



Economics Group

Tim Quinlan, Senior Economist
tim.quinlan@wellsfargo.com • (704) 410-3283
Sarah House, Senior Economist
sarah.house@wellsfargo.com • (704) 410-3282
Shannon Seery, Economic Analyst
shannon.seery@wellsfargo.com • (704) 410-1681

What 737-MAX Groundings Mean for Durable Goods

The widespread grounding of the 737-MAX aircraft means that durable goods orders will likely be under added pressure the next few months. The pause on deliveries also represents a near-term risk to equipment spending.

The Fast-Growing 737 MAX Now Poised for Potential Decline

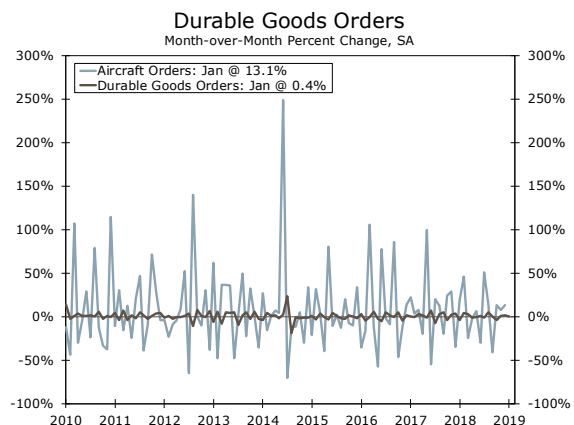
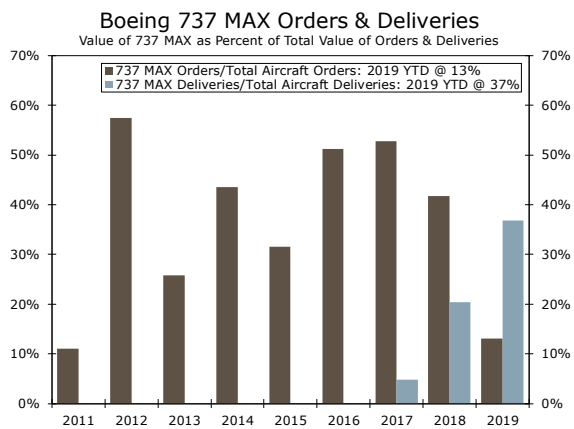
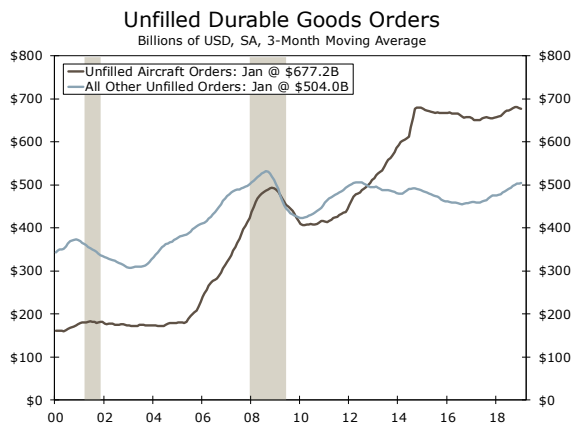
Whether from the Defense Department or from private airlines, aircraft orders are usually a big swing factor in overall durable goods orders. With news this week that the U.S. Federal Aviation Agency (FAA) joined its counterparts around the world grounding the 737-MAX and Boeing halting deliveries, we consider the potential implications for durable goods orders and equipment spending.

The groundings apply only to the 737-MAX, the most recent generation of the world’s best-selling aircraft. Since the first shipment in May 2017, Boeing has delivered just 376 of the aircraft in question, though the total number of orders booked is just over 5,000, the earliest of which were recorded as far back as 2011. If some of those orders were to be canceled, the Commerce Department would subtract them from the headline figure in the month in which they occur for the durable goods report, according to notes in the report release and our discussions with Commerce Department staff.

We have had some success forecasting headline durable goods in recent years partly due to a time series we constructed based on actual orders data from Boeing and an informed guess of an average discount to the list aircraft pricing published on its website. While this is not intended to be spot-on accurate, it functions reasonably well and offers a decent starting point for understanding the potential impact on durables from recent groundings.

Aircraft orders can be highly volatile from month to month, but they made a little under a tenth of total durable goods orders over the past year. From 2011 to 2015, orders for all types of the 737-MAX aircraft comprised roughly a third of Boeing orders, though it has become more important since 2016, comprising just under half of all bookings (47.1% by our estimate). Considering the 737-MAX aircraft comprises almost half of Boeing’s orders in the past few years the total negative impact to durables could be substantial if airlines hold off on new 737-MAX orders the next few months.

