Leading Economic Indicator Increases; Not Yet Cause for Celebration

The American Chemistry Council (ACC) recently released its monthly Chemical Activity Barometer (CAB) [1], a leading economic indicator derived from a composite index of chemical industry activity. The September CAB showed a 0.3 percent growth over the previous month. This represents the third consecutive monthly increase in the CAB, and follows small upward revisions for the previous three months.

“While it is encouraging to see three consecutive months of gains, this is not yet cause for celebration. Rather, what we’re seeing is that the CAB is signaling sub-par economic growth into 2013 as the economy continues to face strong headwinds and concerns around the fiscal cliff crystalize,” said Dr. Kevin Swift, chief economist at the American Chemistry Council.

“Interestingly, we are seeing this year’s economy repeat the pattern of 2010 and 2011. At ACC, we’ve compared this situation to the old Charlie Brown comic strip where Lucy holds the football for Charlie but at the last moment as he goes to kick it, she removes it. Just as the first quarter discussion about economic recovery is finally gaining traction, the proverbial football -- the recovery -- disappears, hence the ‘Charlie Brown’ effect.”

According to Swift, September’s uptick in growth, after three consecutive months of sub-par growth, reveal a trend also witnessed in both 2010 and 2011, where the ACC observed a strong upswing in the fourth quarter of the year, a gradual slowing of growth in the first quarter, followed by consecutive declining months into the third quarter.

The chemical industry's early position in the supply chain uniquely positions the CAB against other economic indicators. The CAB provides a long lead for business cycle peaks and troughs and can help identify emerging trends in the wider U.S. economy within sectors closely linked to the business of chemistry such as housing, retail and automobiles. Applying the CAB back to 1947, it has been shown to lead the National Bureau of Economic Research (NBER), by two to 14 months, with an average lead of eight months. NBER is the organization that provides the official start and end dates for recessions in the U.S.

There were mixed trends in some areas of the September CAB data, with production related indicators mostly positive. In particular, further gains in construction-related plastic resins, coatings, pigments and other chemistry suggest the housing market recovery continues, as reflected in last week's announcement about housing starts rising 2.3 percent in August. Other components were less positive with product and input prices stable and U.S. exports continuing to slow.

The Chemical Activity Barometer is a monthly index developed by the economics department at the American Chemistry Council. The chemical industry has been found to consistently lead the U.S. economy's business cycle given its early position in the supply chain, and this barometer can be used to determine turning points and likely trends in the wider economy.

The CAB's three-month moving average (3 MMA) increased in September, suggesting steady but slow growth prospects in the months ahead. The June, July and August CAB was revised upward from last month's report, June by 0.1 percent, and 0.2 percent for both July and August.

Of its key indicators, production-related indicators, chemical company equities and production grew while inventories and prices remained flat. Other conclusions over the past three-month moving average basis and how this compares to September 2011:

Chemical Activity Barometer for the Latest Six Months and Year-Ago Month

	Sep-11	Apr-12	May-12	Jun-12	Jul-12	Aug-12	Sep-12
CAB	**88.3**	**90.0**	**89.4**	**88.9**	**89.2**	**89.6**	**89.9**
% M/M	-0.2	-0.3	-0.7	-0.6	0.3	0.4	0.3
% Y/Y	1.1	-0.1	-0.3	-0.4	-0.6	1.2	1.8
CAB (3MMA)	**88.8**	**90.0**	**89.9**	**89.4**	**89.2**	**89.2**	

							89.6
% M/M	-0.4	0.1	-0.1	-0.5	-0.6	-0.6	-0.6
% Y/Y	2.4	-0.2	-0.3	-0.3	-0.4	0.1	0.8

*Percentage changes may not reflect index values due to rounding.

During September, the various components of the CAB:

Production	**?**
Chemical Company Equities	**?**
Prices	**?**
Inventories	**?**

Where **?** is continued growing activity; **?** is flat or insignificant growth in activity; and **?** is slowing or negative growth (declining activity).

The CAB comprises indicators relating to the production of chlorine and other alkalies, pigments, plastic resins and other selected basic industrial chemicals; chemical company stock data; hours worked in chemicals; publicly sourced, chemical price information; end-use (or customer) industry sales-to-inventories; and several broader leading economic measures (building permits and new orders). Each month, ACC provides a barometer number, which reflects activity data for the current month, as well as a three-month moving average. Month-to-month movements can be volatile so a three-month moving average of the barometer is provided. This provides a more consistent and illustrative picture of national economic trends.

Applying the CAB back to 1947, it has been shown to provide a longer lead (or perform better) than the National Bureau of Economic Research, by two to 14 months, with an average lead of eight months. The median lead was also eight months. At business cycle troughs, the CAB leads by one to seven months, with an average lead of three months. The median lead was also three months. The CAB is rebased to the average lead (in months) of an average 100 in the base year (the year 2007 was used) of a reference time series. The latter is the Federal Reserve’s

Industrial Production Index.

The chemistry industry is one of the largest industries in the United States, generating $760 billion. The manufacturing sector is the largest consumer of chemical products, and 96 percent of manufactured goods are touched by chemistry.

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