



Economics Group

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Durable Orders Plunge in July

The stark decline in durable goods orders in July was not wholly unexpected as some payback for recent strength in aircraft and defense spending was in order, but underlying details were also disappointing.

Durables Sink on Broad-Based Weakness

Durable goods orders sank 7.3 percent in July, which was a more substantial decline than markets anticipated. Some payback was to be expected after orders posted impressive gains of more than three percent in each of the previous three months. The most volatile components of the report had been leading the recent surge. Between April and June, nondefense aircraft orders and defense orders were up 124 percent and 58 percent, respectively. Boeing already reported nearly a 70 percent drop in the number of aircraft orders, so today's 52 percent decline in the value of nondefense aircraft orders came as little surprise. Defense orders also corrected from the recent run of gains, declining 22 percent.

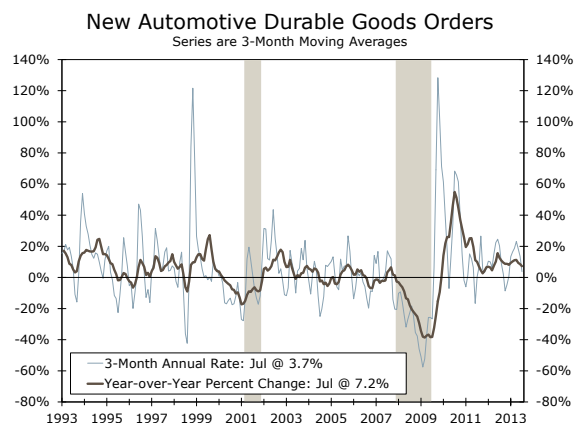
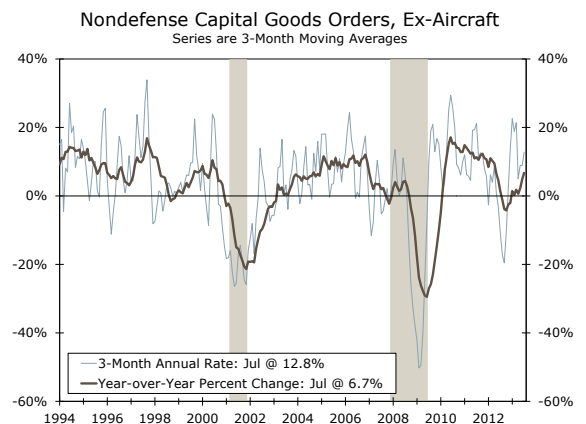
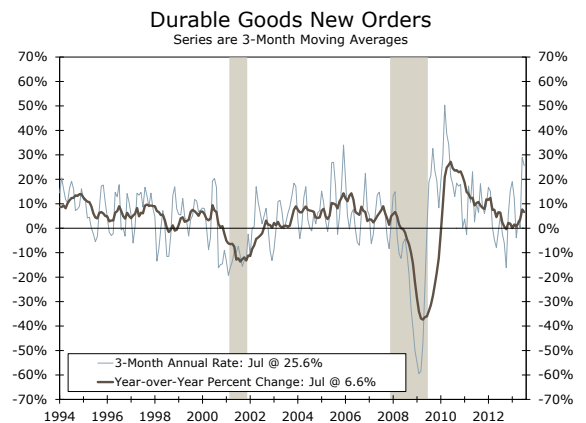
Markets were expecting an ugly headline number, but the details of this report made it more unpleasant. Excluding transportation, orders fell 0.6 percent versus an expected gain of 0.5 percent. Weakness was widespread across sub-sectors, with orders for computers and electronics and electrical equipment falling and orders for machinery and primary metals flat. Orders for vehicles and parts offset some weakness, rising 0.5 percent, but are well off the pace seen earlier in the year, as auto sales and production have cooled over the past couple of months. Core capital goods orders, which exclude aircraft and defense orders, also disappointed, slipping 3.3 percent. This bucks the trend of fairly solid gains over the past four months. Even after today's drop, however, core orders are up 9.1 percent over the past year, suggesting factory activity is not completely falling off the rails.

Capital Spending Getting Off to a Rough Start in Q3

The shipments data, which have a more immediate bearing on growth, shows the current pace of activity in the factory sector remains lackluster. Total shipments fell 0.3 percent, while core capital goods shipments fell 1.5 percent. This slowdown looks to have led to some unintended inventory building; inventories rose 0.4 percent – the most since February.

Manufacturing Sector Still Set for Modest Pick Up

Despite today's drop in orders, our outlook for a modest pickup in manufacturing activity remains unchanged. While the pace of growth in the United States was rather weak in the first half of the year, we expect a slight acceleration in the coming months, which should support better capital investment. In addition, conditions in the global economy are stabilizing, with the Eurozone economy no longer contracting and recent reads on the Chinese economy looking a bit firmer. The latest purchasing managers' indexes point toward activity in the manufacturing sector continuing to expand in August, although at a slightly slower rate. Reads on new orders moderated in the most recent Markit, Empire and Philly Fed indexes, although the Kansas City Fed survey reported some strengthening.



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