Economics

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Economic Indicator — April 26, 2023

Look Past Headline Durables Data, Growth in Core Orders Continues to Slow

Summary

The 3.2% pop in durable goods orders in March was due almost entirely to a surge in aircraft orders. It is private-sector core capital goods orders that matter, which show a continued reversal in demand. Nondefense shipments data suggest some modest downside to Q1 equipment spending, which will print Thursday.

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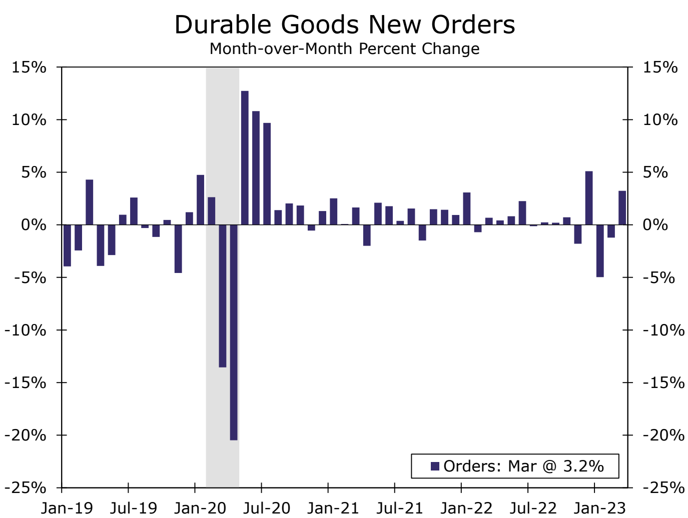


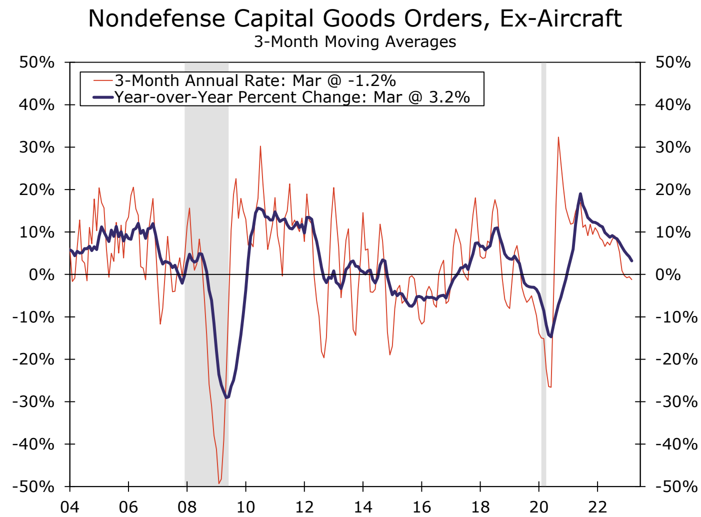
Source: U.S. Department of Commerce and Wells Fargo Economics

Headline Headfake

Look through the headline durable goods data that suggest orders leaped 3.2% in March (chart). The gain last month was due almost entirely to a pop in aircraft orders specifically after weakness in the first two months of the year. It's not unusual to get wide swings in aircraft orders month-to-month, so it's useful to look through this category to gauge the underlying trend in orders. Nondefense aircraft orders popped nearly 80%, and when we exclude the broader transportation category from the data, orders rose just 0.3%.

The trend in private-sector core orders has slowed and suggests the goods sector of the economy still appears to be going through correction as new demand slows amid increased economic uncertainty. Core durable goods orders (excluding defense and aircraft), slid 0.4% in March, marking the fifth decline in seven months (chart).

When we think of the implications for first quarter GDP growth, it is *shipments* or deliveries that matter. Nondefense capital goods shipments popped 3.6% in March, but that comes after some downward revisions to prior months. Nondefense capital goods shipments declined at an 3.3% average annualized pace over the past three months. But in considering higher prices for private capital equipment in Q1, *real* equipment spending was likely a bit weaker. Data on Q1 GDP will print Thursday morning.

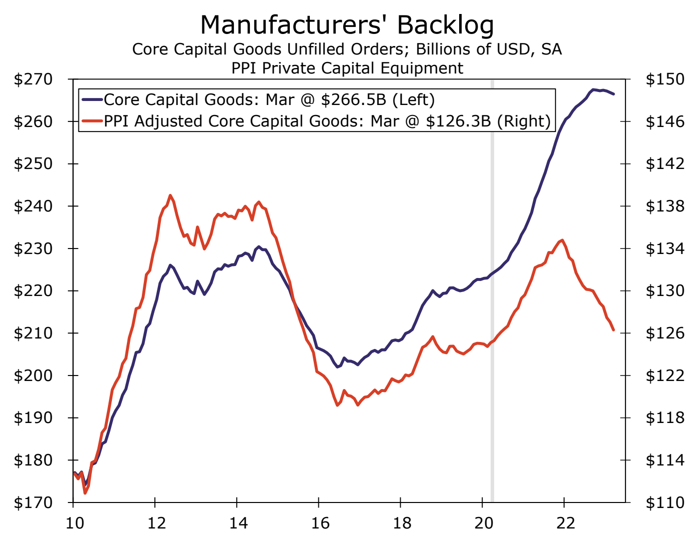


Source: U.S. Department of Commerce and Wells Fargo Economics

Goods Sector Still Signaling Correction

Other industrial data have also been bleak. The ISM manufacturing index has signaled contraction for five consecutive months and manufacturing output has stalled. Conditions for new capital investment continue to grow less favorable and small business plans to make new capital expenditures have rolled over and are approaching new lows.

We continue to anticipate a further tightening in banks' lending standards to take hold, which will further weigh on new investment. Manufacturers' backlog had risen quite quickly during the pandemic and worst of the supply chain crisis. But as supply chains have eased, manufacturers have been able to chip away at backlog as new demand has slowed. Unfilled orders of core capital goods (excluding defense and aircraft) dipped only slightly by 0.1% in March, but the trend in inflation-adjusted backlog has moved markedly lower. As seen in the nearby chart, there is less in the pipeline to help sustain activity going forward. We ultimately expect capex investment to remain under pressure this year as businesses deal with margin compression amid still-high costs and dwindling demand. The result is likely a continued contraction in overall equipment spending growth.



Source: U.S. Department of Commerce, U.S. Department of Labor and Wells Fargo Economics

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