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VOLUME 5

The ITR Advisor

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INDUSTRY SNAPSHOTS

Arrow denotes 12-month moving total/average direction

Retail Sales	Mild Rise
Wholesale Trade	Mild Rise
Auto Production	Flat
Manufacturing	Mild Rise
Rotary Rig	Mild Rise
Capital Goods	Mild Rise
Nonresidential Construction	Mild Rise
Residential Construction	Flat

Steep Rise
Flat
Mild Rise
Mild Decline
Steep Decline

MACROECONOMIC OUTLOOK

US Total Industrial Production ended 2018 up 4.1% from the 2017 level. US Industrial Production is rising. However, US Electric and Gas Utilities Production tentatively entered a declining trend in December. US Total Manufacturing Production (up 2.7%) and US Total Mining Production (up 12.6%) are projected to transition to slowing growth trends early this year. Firms aligned with the industrial economy should be prepared to contend with the back side of the business cycle.

"Firms aligned with the industrial economy should be prepared to contend with the back side of the business cycle."

The US industrial economy is benefiting from a strong consumer sector. US Total Retail Sales were up 5.0% from one year ago. However, the pace of rise for Retail Sales will slow through much of this year. This will contribute to slowing activity in the industrial sector. We do expect Retail Sales to avoid contraction during 2019, which will limit the severity of the recession expected in US Industrial Production. However, firms should budget for waning growth opportunities from the consumer sector in 2019.

US Exports are growing at a slowing pace, which will contribute to the slowing growth trend in the US industrial economy. The global economy is slowing in its rate of growth. As a result, foreign consumers will likely slow their rate of purchasing US consumer goods while foreign firms will likely slow their rate of purchasing US capital goods. As Exports trend on the back side of the business cycle, communicate your competitive advantages to maintain your market share and avoid competing based on price alone. Market your newer offerings to stand out from your competitors.

Firms closely aligned with US Industrial Production should plan for some contraction in the second half of 2019 and in early 2020. However, this will be mild by historic standards. Use the upcoming recessionary period to invest before valuations rise. We expect growth through much of 2020 and 2021.

MAKE YOUR MOVE™

Use the period of growth during the first half of 2019 to prepare for the upcoming recession in the industrial economy. Build up your reserves of cash and look to reduce expenses. With cash on hand during the recession, you will be better positioned to invest for the next period of growth.

INVESTOR UPDATE

The stock market rebounded in January after a few weak months at the end of 2018. Although it is too early to call the start of a rising trend, a strong January supports our expectation that this is not a bear market.

ITR ECONOMICS' LONG-TERM VIEW

2019: Weaker Second Half **2020:** Mild Growth **2021:** Growth

INDUSTRY ANALYSIS

Retail Sales
- Retail Sales ended 2018 up 5.0% from the 2017 level
- Retail Sales will rise throughout this year
- The Conference Board's US Consumer Confidence Index is signaling that business-cycle decline is likely during the majority of this year

Wholesale Trade
- Wholesale Trade was up 7.9% on a year-over-year basis
- Both Wholesale Trade of Durable and Wholesale Trade of Nondurable Goods are in slowing growth trends
- This sector is unlikely to enter a recession during this cycle, but the pace of growth will be slow compared to 2018

Auto Production
- North America Light Vehicle Production was down 0.4% from a year ago
- Light Vehicle Production is recovering but will not rise much above its current level during this cycle
- North America Heavy Duty Truck Production was up 24.3% but will contract in the latter half of this year

Manufacturing
- Total Manufacturing Production rose 2.7% in 2018 from the 2017 level
- Production is currently growing at an accelerating pace but will transition to a slowing growth trend early this year
- Activity will decline through much of the manufacturing sector this year

Rotary Rig
- The Rotary Rig Count was up 16.3% from the year-ago level
- The Rig Count is rising at a diminishing rate
- Both the Oil Rotary Rig Count (up 18.7%) and the US Natural Gas Rotary Rig Count (up 8.8%) are rising at slowing rates

Capital Goods New Orders
- Nondefense Capital Goods New Orders were up 6.6% on a year-over-year basis
- Business-to-business activity will decline during the latter half of this year
- Defense Capital Goods New Orders were up 19.7%
- New Orders in the defense sector will end 2019 just above the 2018 level

Total Nonresidential Construction
- Nonresidential Construction was up 4.4% from a year ago
- Much of the nonresidential sector will expand in 2019
- Warehouse Buildings Construction is an area of opportunity and will likely remain one throughout 2019

