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SupplyDynamics Market Insight

August 2018

Economy Added Disappointing 157,000 Jobs in July But Unemployment Fell to 3.9%—Hiring slowed in July as employers added 157,000 jobs in a possible sign that worker shortages and widening U.S. trade spats are starting to damp employment gains.

The unemployment rate fell from 4% to 3.9%, close to its 18-year low, the Labor Department said August 3. As a result of the low unemployment rate, more businesses are struggling to find workers, especially with the economy growing at the fastest pace in three years in the April-June period. Full Story
Source: USAToday, 08.03.18

Consumer Confidence Rises Above Expectations in July—Consumer confidence gained more than expected in July, but consumers remained concerned about future economic growth. The Confidence Board's index increased to 127.4 in July, beating an estimated 126.5 by Reuters economists. The index was up from a disappointing revised reading of 127.1 in June, sunken by lower income prospects. Consumers reported better feelings toward the current economic situation; however, they were not optimistic about long-term growth.

"Consumers' assessment of present-day conditions improved, suggesting that economic growth is still strong," said Director of Economic Indicators at The Conference Board Lynn Franco. "However, while expectations continue to reflect optimism in the short-term economic outlook, back-to-back declines suggest consumers do not foresee growth accelerating."

The survey measures American's sentiment on current economic conditions and prospects for the next six months, including business and labor market conditions. Since consumer spending accounts for about 70% of U.S. economic activity, economists' pay close attention to the number.
Source: CNBC, 07.31.18

G.D.P. Grew at 4.1% Rate in U.S. in Last Quarter—Here's what that means. The Commerce Department released its initial estimate of second-quarter economic growth on July 27, providing the latest snapshot of the American economy.

- U.S. gross domestic product rose at an annual rate of 4.1% in the second quarter, up from 2.2% in the first three months of the year. It was the strongest quarter of growth since 2014.
- Consumer spending rose 4%, but private investment fell slightly as the housing market cooled.
- Exports rose 9.3%, driven in part by a surge in soybean shipments tied to President Trump's trade policies.
- Consumer prices rose at a 1.8% annual rate.

Economic growth surged in the second quarter. The second-quarter acceleration was widely anticipated by economists, a result of a confluence of events unlikely to recur. Most economists expect growth to slow in the second half of the year. Still, recent data does suggest that the pace of growth has picked up this year. Some economists think full-year growth in gross domestic product could hit 3% in 2018 for the first time in the nearly decade-long recovery, a prospect that became more likely following July 27 strong numbers.
Full Story *Source: NYTimes, 07.27.18*

Orders for U.S. Capital Equipment Raise for Third Straight Month

Orders placed with U.S. factories for business equipment increased in June for a third straight month, a sign of investment momentum heading into the second half despite corporate concerns over tariffs, Commerce Department figures showed June 26. Non-military capital goods orders excluding aircraft rose 0.6% month over month (estimated 0.5% gain) after advancing an upwardly revised 0.7% the prior month; the figure is proxy for business investment. Shipments of those goods, used to calculate gross domestic product, rose 1% (estimated 0.4% increase) after a 0.2% increase.

Bookings for all durable goods, or items meant to last at least three years, rose 1% (estimated 3% advance) following 0.3% decrease (prev. 0.4% drop).

Key Takeaways—The miss in durable-goods orders may at least partly reflect seasonal adjustments around bookings for aircraft and parts, typically a volatile category, which for civilian equipment rose 4.3% after an 11.6% drop in May, according to the report. Defense aircraft and parts orders advanced 20.2% following a 36.1% gain.

Unadjusted figures for the categories showed much bigger increases in June. Boeing Co. previously said that the plane maker received 233 orders in June, up from 43 in May.

