

What's That Down the Road? A Head?

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With apologies to the old Red Skelton bit, this is the question that manufacturers are now asking about 2010. The 2009 recession has been replaced by the 2010 recovery but thus far it is hard to tell one from another. If this is the year of recovery what will that mean? How will this coming year be judged? Against the miserable performances of 2008-2009 or by the boom years that preceded them? In some respects both will serve as reference points.

The four main factors that will affect decision making in the coming year will be familiar to anyone in manufacturing as these are always the elements that companies must adjust to. The first is credit and its availability, the second is the emergence of an inflationary spiral that affects commodities like steel and oil, the third is whether demand factors will recover in time to promote production, and the fourth is the impact of various governmental programs and efforts.

The issue of credit has been at the forefront of many manufacturers' concerns since

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the credit market locked up in the third and fourth quarters of 2008. The ability to borrow has been severely constrained as many of the traditional lenders have vanished and the banks that remain have become much more conservative than they have been in the past. The good news is that the latest surveys from the National Association of Credit Managers shows that credit is starting to loosen up, and by the middle of 2010 the lending environment is expected to look a little closer to the normal that existed in the pre-boom years.

The threat of inflation is not expected to be a major factor through 2010. The estimated rate of producer price inflation is between 1.5 and 2 percent for the year and many think it will be much lower than that. Oil prices should stay in the \$65 to \$80 a barrel range and metals prices will be below levels in 2007 and 2006 — depending on what happens with China's production and demand. There is still a considerable amount of money in the system and should it start to cascade out there will be problems, but on the positive side there should be little wage inflation.

The third factor is perhaps the most vexing. When does demand come back in a consistent manner? There has been some boost in inventories in the last month but this has been a reaction to the fact that the overall rate of inventory had been so low. The consumer has started to come back but remains cautious and more frugal than in the past. There is not much encouraging to say about the automotive sector yet — but there are some signs of life in aerospace and energy.



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The last factor is perhaps the hardest to predict. The biggest change from the past few years is a much expanded role for government. This involvement can be good news or bad news for manufacturers and in many cases the impact will be a little of both. The stimulus money that was supposed to have been spent in 2009 was mostly not allocated and it now looks like 50 percent of it will be spent in 2010. Thus far the money spent has mostly been directed at relieving the budget crisis in various states but there is an intent to direct more of the money to infrastructure projects in the future. There is also the new money that has been suggested by the House of Representatives — around \$80 billion that is supposed to be directed at rebuilding the transportation sector. The stimulus plan has not had the impact it was expected to have, but there is still time to make some difference to the economy.

The second aspect of governmental engagement is not expected to be as salutary. The rush to find ways to correct the mistakes of the banking sector has led to

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regulations that will restrict lending and make the credit challenges worse. There are also plans that will have major implications for manufacturers. The "Cap and Trade" legislation could impose severe fines on those companies that have emission issues and could well make energy more expensive as utilities are faced with compliance issues. Even if Congress fails to act and pass legislation the Environmental Protection Agency stands ready to impose these rules unilaterally. There are provisions in the various health care proposals that could prove to be very expensive and which would impact hiring decisions. The list goes on. The biggest problem for many businesses is the uncertainty around the government actions.

In general terms 2010 will be better than 2009. GDP growth will be in the range of 2 to 3 percent, which is far superior to the negative numbers registered in the last year. Inflation will be down, unemployment should start to stabilize, and the ingredients for a slow and methodical recovery will be in place.

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