Unicorn Hunting, a.k.a.
Searching for Countercyclical Manufacturing Sectors

Throughout my career of industrial market analysis many of the projects I have experienced involved searching for countercyclical sectors to enter or acquire in order to offset the cycles of the base current business.

In all those projects, I have never found a single sector that was both consistently countercyclical[1] to the base business and also of large enough scale[2] to offset the scale of the base business.

Certainly there are many anecdotal examples of a single cycle in which a particular industrial sector or sub-sector did behave in a countercyclical manner. The questions are; has that sector done so in all cycles, or just the most recent one? And will it do so consistently in the future?

Recently I looked at all of the NAICS Code industrial sectors over an extended number of cycles to put this to bed once and for all. The Results[3] below are based upon scouring and analyzing the performance of about 100 subsectors of all 10 durable goods manufacturing sectors[4] in the U.S. economy for the 43 year period of 1972-2013.

> **Number of Cycles** - Over the period the overall economy had 6 official economic cycles[5]. The average for the durable goods subsectors was also 6 cycles. Within that, 93% had 5-7 cycles and only 7% had less than 5 cycles, all of which were in computers and electronics.
>
> **Correlation to the Total Economy –** Two-thirds had a correlation of at least 60% to the total economy[R=0.60]. Half had at least a 70% correlation [R = 0.70]
>
> **Timing of Cycles** – 80% of the subsectors peaked and troughed within plus or minus one year of the peaks and troughs of the total of all durable goods.

---

[1] That may or may not have been the explicit request but that was the essence of the expectation.

[2] For example, the aftermarket replacement parts and services businesses for most industrial sectors are frequently cited as countercyclical to the cycles of the original purchases of those products. While that is generally true, businesses and consumers often not only delay new purchases in economic downturns, but they also frequently delay preventative maintenance, and even necessary repairs, until they are left with absolutely no choice. And the tremendous increase in quality of the original products has dramatically reduced the scale and the margins that are generated by aftermarket parts and services today, compared to 3 or more decades ago when that was a significant countercyclical aftermarket sector. Due to those factors, most aftermarkets are no longer of meaningful scale to offset the downturns in the base corresponding business.

[3] J.T. Gabrielsen Consulting, LLC analysis of data from the U.S. Bureau of Economic Analysis [BEA]

[4] Manufacturing of: Wood Products, Nonmetallic Mineral Products, Primary Metals, Fabricated Metal Products, Machinery, Computer and Electronic Products, Electronic Equipment Appliances and Components, Transportation Equipment, Furniture and Related Products, and Miscellaneous

[5] The 1980 and 1982 'double dip' is officially counted as two by the NBER, although it sure felt like one single miserable never ending downturn IMHO.

Length of <u>Up</u> Cycle – Over 70% were within plus or minus one year of the average length of up cycle for the total of all durable goods, of 3.9 years.

Length of <u>Down</u> Cycle - Over 95% were within plus or minus one year of the average length of down cycle for the total of all durable goods, of 2.6 years. Two-thirds were within plus or minus 6-months of the average.

Conclusion - Durable goods sub-sector sectors all largely follow the overall economic cycles. Therefore they cannot be counter cyclical to one another. Therefore, you are as likely to find and enjoy countercyclical durable goods sectors to offset your base durable goods business, as you are to find a unicorn.

Jon T. Gabrielsen is President & CEO of J.T. Gabrielsen Consulting, LLC. http://www.jtgabrielsenconsulting.com/ The primary mission of the firm is upon Uncovering the Market Growth and Cost Reduction Opportunities for Your Manufacturing Company's Competitive Success.