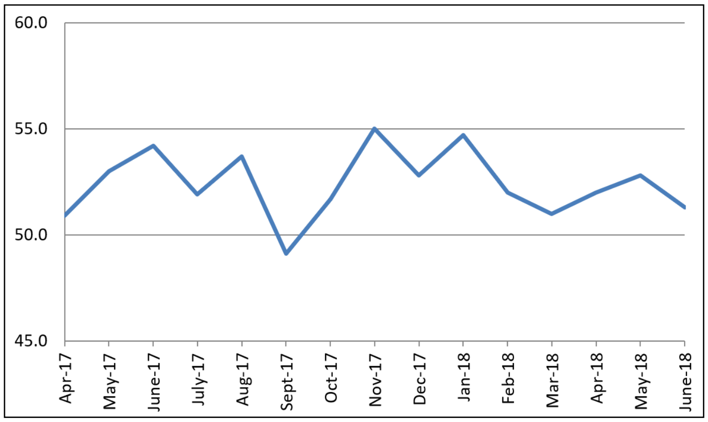
The gain in business-equipment orders included increases in computers and electronic products, along with electrical equipment, appliances and components. Machinery and fabricated-metal products also showed smaller pickups, while orders for primary metals declined for a second month.

The latest data signal business investment remains firm even as President Donald Trump widens a global trade war beyond steel and aluminum and into a growing range of products from China, as well as potential levies on autos.

Business spending, which is getting a boost from lower corporate taxes, is one of the factors supporting a projected pickup in second-quarter economic growth.
Full Story *Source: IndustryWeek, 07.26.18*

Key Economic Indicators

Architecture Billings Index

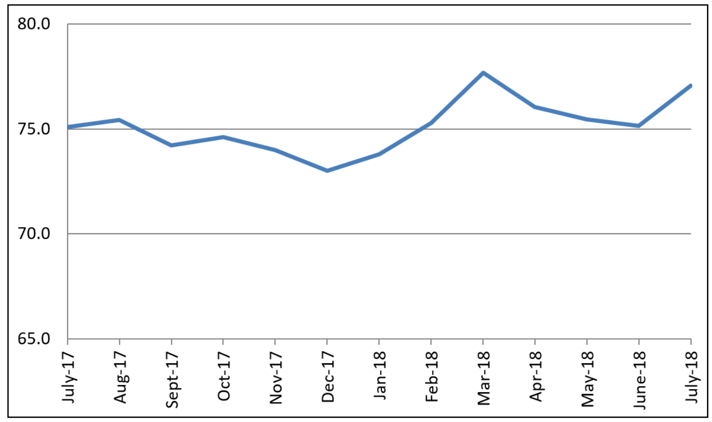


Architecture firm billings slowed in June but remained positive for the ninth consecutive month, according to a new report today from The American Institute of Architects (AIA).

AIA's Architecture Billings Index (ABI) score for June was 51.3 compared to 52.8 in May, which is positive since any score over 50 represents billings growth. As a result, June's ABI shows that demand for architecture firm services continues to improve across all sectors..

The **Architecture Billings Index (ABI)** is a diffusion index derived from the monthly Work-on-the-Boards survey, conducted by the AIA Economics & Market Research Group. The ABI serves as a leading economic indicator that leads nonresidential construction activity by approximately 9-12 months. An index score of 50 represents no change in firm billings from the previous month, a score above 50 indicates an increase in firm billings from the previous month, and a score below 50 indicates a decline in firm billings from the previous month.
Source: American Institute for Architects, 07.18.18

