**The Auto Parts Industry has made a strong recovery since the last recession and we believe this momentum ought to continue in the years ahead. Overall, the big picture has not changed much since our March review, and the industry's short- and long-term prospects remain mostly favorable.**

**Automotive sales and production levels are directly correlated to industry fundamentals and these trends differ greatly on a regional basis. There is a clear contrast between strength in North America and, to a degree, Asia, improvement in Europe, and significant weakness in South America.**

**The sector, as a whole, has performed well so far in the first half of 2015. We have seen solid organic growth across the industry, indicating good business trends of late. However, much of this growth has been offset by unfavorable currency translation rates, due to the strength of the U.S. dollar. Going forward, foreign exchange headwinds will likely continue to mute reported sales and earnings, and have prompted many companies to reduce their top- and bottom-line outlooks. This is especially true for those companies whose sales are primarily outside of the U.S.**

**North America**

The automotive market in North America, particularly in the U.S., has remained vibrant. In fact, in the U.S., which is the world's second-largest market, the seasonally adjusted annual rate (SAAR) of light-vehicle sales for the first quarter was 16.6 million units. During the April and May months, the annualized selling rate was 16.5 million and 17.8 million, respectively. Notably, the May figure was the highest rate since July 2005. Looking ahead, we think auto sales, which have been on an upward trajectory since 2009, will continue to grow at a healthy clip. This assumes demand and production levels will continue to rise. At this point, we project 2015 and 2016 total light-vehicle sales will be 16.9 million and 17.3 million units, respectively. This outlook is largely based on improving economic conditions, particularly related to credit availability, interest rates, fuel prices, consumer confidence, and employment figures. The average vehicle age (which is over 11 years), the number of vehicles in operation, and miles driven should also drive demand for both replacement parts and new vehicles. All told, this healthy auto sales/production momentum ought to persist in the years ahead, though the rate of recovery may moderate.

**China**

China, which is the largest automotive market in the world, continues to lead the pack, and sales/volume growth will likely remain mostly robust. Thus, many companies have worked to expand their presence in this emerging market to take advantage of the opportunities there. That said, a deceleration in economic activity is a growing concern in the coming years.

**Europe and South America**

Economic conditions in Europe, particularly related to the automotive industry, have shown increased signs of stabilization. This is especially true in the western region. Auto sales/production, which were at a 20-year low in 2013, may well continue to improve, though at a gradual rate. However, economic and geopolitical concerns in the eastern region, namely Russia, have put a damper on the European market and have tempered our recovery expectations.

**INDUSTRY TIMELINESS: 14 (of 96)**

Meanwhile, South America, particularly Brazil, remains the weakest spot. This reflects economic deterioration, high inflation, currency losses, import restrictions, and lower demand, among other things. Looking ahead, we expect soft and volatile market conditions to persist in this region.

Consequently, those companies with higher exposure to Europe and South America will probably experience lower revenues and profits.

**Key Industry Trends**

Auto parts suppliers have been working to keep up with key industry trends, notably those that are "safe, green, and connected", to gain a competitive edge. This has prompted many companies to enhance and develop new products and technologies that improve safety, enhance fuel economy, lower emissions, and support in-car connectivity, among other things. However, suppliers must be able to keep up with these fast-pace advancements. Interestingly, we have also seen a lot of news regarding vehicle recalls, which could pose challenges for automotive manufacturers and suppliers.

**Conclusion**

The Auto Parts Industry, as a whole, has both short- and long-term appeal. In fact, it remains a top choice among all sectors covered in the *The Value Line Investment Survey*, and will likely continue to outperform the broader market averages over the comings six to 12 months. True, over the last three months, the industry's rank has slid a few spots, to 14 out of 96, as price and earnings momentum of late has moderated. In addition, the industry has a large selection of equities to choose from that offer above-average price appreciation potential out to 2018-2020. This assumes continual growth in automotive sales/production and demand.

Still, interested investors should be able to endure some volatility, as most equities covered here carry Below-Average Safety ranks, above-market Betas, and low Price Stability scores.

We encourage investors to read the individual reports for a more detailed evaluation before committing funds.

*Michelle Jensen*