Industry Snapshots

Arrow denotes 12-month moving total/average direction.

RETAIL SALES	↗
WHOLESALE TRADE	↘
AUTO PRODUCTION	↗
MANUFACTURING	↘
ROTARY RIG	↘
CAPITAL GOODS	↗
NONRESIDENTIAL CONSTRUCTION	↑
RESIDENTIAL CONSTRUCTION	↘

↑	↗	→	↘	↓
Steep Rise	*Mild Rise*	*Flat*	*Mild Decline*	*Steep Decline*

Macroeconomic Outlook

Growth rate decline in the US economy persists. In September, the annual growth rate of US Total Manufacturing Production fell below zero, indicating year-over-year contraction in the manufacturing sector. US Industrial Production, buoyed by the oil and gas industry, has fared relatively better. However, Industrial Production is roughly 75% manufacturing, so it is likely to follow the path of Manufacturing Production in the near term.

On the consumer side, finances are beginning to show cracks. While still low, credit card delinquencies are rising, as is the percentage of cardholders making minimum payments. Additionally, inflation-adjusted savings balances are in decline. In aggregate, these factors point to a weaker consumer, a consumer unlikely to be able to keep the economy out of recession next year. Thus far, US Total Retail Sales have been resilient, but these and other leading indicators suggest rougher seas ahead.

Businesses too are seeing slowdowns. US Corporate Profits fell below year-ago levels in the second quarter, as did US Exports of Goods to the World. Corporate Bond Yields have not risen as quickly as US Treasurys, but Yields are rising, making borrowing more difficult. Taken in combination, these signals suggest businesses are likely to hold off on capital expenditures in the coming quarters. Lower capex combined with declining exports suggest that recession is on the horizon.

> *"On the consumer side, finances are beginning to show cracks."*

One important signal for recession next year is the US Treasury yield curve. The yield curve, which inverted late in 2022, is pointing to a recession in the US industrial sector beginning around the end of 2023 or the start of 2024. We are monitoring the yield curve, which remains inverted. Should the inversion extend beyond the end of 2023, it may pose a risk to the timing of our outlook for a rate-of-change low in US Industrial Production around the end of 2024.

While it is important to make plans for the coming downturn – like building a cash buffer, evaluating your vendors, and planning opportunities for scheduled downtime of equipment – you should also begin to look ahead to the rising trend coming in 2025. Are there new product lines you are looking to roll out or markets your business could enter? Do you have a long-term labor strategy to combat aging demographic trends? There will be opportunities for growth, so be sure you are prepared to take advantage of them.

Make Your Move

There was a lot of market share shift amid the supply chain constraints of recent years. Make a plan focused on maintaining any market share you gained or on regaining any share you may have lost.

Investor Update

The S&P 500 declined 4.9% in September as investors digested higher-for-longer interest rate probabilities. The declines in August and September signal that not all is well in the economy heading into 2024. The ITR Optimizer™, plus our trajectory toward a mild recession, points to the likelihood of elevated volatility.

ITR Economics Long-Term View

2023	2024	2025
SLOWING GROWTH	RECESSION	GROWTH

Leading Indicator Snapshot

	4Q2023	1Q2024	2Q2024
ITR Leading Indicator™	🔴	🟢	⚪
ITR Retail Sales Leading Indicator™	🔴	🔴	🔴
US OECD Leading Indicator	🟢	🟢	🟢
US ISM PMI (Purchasing Managers Index)	🔴	🔴	🟢
US Total Industry Capacity Utilization Rate	🔴	🔴	⚪

🟢 *Denotes that the indicator signals cyclical rise for the economy in the given quarter.*

🔴 *Denotes that the indicator signals cyclical decline for the economy in the given quarter.*

⚪ *N/A*

KEY TAKEAWAYS

- Recent rise in the ITR Leading Indicator™, US OECD Leading Indicator, and the US ISM PMI (Purchasing Managers Index) may be calling for an earlier-than-forecasted low for the US Industrial Production rate-of-change. At this time, however, we still anticipate a US Industrial Production rate-of-change low around year-end 2024. This is supported by the preponderance of economic evidence, including other leading indicators with longer lead times, a still-inverted yield curve, softer consumer financials, and tightening commercial and industrial credit conditions.
- The ITR Retail Sales Leading Indicator™ is rising, but more data is needed to confirm whether the June reading represents a low. Prior decline in the Indicator suggests the US Total Retail Sales rate-of-change will decline into at least the second quarter of 2024, in line with our outlook.
- The US Total Industry Capacity Utilization Rate moved horizontally in September, but general decline is the dominant trend. This signals downward cyclical movement for the US industrial sector through at least the first quarter of 2024.