Steel Capability Utilization

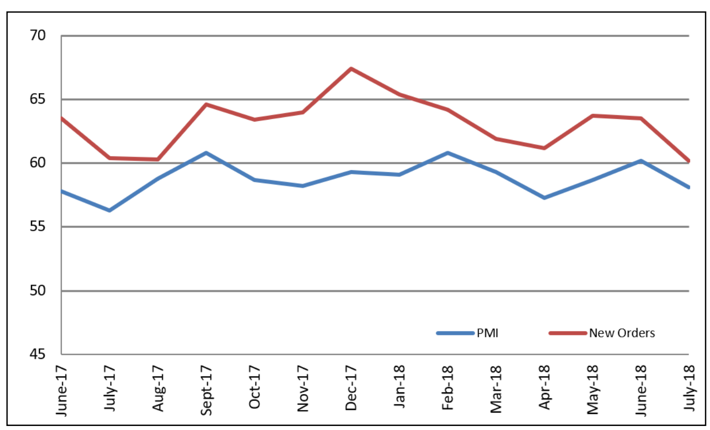


In the week ending on July 28, domestic raw steel production was 1,836,000 net tons while the capability utilization rate was 78.3%. Production was 1,733,000 net tons in the week ending July 28, 2017 while the capability utilization then was 74.3%. The current week production represents a 5.9% increase from the same period in the previous year. Production for the week ending July 28, 2018 is up 1.2% from the previous week ending July 21, 2018 when production was 1,815,000 net tons and the rate of capability utilization was 77.4%.

Adjusted year-to-date production through July 28, 2018 was 53,356,000 net tons, at a capability utilization rate of 76.4%. That is up 3.1% from the 51,770,000 net tons during the same period last year, when the capability utilization rate was 74.4%.

Steel Capability Utilization is a domestic report based on estimates from companies representing approximately 90% of the Industry's Raw Steel Capability as compiled by the American Iron and Steel Institute. *Source: AISI, 07.28.18*

Purchasing Managers Index®



The July PMI® registered 58.1%, a decrease of 2.1 percentage points from the June reading of 60.2%. The New Orders Index registered 60.2%, a decrease of 3.3 percentage points from the June reading of 63.5%. The Production Index registered 58.5%, a 3.8 percentage point decrease compared to the June reading of 62.3%. The Employment Index registered 56.5%, an increase of 0.5 percentage point from the June reading of 56%. The Supplier Deliveries Index registered 62.1%, a 6.1 percentage point decrease from the June reading of 68.2%. The Inventories Index registered 53.3%, an increase of 2.5 percentage points from the June reading of 50.8%. The Prices Index registered 73.2% in July, a 3.6 percentage point decrease from the June reading of 76.8%, indicating higher raw materials prices for the 29th consecutive month.

Of the 18 manufacturing industries, 17 reported growth in July, in the following order: Textile Mills; Electrical Equipment, Appliances & Components; Apparel, Leather & Allied Products; Computer & Electronic Products; Petroleum & Coal Products; Paper Products; Printing & Related Support Activities; Nonmetallic Mineral Products; Machinery; Plastics & Rubber Products; Miscellaneous Manufacturing; Fabricated Metal Products; Food, Beverage & Tobacco Products; Furniture & Related Products; Chemical Products; Wood Products; and Transportation Equipment. The only industry reporting a decrease in July is Primary Metals.
Source: Institute for Supply Management, 08.01.18

Industry News

Chairman Shuster Releases Infrastructure Proposal

On July 25, U.S. House Transportation and Infrastructure Committee Chairman Bill Shuster (R-PA) released his long-awaited infrastructure discussion draft. Key components of the plan include fixing the Highway Trust Fund (HTF), investing in transportation and water resources infrastructure, financing innovative projects, and accelerating project delivery.

The plan also calls for an increase of 15 cents per gallon of gasoline and 20 cents per gallon of diesel to the existing federal gas tax while extending HTF expenditure authority to September 30, 2021.

Additionally, the draft proposes ending the gas tax as a revenue raised in 2028, as a means to encourage Congress to identify and pass another funding solution by then. While providing an incentive to implement an alternative, this is also a risk if there is not a bill passed with a new funding mechanism.

The proposal aims to address long-term HTF solvency by establishing a HTF Commission, which will submit a report to Congress that includes new recommendations to achieve solvency, which cannot include a motor fuels tax increase. This proposal will include a provision allowing for expedited consideration of the legislation by Congress.

