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Economics Group

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Durable Goods Disappoint in December

Durable goods orders ended 2013 much weaker than expected, falling 4.3 percent in December. Ex-transportation, orders also fell, leaving us once again puzzled on the divergence from the ISM index.

Another Head Scratcher

In our last report on durable goods orders, we wrote that November orders "finally closes the gap between lofty survey readings and hard data, which until November had been uninspiring." That gap appears to have widened again. While the ISM manufacturing new orders index improved to a three and a half year high in December, a disappointing report on durable goods leaves us once again wondering which data is painting the true picture of the manufacturing sector. Instead of increasing as markets had expected, durable goods orders fell 4.3 percent in December. To rub salt in the wound, last month's gain was revised down by nearly one percentage point.

There are few positive things to point to in this report. Transportation orders fell not only on a drop in aircraft orders, but on a 5.8 percent decline in vehicles and parts orders. The auto sector has been a bright spot for manufacturing over the past year, but December's drop in orders comes on the heels of weak sales and elevated retail inventories, perhaps causing manufacturers to take pause. Ex-transportation, orders fell 1.6 percent in December. Most major categories saw declines, with a notable exception being machinery products, which are up 13.5 percent over the past year.

Shipments ended the fourth quarter on a weak note, falling 1.9 percent and pushing the inventory to shipments ratio up to 1.67 from 1.62. Over the quarter, however, core capital goods shipments rose at a 6.5 percent annual pace, signaling a decent business spending in the fourth quarter.

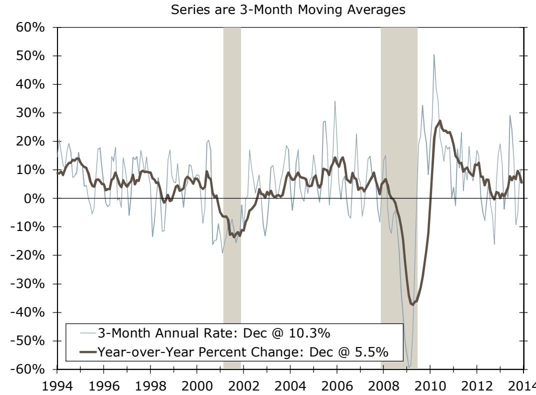
Don't Be So Quick to Ignore Aircraft

Despite Boeing taking in a record number of orders in December, nondefense aircraft orders fell 17.5 percent. The drop seems to stem from seasonal adjustment factors; typically orders rise in December following the Dubai Airshow and indeed, a non-seasonally adjusted orders rose 50 percent in December. However, a sizable share of these orders were for lower value models. Typically we like to exclude aircraft orders due to their monthly volatility and long lead times, but taking a step back from the monthly noise, we see this sector has been a bright spot amid orders for the year. Both orders and shipments of nondefense aircraft outpaced total durable goods for the year, and aircraft shipments are now 21 percent higher than in 2007.

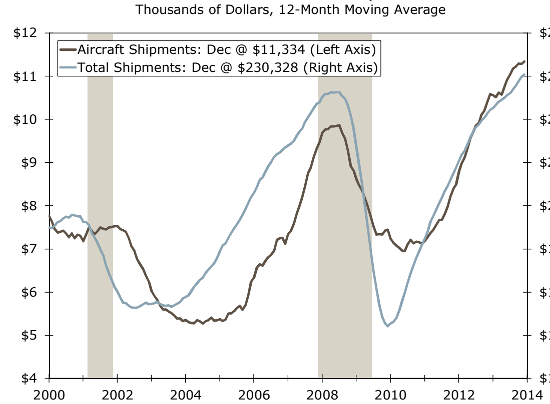
Orders and Shipments Brighter for 2014

With the corporate sector financially strong, credit conditions easing, and economic growth coming closer in line with its long-run trend, we expect business investment to strengthen in 2014. The three-month annualized pace of nondefense capital goods orders ex-aircraft is running at 2.5 percent in December, signaling business investment is set for further gains in the first part of the year.

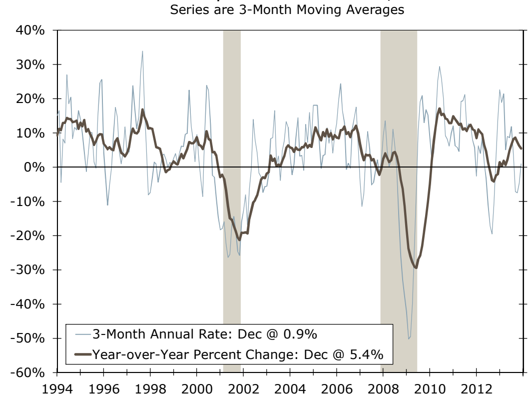
Durable Goods New Orders
Series are 3-Month Moving Averages



Nondefense Aircraft Shipments
Thousands of Dollars, 12-Month Moving Average



Nondefense Capital Goods Orders, Ex-Aircraft
Series are 3-Month Moving Averages



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

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