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Economics Group

Tim Quinlan, Economist
tim.quinlan@wellsfargo.com • (704) 410-3283
Sarah Watt, Economist
sarah.watt@wellsfargo.com • (704) 410-3282

Durable Goods Orders Boosted by Aircraft and Defense

In a mixed bag report, durable goods orders surged for a third straight month in June even as non-transport orders stalled. Core capital goods orders increased by the smallest amount since February.

Great Headline Gain, Only an OK Report Otherwise

The 4.2 percent gain in June comes on the heels of a 5.2 percent monthly increase in May and lifted the dollar value of durable goods to a new record high, cresting above the pre-recession peak hit in December 2007. All other qualifications aside, this is a significant milestone for the recovery in American manufacturing. The last time the notoriously volatile headline number posted three consecutive monthly gains was almost four years ago in the autumn of 2009. The overall level of orders at that point had just plumbed its low point for the recession a few months earlier in the year in June 2009. This turn in the business cycle set up a low base for comparatively "easy" gains that fall.

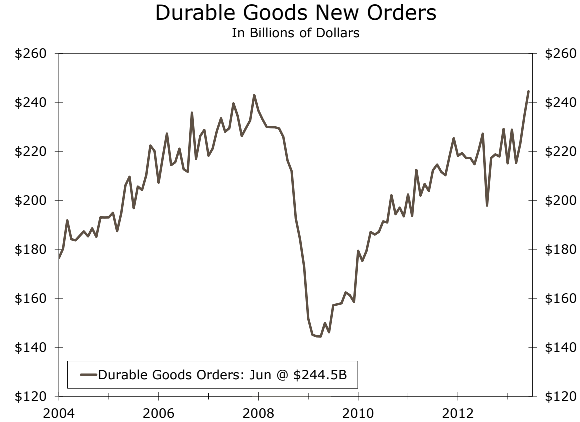
Having acknowledged the positives, the gain in today's report does not reflect a broadly-based advance for the factory sector. Rather, it was primarily a function of increased military spending (up 35.2 percent) and new civilian aircraft orders (up 31.4 percent). A number of other areas that are important to business spending showed either tepid gains like the 0.1 percent increase in fabricated metals, or outright declines like the 1.8 percent drop in electrical equipment or the 2.6 percent decrease in computers and electronics orders.

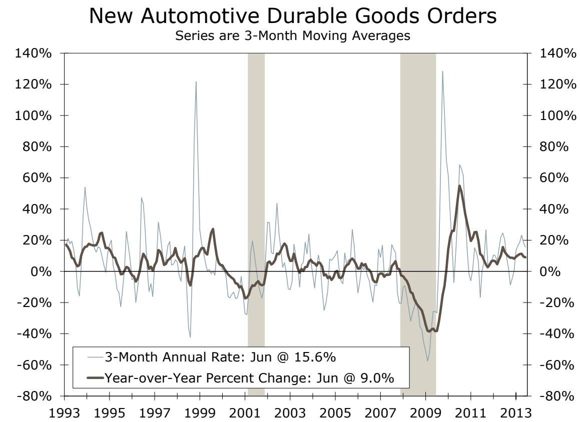
After a 0.8 percent drop in May, its only decline in 2013, auto sales more than bounced back in June, increasing 1.3 percent on the month. Unfortunately, when you strip away the effect of aircraft, autos and other bookings for transportation, orders were essentially unchanged in June.

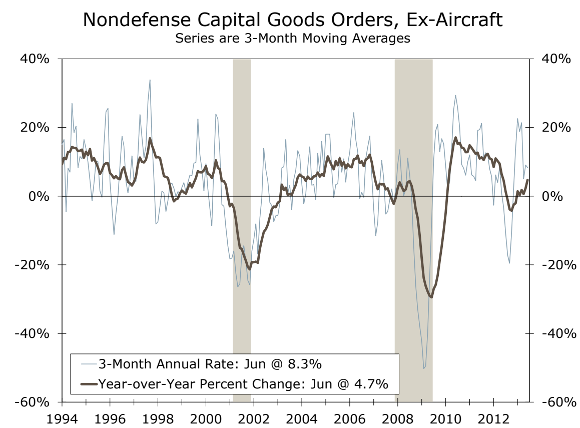
Turn and Face the Strange

Nondefense capital goods orders, ex-aircraft was once our favorite measure for business spending because shipments of that series fed into the official GDP numbers. But with its second quarter release later this month, the Bureau of Economic Analysis is shaking up its calculation for business spending. Although we are not kicking core capital goods to the curb, it will be just one in a number of factors that will shape the outlook for business spending. For more on the changes coming to GDP see our Business Spending Midyear Outlook.

The various purchasing manager surveys around the country have been firming in recent months, but still offer a split decision on the level of activity in the factory sector, specifically, and in business confidence generally. The July reading from the Richmond Fed was negative, but the respective measures from the Federal Reserve branches in New York and Philadelphia both signaled expansion in July. We are somewhat less apprehensive about the outlook for the factory sector than we have been in recent months. Continued improvement in the PMIs will improve our conviction.







Source: U.S. Department of Commerce and Wells Fargo Securities, LLC

Wells Fargo Securities, LLC Economics Group

Diane Schumaker-Krieg	Global Head of Research, Economics & Strategy	(704) 410-1801 (212) 214-5070	diane.schumaker@wellsfargo.com
John E. Silvia, Ph.D.	Chief Economist	(704) 410-3275	john.silvia@wellsfargo.com
Mark Vitner	Senior Economist	(704) 410-3277	mark.vitner@wellsfargo.com
Jay Bryson, Ph.D.	Global Economist	(704) 410-3274	jay.bryson@wellsfargo.com
Sam Bullard	Senior Economist	(704) 410-3280	sam.bullard@wellsfargo.com
Nick Bennenbroek	Currency Strategist	(212) 214-5636	nicholas.bennenbroek@wellsfargo.com
Eugenio Aleman, Ph.D.	Senior Economist	(704) 410-3273	eugenio.j.aleman@wellsfargo.com
Anika Khan	Senior Economist	(704) 410-3271	anika.khan@wellsfargo.com
Azhar Iqbal	Econometrician	(704) 410-3270	azhar.iqbal@wellsfargo.com
Tim Quinlan	Economist	(704) 410-3283	tim.quinlan@wellsfargo.com
Michael A. Brown	Economist	(704) 410-3278	michael.a.brown@wellsfargo.com
Sarah Watt	Economist	(704) 410-3282	sarah.watt@wellsfargo.com
Michael T. Wolf	Economist	(704) 410-3286	michael.t.wolf@wellsfargo.com
Sara Silverman	Economic Analyst	(704) 410-3281	sara.silverman@wellsfargo.com
Zachary Griffiths	Economic Analyst	(704) 410-3284	zachary.griffiths@wellsfargo.com
Peg Gavin	Executive Assistant	(704) 410-3279	peg.gavin@wellsfargo.com
Cyndi Burris	Administrative Assistant	(704) 410-3272	cyndi.burris@wellsfargo.com

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