BUSINESS INTELLIGENCE BRIEF

December 7, 2017

NATIONAL AND INTERNATIONAL NEWS AFFECTING LOCAL BUSINESS

Short Items of Interest – US Economy

- **Labor Market Still Tight –** The number of new applications for unemployment fell again this week and that is yet another sign that the labor market remains very tight. There are no big lay-offs taking place and mist companies are aggressively working to keep their existing employees. The most common means by which companies are adding to their workforce these days is through poaching the employees of other companies. The pipeline for new employees is very weak and there are no reliable means by which to get the people needed. There are still millions of people who need a job but they do not have the skills needed and this can't compete for the jobs that are on offer.

- **High Cost of Education is a Major Issue –** The challenge for the employer is finding the people they need to fill the positions open and the challenge for the worker is get the education and training needed. It would seem that this would be an easy fix but the problem is this education is expensive and not often convenient enough for those who need it. The latest comment on this matter has come from the New York Fed head – Bill Dudley. The suggestion is the US has to do a far better job of integrating people into the workforce through education and the logical first step is to lower the costs. Unfortunately, the education system is facing cuts across the board at the very time it is needed to meet these new needs.

- **Reassuring the Business Community –** The GOP is trying to assuage the fears of the business community when it comes to the tax reform effort. It is not that there is an objection to the reduction to 20% but the huge changes as far as deductions are worrying many. It has been pointed out for years that many of the largest companies have been paying far less than full freight for years and many have not even paid the 20% now suggested as they had breaks. If those breaks all go away they may very well be paying more than they did before. The smaller company stands to get more of a break but even they are worried about what happens with their deductions

Short Items of Interest – Global Economy

- **Jerusalem as Capitol –** In fact Jerusalem has been the capitol of Israel for a very long time and there is no doubt within the country where the seat of power lies. For the world as a whole the issue is not as clear due to the Palestinian claims on the same city. The US and many other nations agree to act like Jerusalem is not the capitol while doing business there as if it was. This is symbolism at its excruciating limit. Now Trump has come out and reversed decades of this feint and stated that Jerusalem is the capitol of the state of Israel. What changes? Nothing really except the US has lost all sense of being impartial and thus in no position to try to broker a deal. Not that the Palestinians had any doubt as to where the US sympathies lie.

- **Schulz Sets Out his Terms –** Before the Social Democrats agree to start talks with Angela Merkel over a "grand coalition" the leader wants a commitment to a much stronger EU – a united states of Europe. This goes much further than what is currently in place and will strain the willingness of many in Europe to stay engaged – it also makes life challenging for Merkel as she has not been a big fan in the past. The Brexit issue has galvanized support for the EU as never before but subsuming nationality like this may not be palatable.

- **Modi Losing Support –** The "Modification" of India has hit some snags and the once very popular leader has been losing ground. It is now expected that he will lose a big chunk of his own home state-Gujarat- as the population wants more change and more growth and thinks he has been wasting his time on unrelated issues.

KC CHAMBER

Looking at the Index of Indices

It is that time once more – time to look at the data that is presented to pair of industrial organizations. The Chemical Coaters Association International and the Industrial Heating Equipment Association commission us to look at some of the data sets that matter most to them and what follows is the executive summary and some select discussions of specific index material. Send me an e-mail at chris.kuehl@armadaci.com if you want to see the whole thing complete with the year over year charts and graphs.

This has been a good year overall and that is more than a little surprising given the anticipation and the turmoil. At the start of the year there was all kinds of enthusiasm regarding the arrival of a supposedly pro-business White House and Congress. The assumption was that a GOP controlled government would final do the things the business community has been hoping for. The scandals and the political infighting rendered that assumption incorrect and nothing much has emerged from Washington. In spite of all this the economy has been growing at a 3.0% pace for two quarters. It seems the business community just decided to focus on what they can control and have just expanded while the consumer has been focusing on what they do best – buy things.

This month the majority of the measures have been trending in a positive direction – nine of the twelve have been up and in more than a few cases the gains have been as good as they have been all year and much better than they had been the month previous. The positives start with "New Automobile and Light Truck Sales" and that is somewhat unexpected as the big post-storm surge has long passed. The pattern even looks somewhat sustainable. The big surprise was the "New Home Starts" as it has been expected this sector would soon start to tail off in response to all those headwinds of higher prices and so on. Instead there has been more building of starter homes than has been the case in some time. The "Steel Consumption" data shows that demand has been up from the auto sector as well as from construction and others. The stockpiling as a result of steel tariff fears seems to be over for now. The "price of other industrial metals" have fallen but this has not been due to lack of industrial demand. These are all metals that attract investors and right now it appears that these commodity investors are being lured into the world of crypto-currency and away from more traditional plays.

