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Economics Group

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Durable Goods Point to Slow Turnaround in Manufacturing

Durable goods orders declined 1.8 percent in May and orders for April were revised lower. Core capex orders rebounded modestly, but the tepid increase suggests improvement in the factory sector will be slow.

Details Modestly Better Than the Headline

The manufacturing sector has been one of the weak links of the economy this year as the stronger dollar and spillover effects from weaker activity in the energy sector have led to a sharp slowdown in activity at U.S. factories. Today's report on durable goods indicates softness continued in May, even as details were somewhat better than the headline.

Durable goods orders fell 1.8 percent in May, while orders for April are now reported to have contracted 1.5 percent in April compared to an originally reported decline of 0.5 percent. Aircraft orders accounted for a sizeable share of the weakness; Boeing orders fell from 37 in April to 11 in May, leading to a 35 percent decline in the value of new orders after seasonal adjustment. Motor vehicle orders, which have been one of the few bright spots in the manufacturing sector this year (up 8.1 percent year to date), were flat over the month. However, with auto sales climbing to the highest level since 2005 last month, demand for new vehicles looks to remain strong and the upward trend in new orders is likely just on pause.

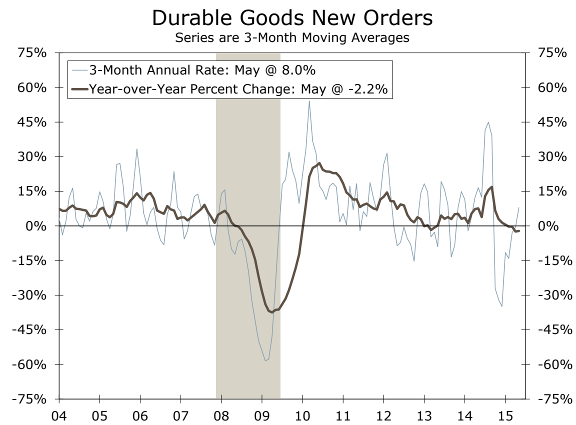
Excluding transportation, orders looked a bit stronger having rebounded 0.5 percent. Computers & electronics led the pickup, increasing 2.2 percent from April and 10.0 percent over the past year. Although orders rose for machinery, primary metals and fabricated metals in May, the toll from weaker energy investment and commodity markets have led to orders remaining below year-ago levels.

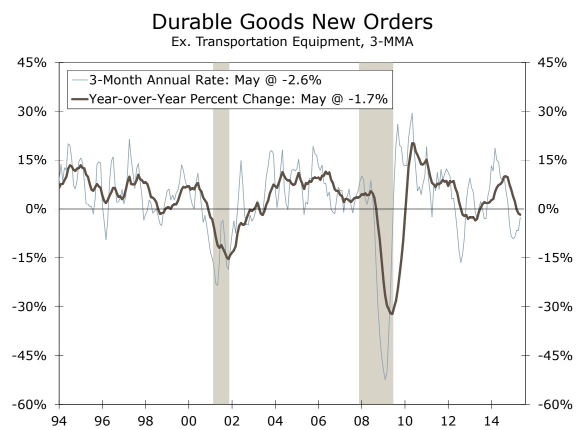
Current activity also remains tepid. Shipments for durable goods orders fell 0.1 percent in May, which marks the fourth decline in five months. However, given weakness early in the first quarter, orders in the first two months of Q2 are up at a 1.4 percent annualized pace compared to Q1.

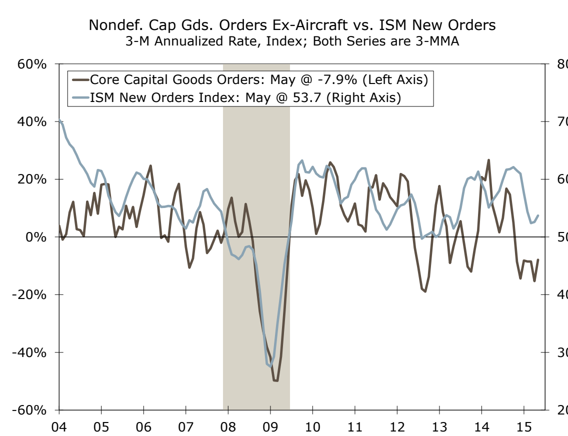
Cautious Outlook on Manufacturing

New orders for capital goods spending excluding defense and aircraft, which we generally consider to be a good guide for future business investment, rose 0.4 percent in May. We are cautious in putting much weight on core capex orders after the head-fake last month; core orders were originally reported up 1.0 percent in April, only to have revisions in the factory orders report one week later show core orders actually contracted 0.3 percent. However, the rebound in May is consistent with improvement in the ISM new orders index, which rose to a five-month high of 55.8 in May.

We are still far from calling the all clear for the manufacturing sector's recent soft patch. The first of the regional June purchasing managers' indices, the Empire and Philly Fed surveys, painted a mixed picture on new orders (contracting in New York, but strengthening in the Philadelphia Fed region). That said, today's increase in core orders offers some modest encouragement from "hard" data that activity is turning around.







Source: U.S. Department of Commerce, Institute for Supply Management and Wells Fargo Securities, LLC

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