

The business outlook for the Auto Parts Industry remains mixed, as some positive trends continue to be offset by increasing challenges. Auto sales have been declining in many parts of the world, particularly for light vehicles, and this is a concern for those companies that cater to that segment. Other notable issues are rising material costs and ongoing trade tensions, particularly between the two largest economies in the world, the U.S. and China.

However, the industry still has some trends in its favor. Miles driven, an important statistic for the sector, continues to rise, which should help to boost sales of auto parts. An aging vehicle fleet, which tends to lead to increased use of auto parts, is another positive development. The heavy-duty truck industry continues to perform well, although medium-duty truck demand is somewhat softer. Too, the ongoing strength of the U.S. economy will remain a positive factor for most in the industry, since the majority of companies we cover here are based in the U.S. and have a large percentage of sales there.

As indicated in previous reports, our discussion on the Auto Parts Industry is centered around automotive sales and production levels, as they are directly correlated with the Industry's fundamentals. These market conditions vary greatly geographically. As such, results can diverge vastly for companies with different core geographies, so investors should take note.

Global Auto Sales Trend Downward

During the September quarter, global light vehicle sales declined roughly 5%, to around 90.1 million units. Demand for vehicles in China, the largest auto market in the world, has weakened in recent quarters, as has demand for vehicles in India. Volumes in North America and Europe have flattened out, as well, with several countries in Europe posting declines. This is, in part, due to rising concerns about recession in that region. Clearly, slowing growth from some of the largest economies in the world is a major concern for auto parts manufacturers.

Additional Challenges

Aside from auto markets, additional weakness in the global economy is being driven by a deterioration in manufacturing activity and global trade. Higher tariffs, along with ongoing volatility in trade policy among major economies, are putting pressure on most economies. New emissions standards, particularly in Europe and China, have also pressured results for several auto parts manufactures.

Material costs have also been on the rise in recent months, putting pressure on most companies' bottom lines. Prices for steel and aluminum, two primary inputs for automotive parts, have increased and narrowed margins for most. While some manufacturers have been able to pass these costs onto customers, others have had to eat the expenses in the short term.

A strong U.S. dollar, compared to most global currencies, remains a concern for U.S.-based companies, as well, as it tempers demand for American products abroad, and also results in lower reported results.

Some Positive Trends Remain

Despite ongoing concerns about global auto markets,

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there are still several positive trend that should continue to support the Auto Parts Industry. Miles driven, a key statistic for the sector, continue to increase, and remains near record highs. This ought to support continued demand for auto parts. Increased wear on the average fleet, which is at a record age of around 12 years, should also help boost sales for auto parts manufacturers, as well. Elevated replacement demand, declines in capacity, and improved carrier profitability are also positive indicators for the sector. Increased adoption of automated transmissions in Europe and Asia should also provide an opportunity for some, including *Borg-Warner*. Other companies that provide parts to heavy-duty truck manufactures, including *Commercial Vehicle*, should also benefit from the gains expected from that segment of the market.

Top Pick

One of the top picks in our Auto Parts Industry is *Gentex Corporation*, a manufacturer of automatic-dimming auto rearview mirrors and electronics for the automotive industry. Despite a slowdown in global light-vehicle production, the company was able to post solid sales growth in the September quarter. Strong demand for exterior mirrors, particularly in North America, drove the advance. Margins widened thanks to the higher volumes, along with a favorable product mix and better product mix. Looking forward, we think Gentex will benefit from good demand for its core auto-dimming rearview mirrors, as these products continue to be incorporated into more vehicles around the globe. Ongoing stock repurchases should also provide a boost to share earnings in the coming quarters.

Conclusion

All told, business prospects for the Auto Parts Industry remains mixed, although there are some more concerns arising. Some generally favorable trends are being offset by declining global light vehicle production. The overall health of the global economy is also an issue. We note that prospects for each company depend on the primary region in which it conducts business, so investors should take note. They are, therefore, advised to review the following individual reports before making any commitments.

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