Other transportation investment recommendations include awarding 30% of BUILD (formally known as TIGER) grants to projects in rural areas and expand program access; extending FAST Act authorization through fiscal year (FY) 2021 and repealing rescissions included in that law. Full Story

Source: InfrastructureReportCard, 07.25.18

E.U. Steel Consumption Up 3% in Q1 2018

The European Union (E.U.) posted a 3% increase in apparent steel consumption during Q1 2018 compared with Q1 2017, according to a recent European Steel Association (EUROFER) report. According to EUROFER, the E.U. steel market began 2018 on "relatively strong footing," but that rising trade tensions could knock the sector off course.

"The latest data confirms the severe impact the US Section 232 tariffs are having by deflecting imports into the EU – with surges across almost all product lines," said Axel Eggert, EUROFER director general, in a release. "This surge is occurring at the same time as growth predictions are being revised onto flatter trajectories. We cannot risk the ongoing recovery being put at stake– and welcome the recent EU safeguard in its efforts to stabilize the sector."

According to the report, real steel consumption and seasonal restocking are factors explaining the 3% rise in apparent consumption during Q1. Domestic deliveries to the E.U. market rose 2.1% during the aforementioned period. Meanwhile third-country imports rose by 9.8% to 10 million tons, hitting the highest quarterly total since Q3 2007, according to EUROFER.

"This confirms that the volume effects of anti-dumping measures imposed by the European Commission over the course of 2017 faded out rapidly due to other third country suppliers filling the gap left by the countries which had duties applied to them," the report states. As for steel demand, the EUROFER report projects growth to continue in 2018 and 2019, but notes the uncertainty of "international steel fundamentals."

"The sharp rise in imports of specific steel product from some third countries confirms that steel trade distortions remain a threat, which could be exacerbated by trade deflection resulting from the Section 232 tariffs applied by the Trump administration," the report argues.

Other highlights from EUROFER:

- In Q1 2018, all steel-using sectors in the E.U. posted production growth (except for steel-tube manufacturing).
- Production activity is forecast to grow 2.8% in 2018 and 1.9% in 2019.
- Economic growth in the E.U. fell to 0.4% quarter-on-quarter in Q1 2018, down from 0.7% in Q4 2017.

Source: MetalMiner, 07.25.18

Industry News

BP's Biggest Deal Since 1999 Scores Prized BHP U.S. Shale Assets

BP Plc agreed to pay $10.5 billion, its biggest acquisition in almost two decades, for most of BHP Billiton Ltd.'s onshore U.S. oil and natural gas assets, including in the prized Permian Basin. The deal gives the London-based energy giant a position in the Permian, a swath of west Texas and New Mexico that's the world's fastest-growing major oil region. It's another sign that BP has mostly rebounded from crude's price crash and the fatal 2010 accident in the Gulf of Mexico that left it with a more than $60 billion bill. "We've just got access to some of the best acreage in some of the best basins in the onshore U.S.," BP's Upstream Chief Executive Officer Bernard Looney said in a statement. The Permian produces about 3.4 million barrels a day, which would make it the fourth-largest member of OPEC, behind Saudi Arabia, Iraq and Iran. To sweeten the deal for its investors, BP will lift its dividend by 2.5% in the second quarter, the first increase since 2014. Still, the shares reacted negatively to the transaction, falling as much as 2.4% in London. BHP gained 2.3% in Sydney. The miner appears to have got the better side of the deal, selling the entire package of assets for a higher price than expected, RBC analyst Biraj Borkhataria said in a note.

