



## Economics Group

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### Durable Goods Orders Disappoint

*The 0.1 percent increase in durable goods orders for August comes on the heels of an even larger drop than was first reported in the prior month. Core capital goods orders were also weaker than expected.*

#### Where is the Strength in the Factory Sector?

The initially reported decline of 7.3 percent in July was revised to an even larger drop of 8.1 percent. After a plunge of that magnitude, some bounce-back might be expected, but durable goods orders barely budged, increasing a scant 0.1 percent in August. Given the recent indications of improving activity we have seen in the various regional PMIs and even in the national ISM index, which has been firmly in expansion territory, this weakness is not only disappointing, it tends to make you second guess the value of the surveys. So what is really going on here?

There were only two major categories that posted declines in orders of more than 3.5 percent in August. Those were defense capital goods, where orders fell 6.5 percent, and defense aircraft, which saw a drop in orders of 11.8 percent. These measures of defense spending are often for big-ticket items and as such are inherently volatile. Having said that, if budget negotiations do not go smoothly this autumn, additional sequestration spending cuts could be a headwind for these categories going forward.

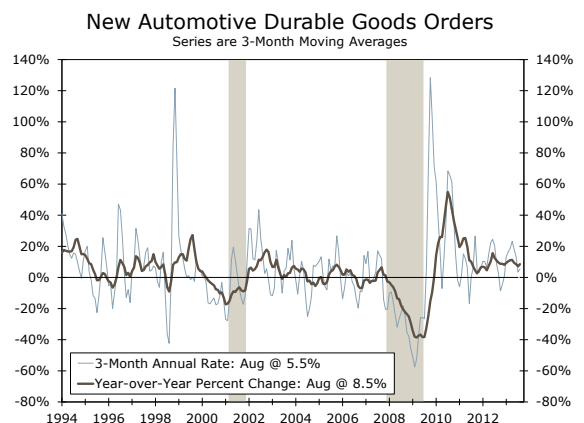
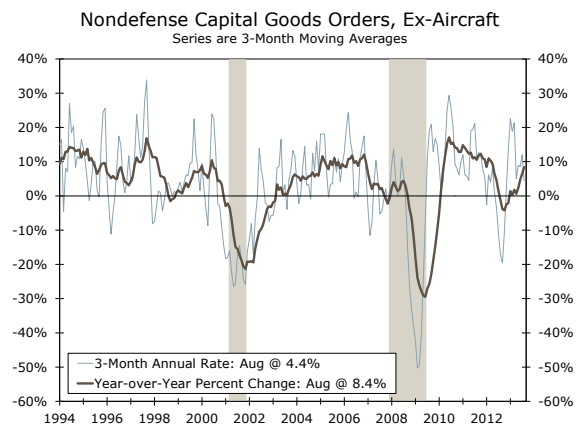
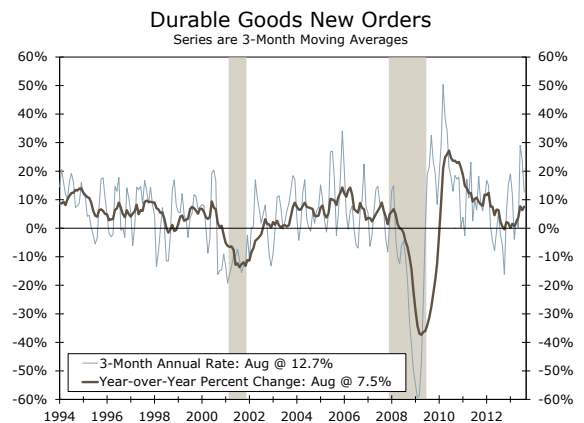
Elsewhere declines were more muted. Computer and electronics products fell 3.4 percent, communications equipment orders fell 1.7 percent and primary metals orders slipped half of one percentage point. Other areas showed outright gains. Fabricated metals orders increased 0.3 percent and machine orders added 0.9 percent. Overall core capital goods orders increased 1.5 percent and while that was not enough to offset last month's decline of 3.3 percent for this series, it is certainly more of a bounce than we saw in the headline.

Not all transportation orders are under pressure. In fact, despite the weakness in defense and civilian aircraft orders, transport orders as a whole rose 0.7 percent in August. This was largely attributable to a 2.4 percent surge in orders for motor vehicles and parts. This report captures sales to dealers, but we know that sales are brisk on dealer lots as well, with total vehicle sales cresting above 16 million in August for the first time since before the recession.

#### Manufacturing Sector Still Set for Modest Pick-Up

The shipments data, which have a more immediate bearing on growth, shows the current pace of activity in the factory sector remains lackluster. The modest gain of 1.3 percent in core capital goods shipments was not enough to offset the 1.4 percent decline in the prior month.

Despite today's drop in orders, our outlook for a modest pickup in manufacturing activity remains intact. Purchasing managers' indexes point toward activity in the manufacturing sector generally continuing to expand in September, although at a slightly slower rate. It also bears noting here that the Richmond Index reported yesterday showed a decline in activity which does not derail our expectations, but does suggest caution.



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