



Economics Group

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Factory Orders Nearly Offset April's Decline

Factory orders climbed 0.8 percent in May, nearly offsetting April's upwardly revised 0.9 percent decline. Manufacturing orders appear to be bouncing back following the Japan earthquake and tsunami shock.

Factory Orders Imply Manufacturing Soft Patch is Temporary

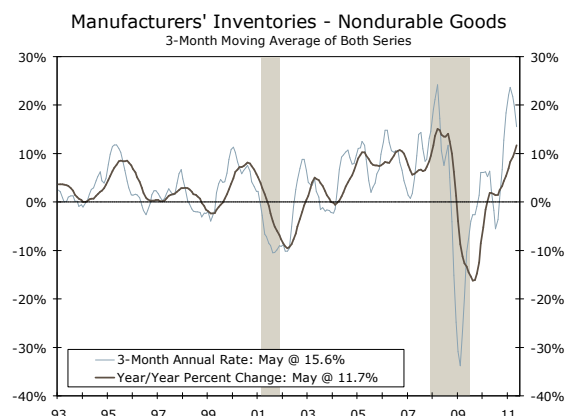
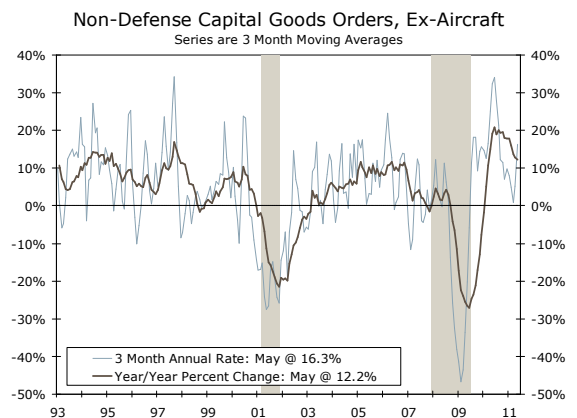
U.S. factory orders returned to growth in May, rising 0.8 percent, following April's upwardly revised 0.9 percent decline. The headline gain was slightly below consensus expectations calling for a 1.0 percent gain, though the previous month's decline was revised up three tenths of a percentage point. Despite recent weakness in regional manufacturing surveys, the ISM manufacturing index for June rebounded, and the May factory orders report suggests that U.S. manufacturing will soon return to a more stable growth trajectory as the transitory impacts of the Japanese tsunami and earthquake fade and auto and aircraft orders rebound. Year-over-year gains in factory orders remain at a solid 13.3 percent. Nondefense capital goods orders excluding aircraft, a better proxy for future business equipment and software spending, jumped 1.6 percent in May, more than reversing April's 0.4 percent decline. Durable goods orders for May were also revised higher than the initial release two weeks ago, rising a healthy 2.1 percent.

Inventory Growth Slows and Shipments Rise

Factory inventories increased 0.8 percent in May, a marked deceleration from April's 1.5 percent increase. Nondurable good inventories, in particular, are moving back toward trend. This should help reduce the need for manufacturers to scale back aggressively in production capacity and employment in the months ahead. However, shipments growth remained sluggish, rising just 0.1 percent in May following April's 0.4 percent decline. As a result, the factory inventory-to-shipments ratio rose to 1.34 months. This ratio, while higher than in the past few months, is still around levels seen as recently as last fall. There is no sign yet that manufacturers will need to throw production into reverse to stabilize inventories, especially if shipments recover in the months ahead. Unfilled orders climbed 0.9 percent in May, a stronger gain than in April when unfilled orders increased only 0.6 percent—another signal that the U.S. manufacturing expansion, while sluggish of late, is not yet dead.

Where's the Growth in Orders?

We are seeing a factory orders rebound over the last three months in a broad cross-section of industries, with particular strength in primary metals, machinery, transportation and furniture. Defense, fabricated metals and computers and electronic orders have been weak, and in some cases contracting, but even in these sectors orders appear to be bottoming out. These indicators provide more evidence that the summer soft patch in U.S. manufacturing is more likely to turn into a manufacturing rebound in the second half of the year than it is likely to be followed by an ever greater manufacturing decline.



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