Rising oil prices have boosted prospects for shale deals, while the Permian is a focus for industry consolidation as technological advances allow explorers to drill ever-longer sideways wells. Concho Resources Inc. agreed in March to acquire RSP Permian Inc., while Exxon Mobil Corp. bought drilling rights for about $6 billion last year. "The Permian is the largest U.S. shale play with the most inventory so it's not hard to see the long-term attraction," said Leo Mariani, an Austin-based analyst at NatAlliance Securities LLC.BP's deal will also give it positions in the Eagle Ford and Haynesville basins in Texas and Louisiana.

In the aftermath of the 2010 Deepwater Horizon catastrophe, which spilled oil into the Gulf of Mexico, BP sold acreage and infrastructure in the Permian, missing out on the region's recent output boom. The deal with BHP underlines BP's increasing confidence that it's nearing the end of claims, fines and penalties related to the incident. The deal is a "transformational acquisition," BP's CEO Bob Dudley said in the statement, and will add current production of about 190,000 barrels of oil equivalent a day and discovered resources of 4.6 billion barrels of oil equivalent. Acquiring the operations will give BP access to wells that pay back in months rather than the years common in bigger offshore projects.

"Shale has been a problem child, so it's good to finally resolve that," said Sydney-based Andy Forster, senior investment officer at Argo Investments Ltd., which holds BHP and manages more than $5 billion (U.S. $3.7 billion). "It's a pretty good price too." BP was among as many as 60 companies that participated in the first round of bidding for BHP's assets, Dudley said in June. BHP also drew initial offers from separate partnerships headed by Chevron Corp. and Royal Dutch Shell Plc, people familiar with the process said in June.The sale process has been completed faster, and at a higher price, than some had expected, Melbourne-based RBC Capital Markets analyst Paul Hissey said in a note. RBC had forecast BHP would garner about $8 billion for the assets, while UBS Group AG expected about a $10 billion sale. Completion of the deal may "provide the clear air for a refresh of the executive management group," he said.

Source: IndustryWeek, 07.27.18

Worker Pay Rate Hits Highest Level Since 2008

Compensation for workers rose to a nearly 10-year high in the second quarter as inflation pressures continued to percolate in the U.S. economy. The employment cost index increased 0.6% for civilian workers in the three-month period ending in June, according to a Bureau of Labor Statistics release July 31. That brought the 12-month rate up to 2.8%, the highest level since 2.9% in the third quarter of 2008, amid the financial crisis and the Great Recession.

Significant wage gains have been a missing part of the economic recovery, with average hourly earnings increases barely keeping pace with inflation.

However, the ECI has been on a steady rise over the past year and a half. The index had struggled to stay above 2% for most of the period following the recession as the Federal Reserve kept interest rates low and inflation stayed well below historical norms. However, the index has been climbing steadily from the 2.2% level just prior to President Donald Trump taking office.

"With the labor market tightening, stronger wage pressures should continue to feed through into higher inflation over the rest of this year," Andrew Hunter, U.S. economist at Capital Economics, said in a note.

The index draws from a sample of 27,200 observations of some 6,600 private businesses as well as 8,000 observations from 1,400 government offices.

Wages and salaries rose 0.5% for the quarter and 2.8% for the 12-month period, while benefits costs increased 0.9% and 2.9%, respectively.

Private industry compensation was up 2.9%, a substantial rise from the 2.4% recorded as of June 2017. Government compensation increased 2.3% for the period, which actually was a pullback from the 2.6% gain recorded in June 2017.

Industry-wise, sales and related jobs recorded a 3.5% gain while transportation and material moving rose 3.4%. Full Story

Source: CNBC, 07.31.2018

David Paul Morris | Bloomberg | Getty Images

Special Section: Tariffs

U.S. Talks With Mexico on New NAFTA Near Completion, Ross Says

President Donald Trump has indicated that his administration may pursue a bilateral deal with Mexico first before negotiating separately with Canada. Negotiations with Mexico on an update to the North American Free Trade Agreement are going well and may be close to wrapping up, U.S. Commerce Secretary Wilbur Ross said. "Our immediate, most close-to-completion negotiations are with NAFTA, particularly with Mexico," Ross said July 30 at a conference in Washington, adding that President-elect Andres Manuel Lopez Obrador has "wasted no time" appointing a new trade team. "There's a pretty good chance that we could be on a pretty rapid track with the Mexican talks." The Mexico peso extended gains during Ross's comments and was up 0.7% against the dollar at 10:21 a.m. New York time.