Industry Analysis

RETAIL SALES

- Annual US Total Retail Sales in September were $8.257 trillion, up 4.0% from one year ago
- Inflation-adjusted annual Retail Sales are at a record high, but are growing at a slower than normal rate
- High interest rates and the cumulative impact of inflation will put downward pressure on Retail Sales in the coming quarters

WHOLESALE TRADE

- Annual US Total Wholesale Trade has been falling since March 2023
- Inventories are outpacing sales, particularly for durable goods, which tend to be more interest rate sensitive
- Expect further decline in Wholesale Trade next year

AUTO PRODUCTION

- Annual North America Light Vehicle Production has tentatively transitioned to a slowing growth trend, but is still 13.2% above the year-ago level
- At the time of this writing, the UAW workers strike is still ongoing and could impact Production in the near term
- Due in part to the shifting of consumer financials and high interest rates, we expect demand, and therefore Production, to decline mildly in 2024

MANUFACTURING

- Annual US Total Manufacturing Production in September was 0.2% below the year prior
- Decline in Manufacturing Production is being driven by decline in the nondurable goods component
- The durable goods component remains in a mild rising trend

ROTARY RIG

- The US Rotary Rig Count in the third quarter was 14.5% below the third quarter of 2022
- While Oil Production is rising, producers are trying to squeeze much of this out of existing capacity
- Material and labor shortages combined with the regulatory environment may disincentivize some exploration activity

CAPITAL GOODS NEW ORDERS

- US Nondefense Capital Goods New Orders in the 12 months through August were 2.6% above the same period one year ago
- Declining US Corporate Profits and the easing inflationary environment are putting downward pressure on dollar-denominated New Orders
- Decline in annual New Orders is expected to begin imminently

TOTAL NONRESIDENTIAL CONSTRUCTION

- Annual US Total Nonresidential Construction in August was 16.0% above the year-ago level
- Decline in the US Architectural Billings Index suggests that a slowing growth trend for Construction is imminent
- Elevated interest rates and tightening credit standards will put downward pressure on Construction

TOTAL RESIDENTIAL CONSTRUCTION

- Annual US Total Residential Construction, denominated in dollars, is below year-ago levels and declining
- Annual Multi-Family Residential Construction is rising, while Single-Family is declining
- Permitting activity portends upcoming decline in Multi-Family Construction and rise in Single-Family Construction

A Closer Look: The US Economy

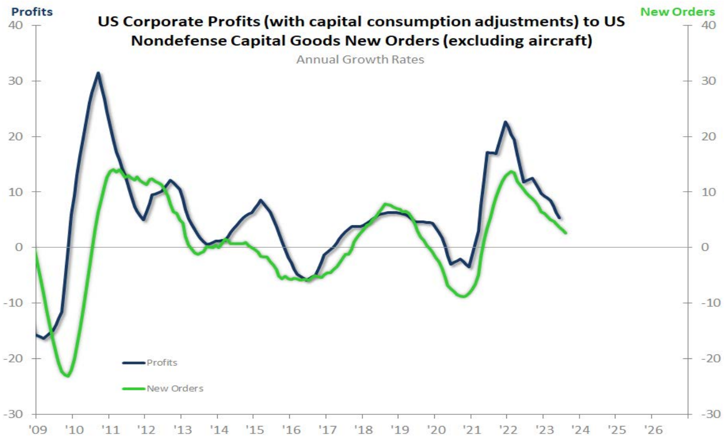
Where Did All the Profits Go?

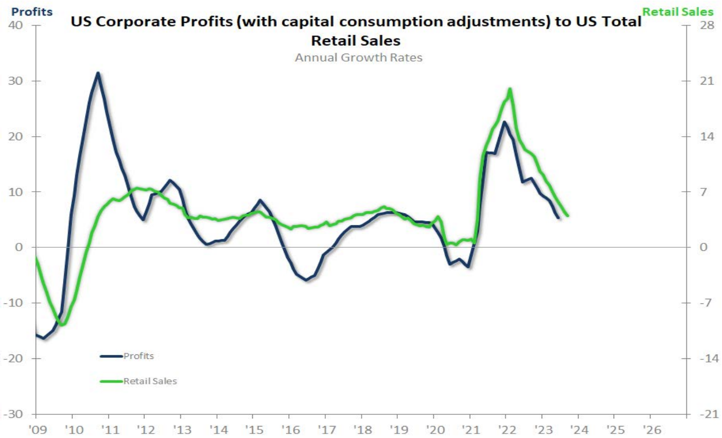
JACKIE GREENE

What you need to know: Decline in Corporate Profits does not have to mean decline in your profits

Profits are key for every business to track and strive to maximize. Profits within a business help to fuel future investment and make all the hard work of running a business worthwhile for the stakeholders. It is also important to look at profits from a broader economic perspective. Just like in your business, declining profits in the overall economy can limit future investment.

