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news and economic outlook for the wire and cable industry
IEWC GLOBAL SOLUTIONS

IN THE SPOTLIGHT

Hope for Free Trade in North America

Disputes between the US and its neighbors to the north and south threatened to disrupt free trade, but with the signing of a new trade deal last week it seems North America will avoid a trade relationship breakdown. The United States-Mexico-Canada Agreement (USMCA) replaces NAFTA and preserves a free trade bloc in North America. Most segments of the economy are unlikely to change as a result of this deal, and many companies can plan for business as usual.

Automotive Industry a Notable Exception

The automotive industry is an exception. The agreement intends to support North American automotive production by raising the threshold for exemption from tariffs. For a vehicle to avoid the tax, 75% of its value will have to originate in the US, Mexico, or Canada, up from NAFTA's 62.5% threshold. This may shift some production to these three countries. However, the higher labor costs relative to Asia could drive up automotive prices.

As important as what was included in the USMCA is what was not. The Trump administration had demanded a five-year sunset clause that would have required the three countries to frequently agree to extend the deal to prevent its expiration. Opponents argued that the clause would make it difficult for firms operating in these countries to plan for the long term, likely discouraging investment. Instead, the deal will last at least 16 years, providing businesses with a longer time horizon for planning.

An Incomplete Win for Free Trade

While the USMCA is largely a win for free trade, other US protectionist policies remain. Tariffs on steel imports are still in effect, including steel from Mexico and Canada. Tensions are escalating between the US and China, leading to tariffs on billions of dollars' worth of goods. These policies are likely to be inflationary in nature for all involved parties. A prolonged full-blown trade war with China would pose a serious long-term threat to both nations. The USMCA may be a sign that cooperation and free trade are possible, and that this threat can be averted.

READERS' FORUM

Rising input costs are cutting into our profits. What can we do about these higher costs and when is inflation expected to slow?

Firms with rising input costs should generally look to pass on these costs to their customers. Ensure that you have the proper price escalators in place to protect your margins. However, keep an eye on your competition. If other businesses are keeping their prices low, you may need to take a hit from higher costs to keep your prices competitive. We recommend that you communicate the other advantages of your products, such as quality, to avoid competing solely based on price. This will make it easier to justify your cost increases to your customers.

There will likely be some relief in 2019. The pace of rise for producer prices is expected to slow next year. Costs for some commodities such as oil and steel are expected to fall in the next several quarters. Purchasing conditions for commodities will likely be more favorable next year.

Arrows indicate 12-month moving total/average direction

Retail Sales

- Up 5.4% during 12 months ending in September
- Growth expected through at least 2020
- Pace of growth will slow through most of 2019

Rotary Rig

- Count during the 12 months through October up 22.2%
- Rig count growth is slowing
- Oil and gas production growth will slow

Wholesale Trade

- Wholesale trade up 8.5% year-over-year, with durable goods up 9.1% and nondurable goods up 7.9%
- Wholesale trade unlikely to enter recession during this business cycle
- Growth rates for both segments will slow by the end of 2018

Capital Goods

- New orders during 12 months through September up 7.4%
- Business-to-business activity will rise through the first half of 2019
- Pace of growth for new orders slowing

Auto Production

- N. America light vehicle production down 2.2% 12 months through Sept.
- Current recovery trend in production is unlikely to last much longer
- Activity will decline in 2019 into early 2020

Nonresidential Construction

- Nonresidential Construction during 12 months through Sept. up 3.1%
- Double-digit growth rates expected for US warehouse building construction in 2019 and US multi-retail building in 2020
- Total nonresidential construction will rise into early 2020

Manufacturing

- Total manufacturing during the 12 months through Sept. up 2.5%
- Production is growing at an accelerating pace
- Much of the manufacturing sector will contract in 2019

Residential construction

- Residential construction up 7.1% during 12 months through Sept.
- Construction is growth is slowing
- Decline in both single-unit housing starts and multi-unit housing starts expected in 2019

October Is Likely a Correction, Not a Bear

October was an arduous month for US equity investors, as the S&P 500 Stock Prices Index closed the month down 6.9% from the start of the month. This was the most punishing September-to-October drop since the 16.8% decline in October 2008, in the heart of the Great Recession. The sharp drop caught the attention of stock analysts and individual investors alike. Pundits were quick to point to the US midterm elections as a source of uncertainty that spooked the market. A look at history tells us that this was not a typical pre-midterm October.

During midterm election years dating back to 1950, the numbers tell us the following:

- October typically fares better during midterm election years, averaging a 2.7% month-to-month increase from September.
- Midterm election years compare very favorably to an average September-to-October performance of +0.8% over all years dating back to 1950.
- This was the second-worst October in a midterm year during the period, behind the 9.2% October 1978 decline.
- There could be some relief coming, as market decline in October has typically been followed by rise in November in midterm election years.
- The average 2.7% increase in stocks in November following midterms beats the all-years average of +1.6% for November.

The fourth quarter of a midterm year is typically kind to the market. The fourth quarters of midterm election years since 1950 have averaged a 5.0% increase from the third quarter, two-and-a-half times the 2.0% average market increase in all fourth quarters during that period. In 1978, the market was unable to fully recover from its October tumble, ultimately declining 7.4% in the fourth quarter from the third quarter.

