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U.S. Outlook

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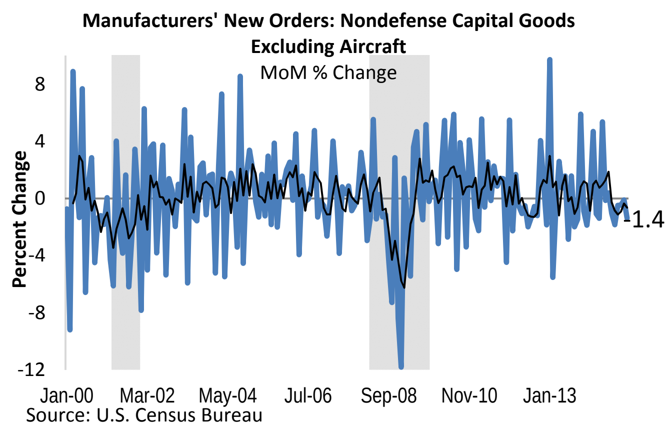
Date	Indicator	For	Estimate	Consensus*	Previous Period
30-March-2015	Personal Income	FEB	0.3%	0.3%	0.3%
30-March-2015	Personal Spending	FEB	0.2%	0.2%	-0.2%
30-March-2015	PCE Deflator	FEB	0.2%	0.2%	-0.5%
30-March-2015	PCE Deflator- Core	FEB	0.1%	0.1%	0.1%
30-March-2015	Pending Home Sales MoM	FEB	0.3%	0.7%	1.7%
30-March-2015	Dallas Fed Manufacturing Index	MAR	-10.0	-9.0	-11.2
31-March-2015	S&P 500/Case-Shiller 20-City Index MoM	JAN	0.8%	0.7%	0.87%
31-March-2015	Chicago PMI	MAR	52.3	52.3	45.8
31-March-2015	Consumer Confidence Index	MAR	97.0	96.6	96.4
1-April-2015	ADP Employment Change	MAR	240K	230K	212K
1-April-2015	Construction Spending MoM	FEB	-0.3%	-0.1%	-1.1%
1-April-2015	ISM Manufacturing	MAR	52.2	52.5	52.9
1-April-2015	Total Vehicle Sales	MAR	16.7M	16.9M	16.16M
2-April-2015	Initial Jobless Claims	03/28	287K	NA	282K
2-April-2015	Trade Balance	FEB	-$42.5B	-$41.3B	-$41.8B
2-April-2015	ISM New York	MAR	NA	NA	63.1
2-April-2015	Factory Orders	FEB	-0.8%	0.5%	-0.2%
3-April-2015	Nonfarm Payrolls- Change	MAR	275K	250K	295K
3-April-2015	Manufacturing Payrolls- Change	MAR	9K	10K	8K
3-April-2015	Unemployment Rate	MAR	5.4%	5.5%	5.5%
3-April-2015	Avg. Hourly Earnings	MAR	0.2%	0.2%	0.1%
3-April-2015	Avg. Weekly Hours	MAR	34.6	34.6	34.6

*Consensus from Bloomberg

What Does the Drop in New Orders Mean?

What's the saying, "Get used to disappointment"? Despite expectations for stabilization, durable goods orders for February remained weaker than expected, dropping another 1.4% on the month. Non-defense capital goods orders, excluding aircraft, often a leading indicator of business investment and industrial production, has dropped now for six consecutive months. This is the longest consecutive monthly decline since September 2012, when orders fell for seven months and culminated in the launch of QE3 at that month's FOMC meeting. Does that mean QE4 is in our near future? Probably not, but it does help explain the FOMC's dovish statement and caution about raising interest rates over the near-term.

Where Did All The Orders Go?



Non-defense capital goods orders, excluding aircraft, jumped 5.4% in one month last June. That makes up for several months of weakness since, but it's clear that durable goods manufacturers may have made some misjudgments about future demand. I see three factors driving this downturn in orders: 1) the rapid strengthening of the U.S. dollar 2) the huge and unexpected plunge in crude oil prices, and 3) the harsh winter weather. The effects of the bad-winter weather are expected to be transitory and should already be fading in March. The impact on manufacturing and business investment from the other drivers is likely to be longer-lasting. The strong dollar is likely the most powerful factor and probably will be the most prolonged of the three. U.S. goods exports are already 3.9 percent lower than a year ago.