We doubt we’ll see significant cancellations, however. Cancellations tend to incur hefty penalties, and Boeing is working on a fix for the issue at hand. In addition, multi-year backlogs at Airbus leave airlines looking to expand or upgrade aging fleets few alternatives. A similar situation occurred after a battery problem linked to fires aboard the 787 Dreamliner caused a grounding of that aircraft from January to April of 2013. Orders still came in during the grounding period and the Dreamliner has subsequently seen steady sales volume. Also reminiscent of that period, Boeing said they will continue to build the 737-MAX while it resolves the issue, which will likely prevent any major disruption to supply chains. Suspended deliveries, on the other hand, could weigh on capex spending as early as the current quarter. The 737-MAX aircraft averaged roughly 40% of aircraft deliveries in the past three months. With fewer aircraft being shipped until the issue is resolved, we see some risk to our near-term outlook for equipment spending.



Wells Fargo Securities Economics Group

Jay H. Bryson, Ph.D.	Global Economist	(704) 410-3274	jay.bryson@wellsfargo.com
Mark Vitner	Senior Economist	(704) 410-3277	mark.vitner@wellsfargo.com
Sam Bullard	Senior Economist	(704) 410-3280	sam.bullard@wellsfargo.com
Nick Bennenbroek	Macro Strategist	(212) 214-5636	nicholas.bennenbroek@wellsfargo.com
Tim Quinlan	Senior Economist	(704) 410-3283	tim.quinlan@wellsfargo.com
Azhar Iqbal	Econometrician	(212) 214-2029	azhar.iqbal@wellsfargo.com
Sarah House	Senior Economist	(704) 410-3282	sarah.house@wellsfargo.com
Charlie Dougherty	Economist	(704) 410-6542	charles.dougherty@wellsfargo.com
Erik Nelson	Macro Strategist	(212) 214-5652	erik.f.nelson@wellsfargo.com
Michael Pugliese	Economist	(212) 214-5058	michael.d.pugliese@wellsfargo.com
Brendan McKenna	Macro Strategist	(212) 214-5637	brendan.mckenna@wellsfargo.com
Shannon Seery	Economic Analyst	(704) 410-1681	shannon.seery@wellsfargo.com
Matthew Honnold	Economic Analyst	(704) 410-3059	matthew.honnold@wellsfargo.com
Dawne Howes	Administrative Assistant	(704) 410-3272	dawne.howes@wellsfargo.com

Wells Fargo Securities Economics Group publications are produced by Wells Fargo Securities, LLC, a U.S. broker-dealer registered with the U.S. Securities and Exchange Commission, the Financial Industry Regulatory Authority, and the Securities Investor Protection Corp. Wells Fargo Securities, LLC, distributes these publications directly and through subsidiaries including, but not limited to, Wells Fargo & Company, Wells Fargo Bank N.A., Wells Fargo Clearing Services, LLC, Wells Fargo Securities International Limited, Wells Fargo Securities Canada, Ltd., Wells Fargo Securities Asia Limited and Wells Fargo Securities (Japan) Co. Limited. Wells Fargo Securities, LLC is registered with the Commodities Futures Trading Commission as a futures commission merchant and is a member in good standing of the National Futures Association. Wells Fargo Bank, N.A. is registered with the Commodities Futures Trading Commission as a swap dealer and is a member in good standing of the National Futures Association. Wells Fargo Securities, LLC and Wells Fargo Bank, N.A. are generally engaged in the trading of futures and derivative products, any of which may be discussed within this publication. Wells Fargo Securities, LLC does not compensate its research analysts based on specific investment banking transactions. Wells Fargo Securities, LLC's research analysts receive compensation that is based upon and impacted by the overall profitability and revenue of the firm which includes, but is not limited to investment banking revenue. The information and opinions herein are for general information use only. Wells Fargo Securities, LLC does not guarantee their accuracy or completeness, nor does Wells Fargo Securities, LLC assume any liability for any loss that may result from the reliance by any person upon any such information or opinions. Such information and opinions are subject to change without notice, are for general information only and are not intended as an offer or solicitation with respect to the purchase or sales of any security or as personalized investment advice. Wells Fargo Securities, LLC is a separate legal entity and distinct from affiliated banks and is a wholly owned subsidiary of Wells Fargo & Company © 2019 Wells Fargo Securities, LLC.

Important Information for Non-U.S. Recipients

For recipients in the EEA, this report is distributed by Wells Fargo Securities International Limited ("WFSIL"). WFSIL is a U.K. incorporated investment firm authorized and regulated by the Financial Conduct Authority. For the purposes of Section 21 of the UK Financial Services and Markets Act 2000 ("the Act"), the content of this report has been approved by WFSIL, an authorized person under the Act. WFSIL does not deal with retail clients as defined in the Directive 2014/65/EU ("MiFID2"). The FCA rules made under the Financial Services and Markets Act 2000 for the protection of retail clients will therefore not apply, nor will the Financial Services Compensation Scheme be available. This report is not intended for, and should not be relied upon by, retail clients.

SECURITIES: NOT FDIC-INSURED/NOT BANK-GUARANTEED/MAY LOSE VALUE