U.S. Trade Representative Robert Lighthizer said last week that the Trump administration is hopeful that NAFTA talks are in the "finishing stages." Negotiations to modernize the deal started in August last year. President Donald Trump also said this month that the U.S. is making solid progress in talks with Mexico, but has indicated that his administration may pursue a bilateral deal with that country first before negotiating separately with Canada. Such a move would upend the decades-old trilateral NAFTA deal and likely stretch out negotiations far longer. Lopez Obrador, who takes office in December, has said he wants to keep the trilateral structure of NAFTA in place.

The current Mexican administration, the Canadian government as well as members of the U.S. Congress have said they support a trilateral structure for NAFTA. ***Source: Bloomberg, 07.30.18***

China Vows Retaliation if Trump Slaps 25% Tariff on $200 Billion of Chinese Imports

China said on August 1 that "blackmail" wouldn't work and that it would hit back if the United States takes further steps hindering trade, as the Trump administration considers slapping a 25% tariff on $200 billion worth of Chinese goods. The proposal would increase the potential tariff rate from 10% the administration had initially put forward on July 10 for that wave of duties in a bid to pressure Beijing into making trade concessions, a source familiar with the plan said on July 31. The tariffs target thousands of Chinese imports, including food products, chemicals, steel and aluminum and consumer goods. While the duties would not be imposed until after a period of public comment, raising the proposed level to 25% would escalate the already bitter trade dispute between the world's two biggest economies.

The source said President Trump's administration could announce the tougher proposal as early as August 1 in Washington. The plan to more than double the tariff rate was first reported by Bloomberg News. China, which has accused the United States of bullying, again vowed to retaliate if Trump proceeds with the measures, warning that pressure tactics would fail. "U.S. pressure and blackmail won't have an effect. If the United States takes further escalatory steps, China will inevitably take countermeasures and we will resolutely protect our legitimate rights," Chinese Foreign Ministry spokesman Geng Shuang told a regular news briefing.

Investors fear an escalating trade war between Washington and Beijing could hit global growth, and prominent U.S. business groups, while weary of what they see as China's mercantilist trade practices, have condemned Trump's aggressive tariffs. Representatives of U.S. Treasury Secretary Steven Mnuchin and Chinese Vice Premier Liu He have been speaking privately as they seek to restart negotiations to defuse the budding trade war, Bloomberg reported, citing sources. A spokeswoman for the U.S. Trade Representative's Office declined to comment on the proposed tariff rate increase or on whether any changes would alter the deadlines laid out for comment period before implementation.

In early July, the U.S. government imposed 25% tariffs on an initial $34 billion of Chinese imports. Beijing retaliated with matching tariffs on the same amount of U.S. exports to China.

Special Section: Tariffs

China Vows Retaliation (continued)

Washington is preparing to also impose tariffs on an extra $16 billion of goods in coming weeks, and Trump has warned he may ultimately put them on over half a trillion dollars of goods—roughly the total amount of U.S. imports from China last year. The $200 billion list of goods targeted for tariffs— which also include Chinese tilapia fish, printed circuit boards and lighting products - would have a bigger impact on consumers than previous rounds of tariffs.

Erin Ennis, senior vice president of the U.S.—China Business Council, said a 10% tariff on these products is already problematic, but more than doubling that to 25% would be much worse. "Given the scope of the products covered, about half of all imports from China are facing tariffs, including consumer goods," Ennis said.

