MARCH 2016 VOLUME 15

SNAP SHOT INDICATORS

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Retail Sales	Mild Rise
Manufacturing	Mild Rise
Medical	Mild Rise
Auto Production	Mild Rise
Wholesale Trade	Mild Decline
Interest Rates	Mild Rise
Capital Goods	Mild Decline
Electronics	Mild Rise
ITR Leading Indicator	Mild Decline
Housing Starts	Mild Rise
Consumer Expectations	Mild Decline
Chicago Fed National Activity	Flat
US Leading Indicator	Mild Decline
Purchasing Managers Index	Mild Rise
S&P 500 Stock Prices	Mild Decline

Steep Rise
Mild Rise
Steep Decline
Flat
Mild Decline

MACROECONOMIC OUTLOOK

US Industrial Production, a key metric for gauging the state of the US economy, is in decline. While there are bright spots within the industrial economy, a variety of factors are weighing on the overall Industrial Production trend. Utilities in 2015 were down 6.3% compared to the 2014 level. Low oil prices and lower-than-normal demand for electricity during an unseasonably warm winter and low oil prices have led to strong declines in mining, which includes oil and natural gas extraction.

Conversely, US Manufacturing, the largest component of Industrial Production, grew 1.8% in the 12 months through February compared to the previous year. However, growth is not uniform across each component of manufacturing. US Nondefense Capital Goods New Orders, a benchmark for business-to-business activity, is falling. Low commodity prices and a relatively strong US dollar are hampering growth in New Orders. Additionally, businesses closely related to the oil industry are suffering from a severe decrease in demand as oil field expansion has all but halted domestically.

Many of the same issues, with which the business-to-business economy is struggling, have proven to be a boon to the consumer-facing elements of the manufacturing segment. Relatively less expensive imports and savings on gas, along with rising employment rates, have instilled confidence and a willingness to spend in the American consumer. Businesses in industries related to the manufacture of consumer goods which are not easily substituted with imports, such as the housing and auto industries, are benefitting the most from increased consumer spending.

Volatility in commodity markets and general uncertainty abroad led to a decline in the S&P500 in February compared to the January level. Stock prices will likely recover as oil and commodity prices begin to recover. Government Long Term Bond Yields dropped 20 points in the same month as similar uncertainty in global markets, along with falling expectations for long-term inflation, are driving demand for safer government bonds.

Despite general weakness in Industrial Production, there are good times ahead for the American economy. Monthly trends are signaling recovery in the US Leading Indicator and the Purchasing Managers Index, both of which are important indicators of economic improvement. Additionally, there are tentative signs of recovery in metal and oil commodity prices; if these trends persist, they will help drive growth over the next year. Overall, expect a stronger second half to 2016 followed by general expansion of the economy through 2017.

MAKE YOUR MOVE™

Look for ways to tap into the European market as a stronger euro would mean US made products will be relatively less expensive to purchase in Europe.

INDUSTRY ANALYSIS

Retail Sales

Total Retail Sales (Deflated) over the past year increased 1.7% from the prior year. The rate of growth will slow through 2016 before accelerating in 2017 as the consumer remains a driving force in the US economy.

Wholesale Trade

Wholesale Trade for the 12 months through January was down 3.8% compared to the year before. Internal trends indicate that decline will persist through the first half of 2016, before growth takes hold in the second half of the year.

Manufacturing

Total Manufacturing Production grew 1.8% over the 12 months through February compared to the year before. The rate of growth will slow into the third quarter of 2016. Segments closely tied to oil and commodity prices are underperforming, while consumer-facing segments will present the strongest opportunities for growth through 2016.

Interest Rates

US Long Term Bond Yields dropped in February by 20 basis points. Yields are being driven down by investors seeking relatively safer investments in response to weak financial markets and rising global uncertainty.

Medical

US Medical Equipment and Supplies Production grew 1.7% in the 12 months through January compared to the previous year, and Personal Consumption Expenditures on Pharmaceutical Products are up 8.3% in the same period. Production will grow through at least 2018, as an aging American population incurs progressively higher healthcare costs.