Inventory shipment ratios have been on the rise and are now out of whack with current demand. The all-manufacturers inventory to shipments ratio hit 1.4 in January – meaning inventories are higher than normal relative to shipments. This is the highest ratio since the "Great Recession".

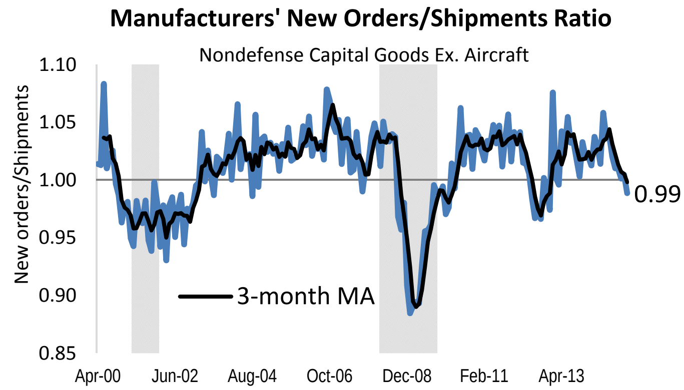
Inventory shipment ratios for computers and electronic products and non-durable apparel manufacturers appear especially high by historical standards, indicating the rise is likely due to an adverse impact from the strong U.S. dollar and weak global demand. The inventory shipment ratio for computers and electronics products hit 1.74 in January, the highest level since August of 2001. Going back to January 1992, we could not find a time when apparel manufacturers' inventory shipments ratio was as high as it was in January at 2.4. This could mean future cuts in production and jobs in these sectors until shipments improve.

Inventory Shipment Ratios On The Rise

Source: Census Bureau

The bad news from the durable goods orders report for February is that new orders are not improving, but continue to deteriorate. The new orders-shipment ratio for non-defense capital goods orders ex. aircraft slipped to 0.99 in February, the lowest reading since the slowdown of 2012 that got the Fed's attention.

New Orders Fall Below Shipments for First Time Since 2012



Source: Census Bureau, BOTW

In short, even if orders pick up from here, it will take several more months before inventories come back in-line with demand, which suggests continued weakness in manufacturing surveys and production in the months ahead.

On the bright-side, a modest manufacturing slowdown or downturn doesn't necessarily lead to out-right recession. Manufacturing employs only 12.3 million people or 8.7% of total nonfarm payrolls of 141.1 million. But there are multiplier effects on the rest of the economy. During the 2012 manufacturing slowdown, industrial production growth slipped from 4.5% (year-on-year) to 2.3% (a 2.2 percentage point decline in growth). Over the same period, real GDP growth fell about 1.1 percentage points from 2.7% to 1.6%.

The U.S. economy has gotten off to another shaky start, much as it did in Q1 of last year. Tracking estimates of the current quarter's real GDP growth are around 1.5 percent annualized. Retail sales, industrial production, and now durable orders have disappointed. We lowered our forecast for business investment and exports in Q1 this week and project slightly slower growth from these sectors in Q2 as well, including industrial production growth. The lingering weakness in this month's durable goods orders and the resulting inventory overhang that has developed will see to that.