There were impressive gains as far as capacity utilization and some of the other broad measures of the economy. The rate of utilization is still short of the preferred range but it is heading in the right direction. The capital investment numbers were not quite as good but it has been noted that cap-ex is not likely to surge much unless the capacity numbers are over 85% and thus far they are still well short of that number. There is still too much slack in the system but it is less pronounced than it has been. The data from the Purchasing Managers' Index is strong and the "New Orders Index" is still in the 60s and that is as high as this index has been in many years – at least consistently. The overall PMI is solidly in the 50s and gaining.

The action in the various industrial measures is steady – no big gains to speak of but no declines either. The performance of "Durable Goods Shipments" has been steady and that is due in part to the absence of any big sales in the aerospace sector. The purchasing here has been steadier than usual and there has been a similar performance as far as machinery and other goods are concerned. There was a slight decline as far as "Factory Orders" were concerned but this is likely seasonal to a degree as the retailers have already done their ordering for the holiday and production levels are down. There was also some movement (however slight) in "Appliances) as there are more unfilled orders and a somewhat reduced level of inventory.

The last two categories are the Credit Managers' Index and the Transportation Index and both of these serve as harbingers of what is to come. The credit manager is at the forefront of each and every business decision that would involve credit and that is most of them. The transportation data is always seen as the canary in the coal mine as it will feel anything happening in the economy first. If there is no activity there is nothing to ship and busy factories mean busy trucks and trains and planes. Both of these indices are trending up and dramatically and that is a very good indicator as far as what to expect in the coming year. If past patterns hold the Q4 numbers will be strong but not quite as robust as Q3 and then there is likely to be a bigger decline in Q1 of next year. These data sets suggest that this year might be better than those in the past – albeit marginally.

New Automobile/Light Truck Sales - The twin storms that ravaged Texas and Florida had their silver lining. It is no wonder that economists are referred to as dismal scientists as we tend to look at natural disasters a little differently. They are certainly tragic and destructive and all that BUT after they are over and have done their worst there is an opportunity to extensively rebuild and that ends up giving the economy a nice little boost. It certainly had an impact on the automotive sector as millions of vehicles had to be replaced and quickly. The sales of new cars and trucks may have been in excess of 3 million and that pushed the entire sector forward. That was that nice bump in September and then there was the subsequent return to normal. This latest surge is a second order reaction to some degree. Once the emergency car purchase was over there was a demand for the vehicle that was really needed or wanted and those others were consigned to the used car lots.

This can also be a good time of year for car sales as this has been an active holiday season thus far. In the last few years there have been substantial jumps in sales as seen in the graph of the last year. This year has also seen a little burst of activity but nothing quite like the one last year – at least not yet. The consumer has more to spend and is more confident in terms of those big purchases and that will likely push sales a little faster.

More From the IHEA/CCAI

New Home Starts - The sales of new homes took off this month and for that matter so has the sales of existing homes. The motivation seems simple enough as consumers are feeling better about their financial situation now and in the future. The low rates of joblessness suggest that people can be assured they will have the means to handle a mortgage. The perplexing aspect of this surge is that home prices have been going up rather sharply. That was described for months as a "headwind" the housing market would struggle with but that has not really manifested at this point. The most aggressive sector for new homes have been those that are described as "starter homes" and these had not been a big part of the market until this point. There are still many of those bigger homes being sold as well.

It is not clear what impact the tax conversation has had on home sales but the real estate community has been expressing concern over what might happen to the mortgage interest deduction. It appears that it may go away for more expensive homes and that would likely dampen demand for these. It is also possible the deduction will vanish altogether although both the House and Senate seem to be backing away from that option. It doesn't appear to be driving people to buy now while the deduction is in place but it may if the deal gets done.

Steel Consumption - The rate of steel consumption improved this month for a variety of reasons. Top of the list was the extra vehicle production that has been taking place through the last few months but there has also been some additional consumption related to construction – both in the private sector and the public sector. There has not been a huge boost in infrastructure work as promised at the start of the year but there has progress in the harder hit areas of Texas, Florida and Puerto Rico. These are still temporary boosts. Earlier in the year there was some stockpiling of steel in anticipation of steel tariffs but that seems to have played itself out to some degree. The tariff plan is stalled for now but remains on the table and could reappear at any moment.