Capital Goods New Orders

Nondefense Capital Goods New Orders over the past 12 months are down 4.8% compared to the previous year. New Orders will resume growing around mid-year. In general, 2017 will be a better year for business-to-business activity than 2016.

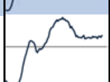
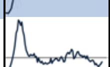
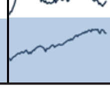
Consumer Expectations

Consumer Expectations are faltering as plummeting oil prices and sluggish growth abroad have raised questions about future economic conditions. However, rising employment is helping to counter some of the negativity felt in consumer expectations.

Office Buildings Construction

Annual Private Office Buildings Construction ticked up to $49.0 billion in January, an increase of 26.0% compared to the same 12 months last year. Growth is decelerating, and Office Buildings Construction in general will be 15.7% higher in 2016 than in 2015.

SNAPSHOT INDICATORS

Indicator	Direction		What it means for the US economy
ITR Leading Indicator™ (Actual)		Tentative rise	If this emerging rising trend persists, it would support a rise in the economy in the second half of 2016.
Housing Starts (Most recent 12 months compared to same 12 months one year ago)		Mild rise	General rise in Starts suggests consumer strength will persist in 2016.
Consumer Expectations Index (Most recent 12 months compared to same 12 months one year ago)		Decline	Cyclical decline suggests weaker economic conditions into late 2016.
Chicago Fed National Activity Index (Six-month average)		Decline	A fourth month of decline suggests that the economy could weaken into at least the second half of the year.
US Leading Indicator (Most recent month compared to same month one year ago)		Mild decline	General decline points to a weaker US economy into the latter half of 2016.
Purchasing Managers Index (Most recent month compared to same month one year ago)		Tentative rise	Upward movement supports expectations of a cyclical low in the economy in the second half of 2016.
S&P 500 Stock Prices (Raw Data)		Mild decline	Stock market volatility will persist through the near term signaling minimal upside momentum for the economy in the first half of 2016.

LONG-TERM VIEW

2016:
Growth Second Half

2017:
Ongoing Strength

2018:
Slower Growth

EUROPE GROWS, EUROPE WOES, AND WORRIES ABOUT CASH FLOW

By: Keith Ellis

Europe Industrial Production will rise in 2016 while many other regions of the world decline. This could lead to a net inflow of investments into Europe as companies and investors seek safety for their assets while other global markets decline. This supports that the rise in exports will diminish and domestic consumer trends will become more important to the growth of the European economy. We see opportunities within the broader European economy (that will persist despite slower growth in export volume) which could drive confidence in the euro. Underlying our expectation of growth in Europe is that the European consumer is strong. Annual Retail Sales in Europe are growing at the fastest pace in over three years and Residential Construction permits are outperforming Non-residential Construction permits.

