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Economics Group

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Durable Goods Orders Unexpectedly Fell in September

Durable goods orders fell 1.3 percent month-over-month in September, despite expectations for a modest increase. Weakness for new orders was broad based, but the transportation sector was notably weak.

Transportation Sector Puts on the Brakes

Following two consecutive months of volatile data as a result of huge swings in nondefense aircraft, durable goods orders fell 1.3 percent in September (top chart). This comes as consensus expectations were looking for a 0.5 percent increase. The reading for "core" capital goods orders was a bit more disappointing, posting a 1.7 percent decline despite a relatively firm trend thus far in 2014.

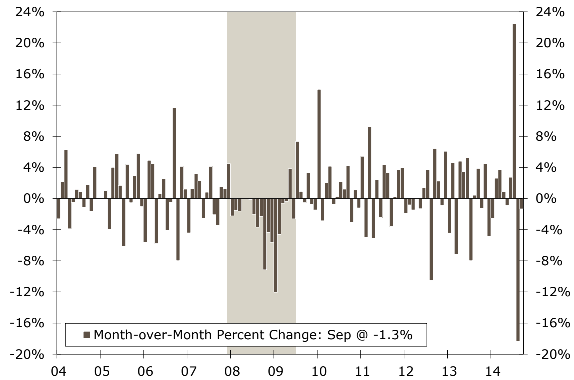
Orders in the transportation sector posted a 3.7 percent decline, but weakness was concentrated in the notoriously volatile nondefense aircraft sector, which fell 16.1 percent. This is a relatively tame movement compared to the wild swings in the previous months, as Boeing orders surged in July and experienced a pullback in August. Vehicles and parts were essentially flat on the month, registering only a 0.1 percent drop. Weakness in September can be attributed to continued troubles abroad, most notably the slowdowns in China and the Eurozone. However, this relatively weak finish to Q3 is no reason to sound the alarm just yet.

If we take a step back and look at Q3 as a whole, a weak September does not derail the positive momentum in the factory sector. Core capital goods orders rose 10.4 percent at an annualized rate in Q3, following a similarly-strong 11.8 percent gain in Q2 (middle chart). Excluding transportation, durable goods orders fell just 0.2 percent, as several sectors actually showed improvement over the month. Primary metals, fabricated metal products and electrical equipment all posted modest improvements, suggesting there are still positive takeaways despite the disappointing headline and "core" readings.

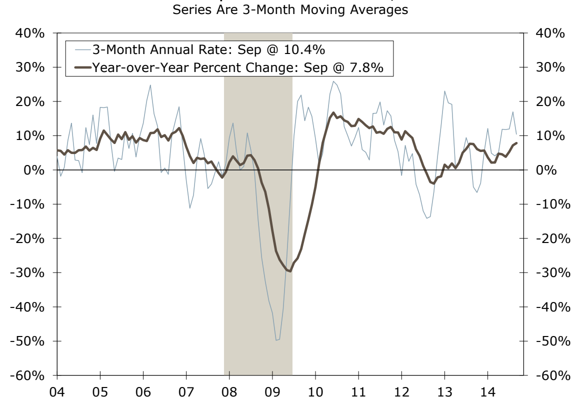
The 0.1 percent gain in total shipments was more encouraging, coming on the heels of the previous month's 1.8 percent decline. While transportation orders disappointed, shipments in this sector were relatively positive, up 0.3 percent, with both vehicles and parts and nondefense aircraft contributing to the gain. In the context of Q3 GDP that will be released later this week, nondefense capex shipments (which are incorporated in the equipment portion of business fixed investment) grew at an annualized rate of 16.8 percent, following just a 6.5 percent pace in Q2. This is consistent with our view for relative strength in equipment spending in the second half of this year, as we look for roughly 7.0 percent annualized growth.

Inventories grew 0.4 percent for the fourth consecutive month as the inventory-to-shipments (I-S) ratio ticked up to 1.65 (bottom chart). Despite recent monthly gains, we still look for inventories to impose a modest drag on Q3 GDP. Unfilled orders were up 0.3 percent, marking the eighth consecutive monthly gain. While today's report was clearly weaker than expected, a look at the underlying details paints a less negative picture as month-to-month volatility is expected.

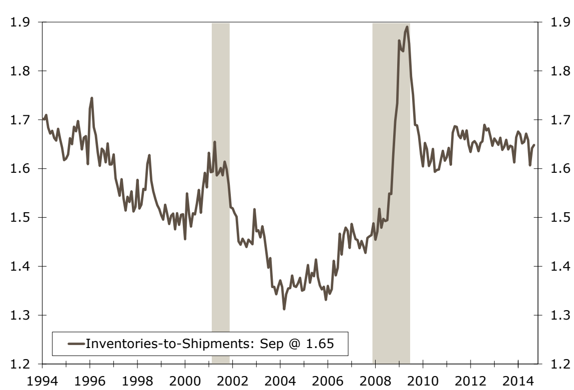
Durable Goods New Orders
Month-over-Month Percent Change



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



Durable Goods Inventories-to-Shipments Ratio



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

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