Major Economic Indicators

Economic Data	2014.1	2014.2	2014.3	2014.4	2015.1	2015.2	2015.3	2015.4	2016.1	2016.2	2016.3	2016.4	2013	2014	2015	2016
	History				Forecast								Yr/Yr % chg or Annual Avg.			
Real GDP*	-2.1	4.6	5.0	2.2	1.5	2.7	2.9	3.0	2.7	2.8	2.7	2.7	2.2	2.4	2.8	2.8
Personal Consumption Expenditures*	1.2	2.5	3.2	4.2	2.8	3.5	3.5	3.4	3.1	3.1	2.9	2.8	2.4	2.5	3.4	3.2
Non-residential Fixed Investment*	1.6	9.7	8.9	4.8	2.2	2.8	5.0	5.0	4.7	4.6	4.6	4.2	3.0	6.3	4.6	4.7
Private Housing Starts (000s units)	925	985	1,030	1,075	1,010	1,070	1,101	1,133	1,145	1,170	1,230	1,250	930	1,004	1,079	1,199
Vehicle Sales (mill. Units, annualized)	15.6	16.5	16.7	16.8	16.6	17.1	17.2	17.2	17.2	17.2	17.3	17.3	15.5	16.4	17.0	17.2
Industrial Production*	3.9	5.7	4.1	4.3	0.0	2.0	3.3	3.2	3.4	3.4	3.4	3.4	2.9	4.2	2.7	3.3
Nonfarm Payroll Employment (mil.)	137.8	138.6	139.4	140.2	141.1	141.9	142.7	143.6	144.4	145.2	146.0	146.7	136.4	139.0	142.3	145.6
Unemployment rate	6.7	6.2	6.1	5.7	5.5	5.3	5.2	5.1	5.0	5.0	4.9	4.9	7.4	6.2	5.3	5.0
Consumer Price Index* (percent)	2.1	2.4	1.2	-0.9	-3.0	1.7	1.9	1.9	1.9	1.9	2.0	2.1	1.5	1.6	0.1	1.9
"Core" CPI* (percent)	1.8	2.2	1.4	1.5	1.9	1.8	1.8	1.9	1.9	1.9	2.0	2.0	1.8	1.7	1.8	1.9
PPI (finished goods)* (percent)	4.1	3.5	0.4	-5.1	-11.5	0.3	1.0	1.1	1.3	1.3	1.4	1.4	1.2	1.3	0.3	1.8
Trade Weighted Dollar (Fed BOG, major)	76.9	76.4	77.5	82.2	89.3	90.0	90.4	90.7	91.0	91.8	92.5	92.4	76.1	78.3	90.1	91.9
Crude Oil Prices -WTI ($ per barrel)	99	103	98	76	50	50	52	54	62	63	64	65	98	94	52	64

*Quarterly Data Percent Change At Annual Rate; Annual Data Year-on-Year % Chg, or Annual Average.

Financial Data	2014.1	2014.2	2014.3	2014.4	2015.1	2015.2	2015.3	2015.4	2016.1	2016.2	2016.3	2016.4	2013	2014	2015	2016
	History				Forecast								Annual Average			
S & P 500	1,835	1,900	1,976	2,009									1,644			
Dow Jones Industrial Average	16,177	16,604	16,954	17,345									15,010			
Federal Funds Rate (effective)	0.07	0.09	0.09	0.08	0.12	0.13	0.21	0.46	0.88	1.13	1.38	1.71	0.11	0.08	0.23	1.27
Treasury-3 Month Bills (yield)	0.05	0.03	0.03	0.02	0.04	0.05	0.11	0.36	0.78	1.03	1.28	1.61	0.06	0.03	0.14	1.18
Treasury-2 Year Notes (yield)	0.37	0.42	0.52	0.52	0.59	0.65	0.88	1.08	1.55	1.85	2.10	2.43	0.31	0.45	0.80	1.98
Treasury-5 Year Notes (yield)	1.60	1.66	1.70	1.57	1.46	1.53	1.72	2.00	2.44	2.64	2.89	3.02	1.17	1.63	1.68	2.75
Treasury-10 Year Notes (yield)	2.77	2.62	2.50	2.27	1.98	2.17	2.35	2.51	2.71	2.84	2.95	3.18	2.35	2.54	2.25	2.92
Treasury-30 Year Notes (yield)	3.68	3.44	3.27	2.97	2.55	2.75	2.90	3.05	3.16	3.27	3.40	3.53	3.44	3.34	2.81	3.34
Prime Rate	3.25	3.25	3.25	3.25	3.25	3.25	3.33	3.58	4.00	4.25	4.50	4.83	3.25	3.25	3.35	4.40
Libor 3-Mo. U.S. Dollar	0.26	0.25	0.24	0.23	0.26	0.27	0.33	0.58	1.00	1.25	1.50	1.83	0.28	0.25	0.36	1.40
Mortgage-30 Year (yield)	4.36	4.23	4.14	4.03	3.71	3.92	4.16	4.30	4.52	4.65	4.76	4.99	3.98	4.19	4.02	4.73
BAA Corporate (yield)	5.12	4.82	4.74	4.74	4.52	4.62	4.70	4.87	5.05	5.20	5.32	5.55	5.10	4.86	4.68	5.28

Source: Bank of the West Economics, Bloomberg, Federal Reserve