Precision Machining Industry Prognostications: How'd We Do?

By Miles Free – Director of Industry Research and Technology

Before we make our predictions for the coming year, perhaps a brief review of what we thought was ahead last year might be in order. In July 2017, we committed in this space in an article entitled "Precision Machining Industry Outlook: You Should Be Bullish, Too." Then in February 2018, our Craftsman's Cribsheet, "A Cribsheet for 2018," was published in these pages. Let's take a look at how we did.

Precision Machining Industry Outlook: You Should Be Bullish, Too

Let's just jump to our conclusion:

"What's our take? Economic expansion and recovery is once again underway. The list of positive indicators that point to higher industrial activity in 2017 is growing. PMPA's own indicators for shipments, lead times, employment are positive at 96 percent of respondents expecting employment to remain the same or increase in the next three months and profitability all point to 'manufacturing optimism' at this time. The Labor Force Participation Rate is finally recovering, but something has changed. The risk that we face in our shops has declined. Have you changed your outlook based on the view of these facts?"

Today, our comment is, "Boy is it! At the time we wrote the 2017 piece, our June Business Trends Index had just hit a near record at 135, three months after achieving an all-time high of 137 in March 2017. PMPA's August Business Trends report in 2018 came in at 143, tying the new all-time high record set in March 2018. August 2018 was up 9.2 percent over August 2017. Demand remains strong, for August sales to tie March, typically our industry's strongest month. It is really a bellwether event."

To what did we attribute our belief in a positive 2018? Three key factors: end of hostile regulatory enforcement, tax reform and market indicators.

End of Hostile Regulatory Enforcement

We said, "*The de-emphasis of hostile enforcement by the regulatory agencies under the new administration is a convincing reason to consider again the opportunities to grow and invest in our shops.*" What made that happen? The president's unprecedented pledge for regulatory rollback, eliminating two existing regulations for every new

regulation yielded approximately $8.1 billion in lifetime regulatory savings, with more than another $9 billion expected in 2018.

Tax Reform

We mentioned tax reform. In a bit of understatement, we said, "Tax Reform is another positive indicator that seems to bode well for our prospects in the coming year."

The Tax Cuts and Jobs Act signed in December 2017 was the first major overhaul of the federal tax code in three decades. That it encouraged U.S. manufacturing is borne out by the sales records in our business trends reporting, already mentioned above. And the successful IMTS in Chicago, which set records for most exhibit space and highest number of exhibitors and booths.

Market Indicators

"*Our shops serve many markets, and the outlook for many of them is quite positive as well. Some market indicators that bode well for our industry include the PMPA Business Trends Shipments index, which recently hit a new all-time high of 138. The index was 100 for calendar year 2010.*

The Housing Market Index hit a 12-year high, its highest since June 2005. Many precision parts are involved in the equipping of homes with appliances, HVAC, electronics

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and not to mention the vehicles and tools purchased by the builders as their business expands. Single-family housing starts jumped from 819,000 to 872,000 earlier this year, a pace unseen since February 2007.

Retail sales remain high, 5.7 percent to 6.0 percent, the highest year-over-year performance since 2012.

Specific market sectors that appear to be level or growing this year include U.S. housing starts, industrial machinery new orders, industrial production and North American light vehicle production."

A Cribsheet for 2018

New Technology

In our February cribsheet, we thought new technology was in store for our shops in 2018. The record-setting IMTS Conference affirms that, and the number of PMPA shops I know working on robotics projects cements that one as a win.

Training

I wish we could say training was in the win column, but frankly, we are calling it a miss. Who would have thought our shops would be too busy to train? I certainly didn't. On the plus side, the participation in Mfg Day by our shops continues to grow, and the number of Student Summit attendees at IMTS is another indicator that this one is still cooking.

Increased Working Capital

I don't have a lot of insight into this, but our colleagues at Gardner Business Capital Spending Report are on record as saying, "Machine consumption increased 3 and 6 percent in 2017 and 2018, respectively." Spoiler alert: They see machine tool consumption increasing 11 percent to $7.748 billion in 2019. We'll take it!

What We Missed

We had been working on the tariff issues since early in 2017 and even met with Commerce Department Secretary Wilbur Ross in July 2017. We knew the tariffs issue was important, but we had no idea of how it would impact our industry. I'm not so sure we understand it any better today, either.

The Year Ahead

So, what do we think is in store for 2019? Despite the record level of sales our shops are producing in 2018, several of our most important markets have been in slowing growth or even recession. U.S. housing starts, North American heavy truck, U.S. industrial new orders have been in a slowing growth phase, while U.S. aircraft and parts production was in a recession, down 2.2 percent year to date and expected to be negative 3.5 percent for the calendar year.

Our Business Trends Reports so far this year show precision machining to be overachievers at 111-percent of 2017 year-end average for sales.

Our economists have walked the dire "recession in 2019" of a couple years ago, back to a more nuanced, "soft landing in 2019."

What do we think? As much as we'd like to say recent records are a positive sign, such as record GDP growth, record stock prices and record lows in unemployment, it is difficult to make the case that these will be positive factors in the year ahead. Reversion to the mean is far easier to expect than to make up some story as to how our current record workforce shortage is somehow a positive for our short-term future employment, and thus, increased production and increased sales.

The actions of the Federal Reserve to remove liquidity will play an outsized role in limiting availability of capital and, coupled with continued fiscal deficits, will remove liquidity and savings. This will discourage investment.

I see slower growth ahead in 2019. I see shops culling their customer list to optimize their office, production and financial operations. Some accounts are just too painful to deal with and too slow to pay. I see shops continuing to invite their communities in to see the amazing high tech jobs available without college or college debt and gaining a couple of strong candidates through internships and other means throughout the year. And, I'm going to double down on my loser from last year—training. If we don't do it, who will? If we don't do it now, how will it help us when we need trained people down the road?

Our take is 2019 will be like 2018, only softer. It is up to us to make it smoother. We do that by the choices we make. Such as is this customer really worth the aggravation? Which of my team will respond positively to this new training opportunity? If I automate this process, I can take that operator and upskill them to what?

My vision is not as clear on the economics as it was in 2017. But the vision of an industry needing to upskill all its performers is 20-20 in my mind.