"The cost increases will be passed on to customers, so it will affect most Americans' pocketbooks." Trump had said he would implement the $200 billion round as punishment for China's retaliation against the initial tariffs aimed at forcing change in China's joint venture, technology transfer and other trade-related policies. He also has threatened a further round of tariffs on $300 billion of Chinese goods.

The U.S. Trade Representative's office initially had set a deadline for final public comments on the proposed 10% tariffs to be filed by Aug. 30, with public hearings scheduled for Aug. 20-23. It typically has taken several weeks after the close of public comments for the tariffs to be activated. ***Source: CNBC, 08.01.18***

Trump Relents on EU Car Tariffs, as U.S.—China Fight Derails Qualcomm Deal

In what the EU chief called a "major concession," U.S. President Trump agreed on July 25 to refrain from imposing car tariffs while the two sides launch negotiations to cut other trade barriers, easing the threat of a transatlantic trade war. After a meeting at the White House, Trump and European Commission President Jean-Claude Juncker said the talks would also seek to "resolve" U.S. tariffs on steel and aluminum and Europe's retaliatory duties - marking a step back from Trump's signature import protections for American metals producers. The breakthrough came as the bitter trade dispute between the U.S. and China appeared to claim a major casualty, with China not approving U.S. chipmaker Qualcomm Inc's (QCOM.O) takeover of NXP Semiconductors (NXPI.O), likely shutting the door on the $44 billion deal. Qualcomm needed Beijing's okay because China accounts for nearly two-thirds of its revenue, but a deadline at midday on July 26 in Asia passed without word from China's regulator. Qualcomm had said on July 25 it was dropping the bid.

Trump said Europe agreed to increase purchases of U.S. liquefied natural gas and lower trade barriers to American soybeans, aiding U.S. farmers and the energy sector. "Soybeans is a big deal. And the European Union is going to start, almost immediately, to buy a lot of soybeans," Trump told reporters after the meeting. Trump later tweeted that work on documents was "moving along quickly," adding that the meeting with Juncker had "great warmth." "A breakthrough has been quickly made that nobody thought possible!" Trump wrote, marking a turnaround from July 15, when he called the 28-nation European Union a "foe" on trade. Juncker said the two sides agreed that as long as they were negotiating on trade, they would hold off on further tariffs, including potential U.S. tariffs on cars and auto parts. He later told reporters that was a "major concession" on Trump's part and that he expected the U.S. president to follow through on it.

U.S. import tariffs of 25% on steel and 10% on aluminum imposed in March will remain in place during the talks, but Juncker added: "It is the first time that the Americans agreed to reassess the measure that they have taken in the steel and aluminum sector." European governments and EU officials hailed the Trump-Juncker agreement as a major success. "Breakthrough achieved that can avoid trade war and save millions of jobs! Great for global economy," tweeted German Chancellor Angela Merkel's economy minister, Peter Altmaier. The Alliance of Automobile manufacturers, a trade group representing both domestic and foreign-brand automakers, welcomed the agreement to hold talks instead of impose tariffs, saying the announcement "demonstrates that bilateral negotiations are a more effective approach to resolving trade barriers, not increasing tariffs."

Trump and Juncker said the U.S.—EU talks would seek to eliminate tariffs, trade barriers and subsidies for non-automotive industrial goods, and cut barriers to transatlantic trade in services, chemicals, pharmaceuticals and medical products. They also said they would cooperate to reform the rules of the World Trade Organization, which the Trump administration frequently criticizes for favoring U.S. trading partners. Trump's threat to impose tariffs on auto imports on national security grounds would hit European carmakers BMW (BMWG.DE) Daimler (DAIGn.DE) and Volkswagen (VOWG_p.DE) as well as Japanese and South Korean car companies.

The Commerce Department could recommend new tariffs as early as September after an investigation into whether car imports posed a risk to U.S. national security. The two leaders did not specifically mention car tariffs in their statements, keeping the focus on other industrial products.
Source: Reuters, 07.26.18