	22.3	46.5	34.2	16.0	30.6
Company Business Indicators										
New Orders	15.0	28.0	43.8	25.5	2.5	16.1	49.7	31.9	14.7	35.0
Shipments	14.9	29.4	47.7	22.8	6.6	20.0	50.3	32.5	14.2	36.1
Unfilled Orders	-0.1	7.2	60.7	26.2	-19.0	-7.1	18.2	63.1	15.4	2.9
Delivery Times	0.5	1.9	83.0	15.1	-13.2	-6.2	9.0	73.3	13.9	-4.9
Inventories	2.0	21.1	54.4	21.5	-0.4	-12.5	19.5	50.3	28.1	-8.7
Prices Paid	30.9	31.9	59.7	8.4	23.5	32.5	38.6	50.4	9.4	29.2
Prices Received	15.7	17.3	73.5	9.2	8.1	16.5	32.4	57.7	6.0	26.5
Number of Employees	5.4	18.0	71.0	10.9	7.1	7.0	30.5	57.0	9.1	21.4
Average Employee Workweek	-2.8	18.6	66.3	14.2	4.4	3.5	22.4	66.7	7.3	15.1
Capital Expenditures	—	—	—	—	—	15.7	27.1	43.5	7.1	19.9

Notes:

- (1) Items may not add up to 100 percent because of omission by respondents.
- (2) All data are seasonally adjusted.
- (3) Diffusion indexes represent the percentage indicating an increase minus the percentage indicating a decrease.
- (4) Survey results reflect data received through June 14, 2005.