Total Residential Construction
- Residential Construction was up 4.3% from one year ago
- Construction is growing at a slowing rate
- Single Unit Housing Starts and Multi Unit Housing Starts will decline during the first half of 2019
- The nonresidential sector will likely present more growth opportunities this year

LEADING INDICATOR SNAPSHOT

	1Q19	2Q19	3Q19
ITR Leading Indicator™	🔴	🔴	🔴
ITR Consumer Activity Leading Indicator™	🔴	🔴	N/A
US Leading Indicator	🟢	🟢	N/A
Purchasing Managers Index	🔴	🔴	🔴
US Total Capacity Utilization Rate	🟢	🔴	N/A

Green denotes that the indicator signals cyclical rise for the economy in the given quarter. Red denotes the opposite.

- Most of the indicators support our expectations for Industrial Production to transition to a slowing growth trend in the near term
- Decline in the ITR Leading Indicator™ supports expectations for Production to slow through at least the third quarter of this year
- The US Leading Indicator has been declining in recent months and suggests a second-quarter peak for Production

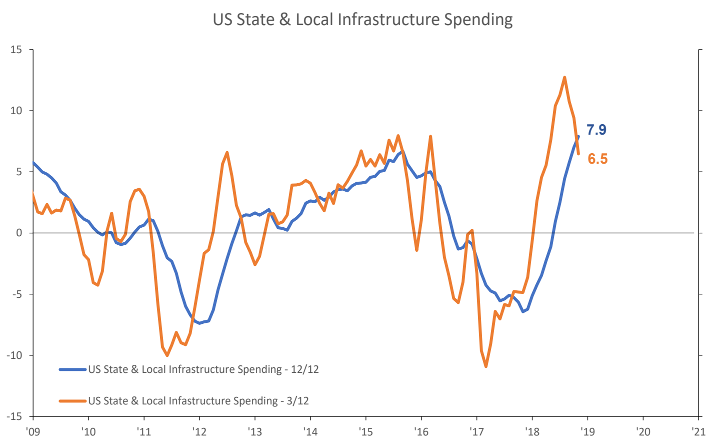
Is an Infrastructure Bill the Magic Pill?

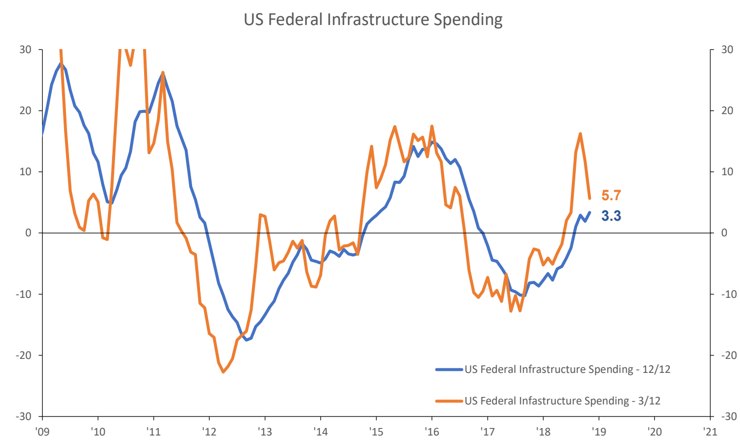
By: Alan Beaulieu

What you need to know: *Both federal infrastructure spending and state and local infrastructure spending are showing slowing rates of growth on a quarterly basis.*

Both federal infrastructure spending and state and local infrastructure spending are showing slowing rates of growth on a quarterly basis (the 3/12s are moving lower). A slowing in the rate of spending still means there will be work for contractors and demand for materials. The current status shows the following:

	Phase	Comment
US Federal Infrastructure Spending	B	$8.5 billion and slowing soon
US State & Local Infrastructure Spending	B	$168.0 billion and slowing soon