For the most part consumption levels have been fairly constant with no big dips or big surges. The major steel using industries have not seen big changes and that has promoted general stability. The ongoing concern in the US is that scrap steel is in relatively short supply. There are not as many cars getting junked and there is not as much steel in them these days. Building tear downs have been few and far between and that has impacted the overall availability of the scrap needed to fuel the mini-mills.

Industrial Capacity Utilization - Last month was a bit depressing as the steady march of capacity utilization seemed to have been interrupted. This month things appear to be back to normal or at least headed that way. As has been stated repeatedly the rate of capacity utilization is a very good measure of whether an economy is in the "sweet spot" where the business community is using its equipment and staff efficiently. If the rate of utilization is under 80% there is too much slack in the system – too little efficiency., When the rate is over 85% there is too much pressure on that business and there will likely be issues of shortage and bottlenecks. Business will not invest in new machinery or people when their capacity usage is under 80% but they will when that usage number is past 85%.

In a related measure that is produced by the Fabricators and Manufacturers Association – the FFJSCR – there is a measure of capacity usage for the smaller job shops and business. The Forming and Fabricating Job Shop Consumption Report holds that capacity usage for this group is in the high 60s – quite a bit less than the national norm.

PMI New Orders - The data from the Purchasing Managers' index has been as strong as it has been in years. The overall PMI has been consistently in the mid to upper 50s and the new orders index has been sitting above 60 since the middle of the summer and has been in that high growth territory for four of the last twelve months. The increase in activity has been taking place in a variety of sectors – everything from automotive to aerospace and even the agricultural sector. The service sector part of the PMI has been just as active and that bodes well for the year to come. The new orders numbers are more forecast oriented and show what purchasing managers are expecting in the next quarter or two. The reports suggest that more machines are being purchased and there has been some inventor build as well.

This is not the only sub-index of the PMI that has been doing well. There have been gains in export numbers as well as hiring and that also points to a solid 2018.

The Variety in Uber

I know full well that Uber has been having more than a few issues – the founder of the company may have a great idea but his skill as a leader left much to desire. There have been issues of how the drivers are treated, the way that data has been handled and so on. These issues may or may not affect the company's longevity but ride share apps will live on and what I find more interesting is the motivation of these drivers. I take lots and lots of Uber rides – every time I travel. In just the last week I have met several people with very different approaches to the job.

There was the guy yesterday who makes his living as a salesman. He noticed that he often had two or three hours to kill between appointments and signs on to Uber for that period so he makes a few bucks as opposed to spending them sitting in a Starbucks. Earlier that day I had a guy from Nigeria that had abandoned the cab business as it was far too hard to make money. He was a driver back home in Lagos and is still a driver – this is his chosen career. Earlier in the week I had a retired school teacher that just gets bored sitting at home all evening and only works during the day. Last week I had a driver who was Croatian and was striving to be a model or spokeswoman. "I need to better my English so I drive people all day and talk a lot". The point is that these are mostly very entrepreneurial people who have a realistic view of the business and as a bonus for me – I learn a lot about the local communities I am passing through.

Global Manufacturing Roundup:

- **General Global Manufacturing Inched Up on a Seasonal Basis in November.** Global manufacturing activity inched up in November to 53.5, its **highest level since March of 2011**. New orders were also up again, rising to 55.1 from 54.2 in October. The future output index rose to 63.1 from 62.6 in the prior month. Coupled with strong new orders, the future output index helps understand what future transportation demand will be like. Based on the notion that every metric in the November manufacturing report was higher, transportation demand should also be higher.

- **Mexico Manufacturing Rebounds Strongly in November.** The Mexican manufacturing sector has rebounded in November with the composite reading rising to 52.4, up from 49.2 in October. New orders took the strongest month-over-month increase in more than 18 months. Domestic demand in the wake of the massive earthquake that hit the southern regions of the country in September have rebounded and are expected to remain strong in the coming months during the recovery phase.

  We still saw an increase in key segments such as automotive and consumer goods. The automotive market has seen a significant resurgence of late. Some of that is due to the hurricanes in the US in which more than 1 million vehicles were estimated to have been destroyed.

- **United Kingdom:** The UK saw manufacturing grow again in November, hitting the strongest levels in more than 51 months. The index came in at 58.2, rising from 56.6 in October. Once again, new orders remain robust and hiring was much stronger in November. Unlike previous months, the impact of a weaker currency across the UK led to an uptick in export activity, a factor that will remain in place until Brexit negotiations are completed sometime in 2018.

Armada Staff –Chris Kuehl, Keith Prather, Karen Sanchez **P.O. Box 733 – Lawrence, Kansas 66044 – intel@strategic-briefs.com**