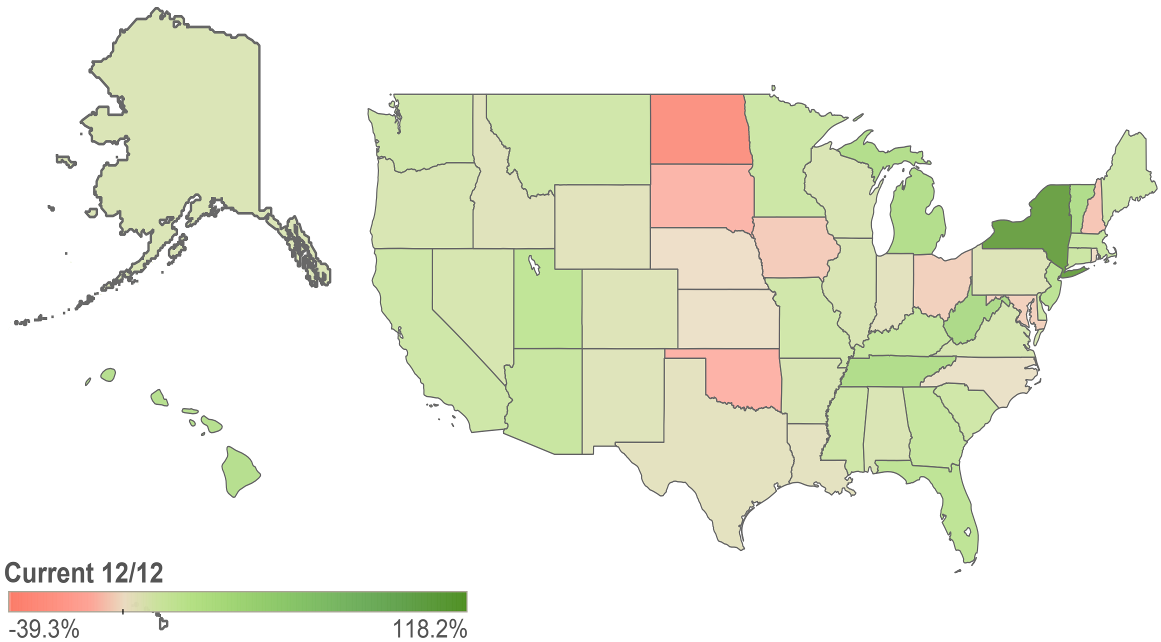
A strengthening euro relative to the dollar is good news for US export-reliant companies and bad news for US consumers who enjoyed the lower-cost luxury imports in the past year. A weaker dollar will provide the means for many export-heavy producers to recapture some market share that was lost due to price disadvantages in the current weak global demand environment. US Corporate Profits are rising and the bond markets will see increased activity as companies expand operations for 2017. The financial market's volatility will ease in the coming months and the spread on bond yields will tighten, suggesting improving US markets for 2016. A weaker US dollar could also help inflate their earnings that are then brought into US dollars.

With interest rates and inflation rates persistently low in the US and in Europe, the near-term impact of the exchange rate on inflation will be muted. Expected improvement in Energy Prices later this year will have a much greater impact. We do foresee an upcoming US consumer-lead recession in 2019 due to rising interest rates, inflation, and lower Retail Sales which may be worsened by negative exchange rates and cash flow reversals.

Generally speaking, cash outflows are a negative sign for an economy. Should concerns mount regarding the banking system in Europe, we could see shifts in this capital flow direction. If there was a bank crisis in Europe, the cash outflow effects would not be wholly directed at the US; we would likely also see the Japanese yen strengthen. Our forecasts of accelerating growth in China, Europe, and parts of the Middle East suggest that any concerns for the banking system in Europe will be unlikely to develop in this cycle, but will become more acute in association with the 2018-2019 business cycle decline ITR Economics is forecasting.

In conjunction with general expansion over the next two years in Europe, we see a strong consumer market that is ready to be mined. With a weaker dollar, US based exports will become more attractive to the European consumer. These opportunities will persist in the near-term; however, we suggest being cautious of your long-term exposures in the market to avoid fallout in the next cycle. As a weakening dollar generally results in increased producer prices and inflation, take steps now to increase efficiencies to protect margins domestically while also building your supply chain to meet an increasing global demand by the end of 2016.

STATE-BY-STATE: Home Permits



The Central region shows the most noticeable clustering of Home Permit decline in the nation. In terms of individual states, North Dakota (-39.3%), Oklahoma (-12.3%), South Dakota (-11.0%), and Iowa (-1.3%) show the steepest percent decline in Permits. The decline in the oil & gas and farming industries over the past year has weighed on this region. The Southeast, Northeast, and West region show clustering of Permit growth as technology and service investments in these areas are rising. New York is still seeing lingering growth from legislation that pulled forward many housing projects.

READER'S FORUM

What are your expectations for China?

Alex Chauspvsky, an Analyst at ITR Economics©, answers:

Answer:

We expect the Chinese economy, as measured by Industrial Production, to decelerate further in the first half of 2016 before activity picks up in the second half of the year. China's Leading Indicator has been rising since last August, signaling a cyclical reversal for China's economy in the second half of this year.

In addition to the China Leading Indicator, good news can be seen in two key areas. The first is Automobile Production, where the rates-of-change are signaling that the government incentives to spur this industry are working. The second key industry trend is in Railroad Freight Carried (measured in tons). Freight is experiencing 1/12 and 12/12 rate-of-change rise. This signals positive business cycle momentum and a healing industrial base as measured by freight movement.

Please send questions to questions@itreconomics.com