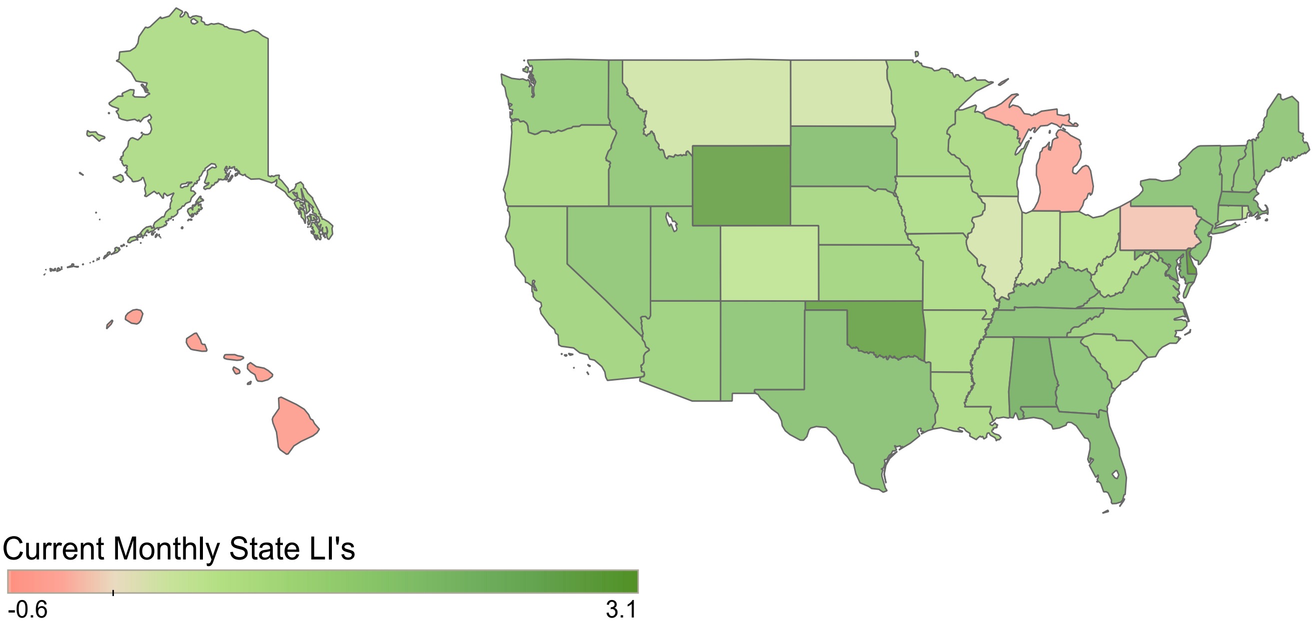


We often get asked if a major infrastructure bill out of Washington would change our forecast for 2019 and 2020. The short answer is no – it would not.

First of all, the plan floated in 2017 was not well received by either party, and right now we are without significant legislation to fund new infrastructure spending in the US.

There are two things to consider regarding any bill that might surface on this subject. One is the enormous amount of time that elapses between passing legislation, funding it, and then funding specific projects. There is really no such thing as a "shovel ready" project because each project must be evaluated and weighted. A federal bill in 2019 would not likely result in much money being disbursed until well into 2020.

The second thing to consider is the actual funding. Where would the money come from? There are a few choices, two of which would impact consumers and business in the near term. One option is to raise gasoline taxes or income taxes. The other option is increased federal borrowing, which pushes the cost (less interest payments) into the future.



- The US Leading Index rate-of-change is declining but is above the year-ago level, which is consistent with our expectation of slowing growth for the US economy
- State Leading Indexes are signaling rise in GDP for nearly every state in the country during at least the next few months
- Michigan, Pennsylvania, and Hawaii are areas of weakness; Leading Indexes for these states are signaling that decline in their respective GDPs will take hold in the next few quarters

READER'S FORUM

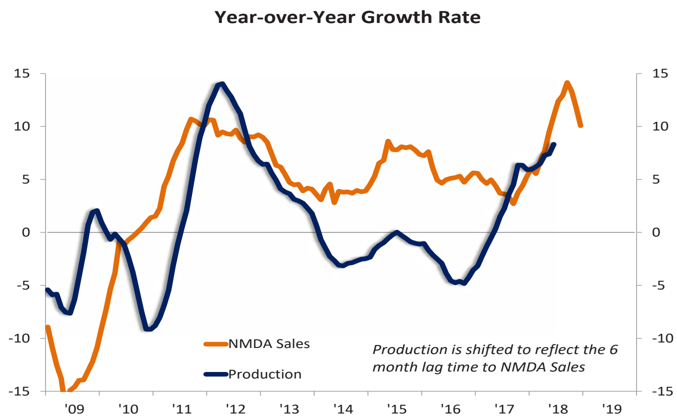
ITR recommends looking to countercyclical markets when the business cycle turns downward. What do you expect will be some growth markets in 2019 as the economy loses steam?