Start by looking at a broad measure of profits, like US Corporate Profits. Annual Corporate Profits fell during the second quarter, the first such decline in Profits since the COVID-induced decline in the first half of 2020. Corporate Profits have a strong historical relationship to US Nondefense Capital Goods New Orders and US Total Retail Sales, which means that this decline in Corporate Profits spells trouble for future spending in both the B2B and the consumer sides of the economy.





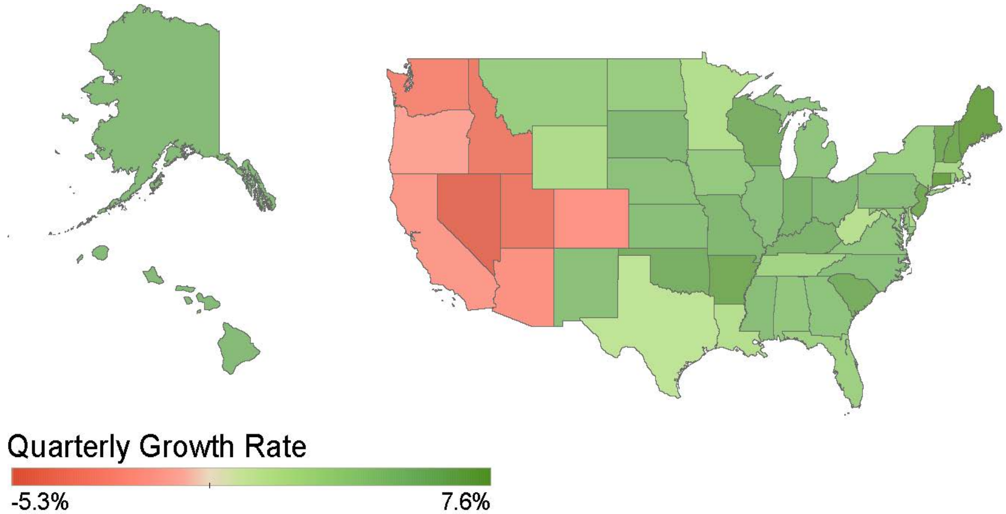
The decline in Corporate Profits is being driven by both higher costs and lower demand. On the costs side, prices for most components and finished goods are much higher than their pre-pandemic norms, and higher wages are a major contributing factor to higher variable costs. Slowing or declining demand in most end-use markets also means less top-line Revenue generated through volume is coming in to support a business's fixed costs.

What can you do about it?

1. Evaluate your costs. Can you negotiate prices with your suppliers?
2. Watch wage pressures. The Consumer Price Index will rise a relatively muted 1.6% in 2024. Use this number when discussing wage increases.
3. Lose the losers. If established business segments are not profitable during this phase, eliminate them.
4. Plan for it. If you are heading into a recession that will impact the volume of work coming in, acknowledge it and do not expect volume to carry you through. You can maintain profitability even during a recession if you take the appropriate steps.

Keep in mind that we have been talking about US Corporate Profits on the whole. Not all segments of the economy move in sync. US Machinery Industries Corporate Profits are up 78.7% from the prior year, while Domestic Financial Industries Corporate Profits are down 9.7% over the same time period. Track the corporate profits trends for your industry to get insights into future business investment in your industry and to have a benchmark for your business.

State-by-State: Prices



- US Home Prices in the 12 months through July were 6.2% above the year-ago level.
- However, Home Prices are not rising throughout the entire country; year-over-year decline in quarterly Prices is occurring in much of the western region of the US.
- This year-over-year decline is occurring in eight states and the District of Columbia.
- Some green shoots are visible in the housing market; permits and housing starts are showing signs of life. This would typically signal some easing in Prices on the horizon as the supply of homes increases.

Readers' Forum

With regard to the United Auto Workers strike that began in September, how does ITR Economics think it will impact the macroeconomy this year?

Jenna Allen, Economist at ITR Economics™, answers:

The ongoing UAW strike involves a targeted work stoppage strategy, rather than a complete stop on production, at three major US automakers. These automakers account for around 50% of US automobile production. We could see minor downside pressure on US automobile production and a slight near-term uptick in steel scrap prices, but the strike is currently unlikely to have a significant impact on our forecasts. If the strike is prolonged, there could be additional risks. Stand by for updates as the situation develops.

Please send questions to: questions@itreconomics.com