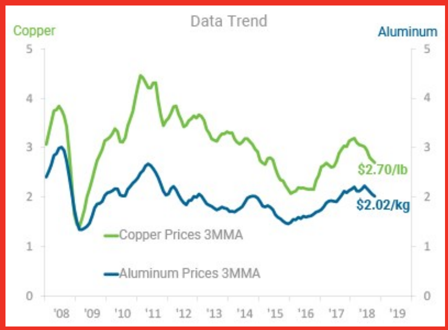
Timing and forecasting the stock market falls outside of our scope at ITR. However, we do watch the rate-of-change signals coming from the stock market as part of the broader macroeconomic picture, and the October dip has turned the cyclical momentum of the market in a negative direction. This situation is a bit different than the similar market turbulence that occurred in February and March of this year, as the leading indicators at that time were giving us more good news than bad for the economy. Now the signal from the S&P 500 is joining the preponderance of leading indicator evidence to suggest a downside, and it is consistent with our forecast of business-cycle decline characterizing 2019.

We do not think that this will be a full-fledged bear market because we do not expect GDP contraction to occur in 2019, which we think increases the likelihood that this is another correction taking place. It is consistent with the market risks that ITR speakers have been highlighting for audiences this fall, including a high CAPE ratio, an increasing percentage of companies issuing negative earnings per share guidance, and consistent weakness plaguing non-US equities prior to our domestic market struggles. Stay cautious.

Copper & Aluminum Prices

US Copper futures prices during the three months through October averaged $2.70 per pound, down 11.1% from the year-ago level. Chile total copper production is currently declining, but remains near the record-high level. Supply factors in Chile, the world's largest copper producer, suggest that prices will likely fall further during the next few quarters.

US aluminum futures prices averaged $2.02/kg, 4.6% below the year-ago level. The Trump administration imposed a 10% tariff on aluminum earlier this year that may keep prices above what supply and demand fundamentals would otherwise suggest. Please note that this tariff was not rescinded as part of the recent United States-Mexico-Canada Agreement. However, further slowing growth expected in the global economy, particularly in China, the world's largest consumer of aluminum, will likely limit demand for the metal. The United States' expected transition to the back side of the business cycle next year will likely only exacerbate this trend. Waning growth in industrial activity suggests that further downward pressure on prices is likely into 2019. With prices of both copper and aluminum expected to fall through much of next year, take caution before locking in input costs in the near term.

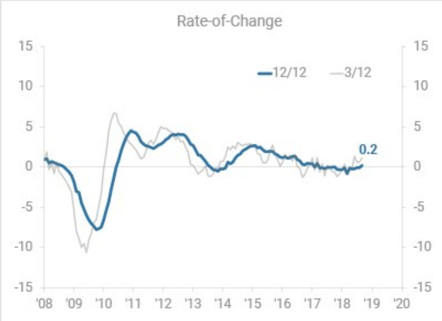


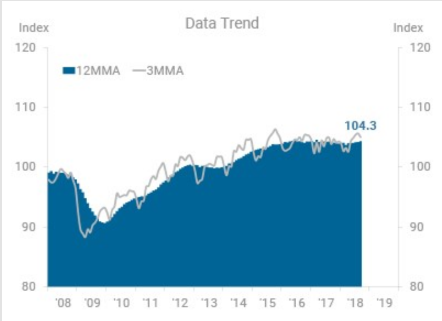
GLOBAL DEEP-DIVE

Mexico Industrial Production

Average Mexico industrial production during the 12 months ending in September was up 0.2% from the same 12-month period one year earlier. Production will be relatively flat in 2019, ending the year near the 2018 level.

The mining sector has been an area of weakness during the last several years, having contracted since early 2013. While Mexico mining production is currently recovering, this segment will likely continue to be a downward pull on the overall Mexican economy in the near term. Meanwhile, Mexico manufacturing production is expanding, up 1.7% from the year-ago level, but at a slowing pace. Mexico joined Canada and the United States to form a new trade agreement to replace NAFTA. This deal alleviates concerns over potential trade restrictions that would have likely constricted the Mexican economy in the long term. However, despite the agreement, do not plan for significant growth opportunities in Mexico in the near term. Take caution not to over-invest in this region for 2019.





Global Economic Outlook

	12-month Moving Avg	Chg. Over Prev. 12 Months	2018 YTD	2019 Projected	2020 Projected
Canada Industrial Production		4.0	3.6	-1.2	2.5
Mexico Industrial Production Index		0.2	1.7	-0.4	2.4
Brazil Manufacturing & Mining Industrial Production Index		2.7	2.2	-1.0	2.8
Western Europe Industrial Production Index		2.3	1.1	-1.3	1.4
Eastern Europe Industrial Production Index		4.7	3.5	-1.3	4.3
India Industrial Production Index		5.7	5.0	3.3	5.5
China Industrial Production Index		6.3	5.8	5.4	7.1

Note: Forecast color represents market projection at end of year.

Accelerating growth Recovery Slowing growth Recession