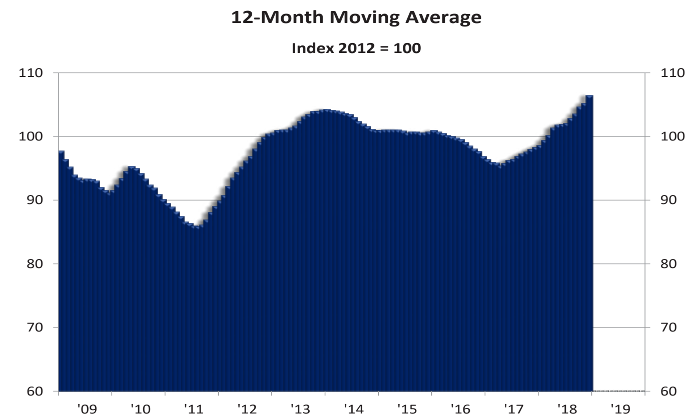
James Giles, Economist at ITR Economics™, answers:

While we do expect business-cycle decline through much of the industrial sector in 2019, certain markets will trend in a positive direction. US Civilian Aircraft Equipment Production and US Medical Equipment and Supplies Production, which have contracted in recent quarters, are recovering and will expand in 2019. Nonresidential construction, which typically lags the industrial economy, will also grow throughout this year. Although the macroeconomic business cycle is turning downward, firms in the civilian aircraft equipment, medical equipment, and nonresidential construction sectors should lead with optimism and invest with the expectation of growth in 2019.

Please send questions to questions@itreconomics.com

US Ship and Boat Building Production

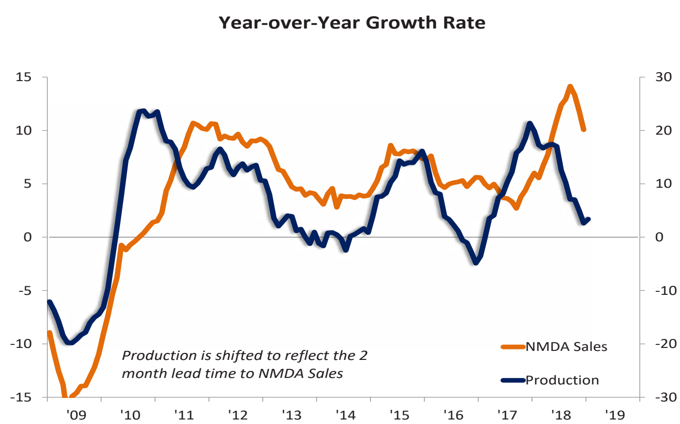


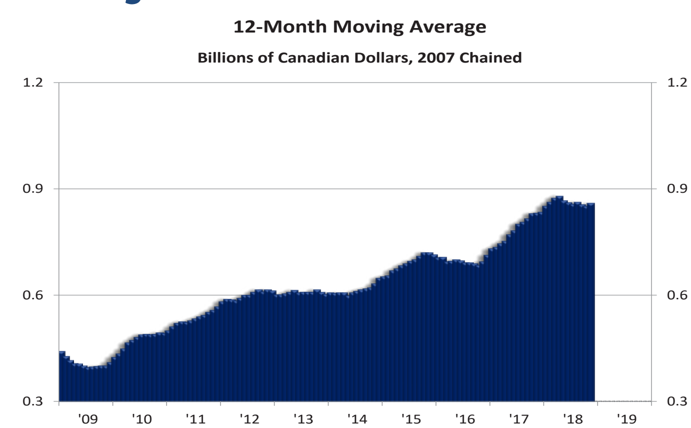


US Ship and Boat Building Production ended 2018 up 8.3% from the 2017 level. Production is rising at an accelerating pace. However, the Boat segment has tentatively transitioned to a slowing growth trend, and although more data is necessary to confirm this transition, it is unlikely that the pace of growth will rise much above the current level.

Ship and Boat Building Production is benefiting from a strong consumer sector. However, Retail Sales will grow at a slowing pace through the majority of this year, which suggests that Ship and Boat Building Production will slow in its pace of rise imminently. Revisit your capital expenditure plans with the expectation for slowing growth in Production, taking caution not to overinvest.

Canada Ship and Boat Building Production





Canada Ship and Boat Building Production during the 12 months through November was up 3.4% from the year-ago level. Production has declined in recent months, and despite mild rise in the most recent month of data, general decline through at least the first half of 2019 is possible, which poses a risk to firms operating in Canada.

The Canada Purchasing Managers Index for Manufacturing is declining. This indicator is signaling that Production will face further downward pressure during at least the first half of 2019, consistent with our expectations. Firms should communicate their unique competitive advantages, such as cost or quality, to stand apart from the crowd and maintain market share as activity declines during the next few quarters.

* Report includes two participating companies providing less than two years of data. This addition may skew near-term performance of NMDA Sales.

