

VIEWPOINT

More Than Just Tariff Noise? Appliance Shipment Weakness

NICHOLAS BENDER | JULY 30, 2018

For restaurant critics, the decibel meter has become a necessary tool. A generation of chefs and restaurateurs have designed spaces to maximize acoustics, elevating background noise to levels of distraction. This sensation must feel familiar to investors who have listened to global trade chatter rise to an unpleasant roar. The U.S. appliance market is emblematic of the shift, as multiple rounds of trade restrictions have upset industry dynamics. Moreover, the reverberations threaten to impair housing activity.

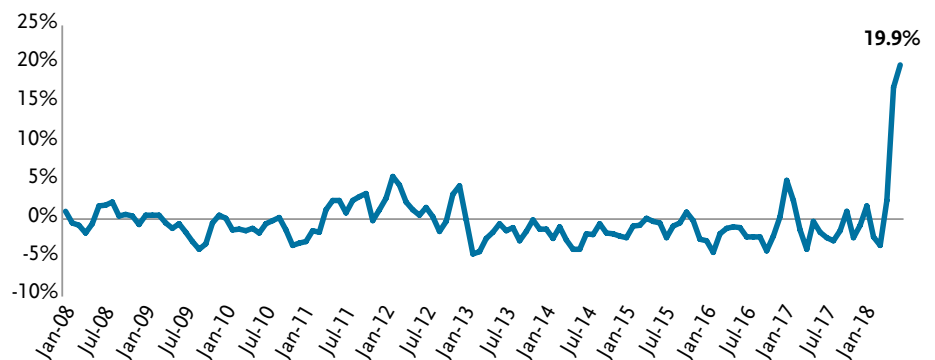
The appliance market was upended in January when the White House approved anti-dumping tariffs on imported washing machines. This was a blow to Samsung and LG, the South Korean-domiciled appliance makers that combine for more than 30% of the U.S. market. The move was expected to be a windfall for Whirlpool, allowing the company to increase prices and boost its mid-single-digit operating margins. However, the excitement was short-lived due to steel and aluminum tariffs that were announced just weeks later. Given higher input costs, raising prices became a necessity rather than a luxury. As a result, laundry equipment prices have increased nearly 20% in the last three months.



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3-Month Change in Laundry Equipment Prices

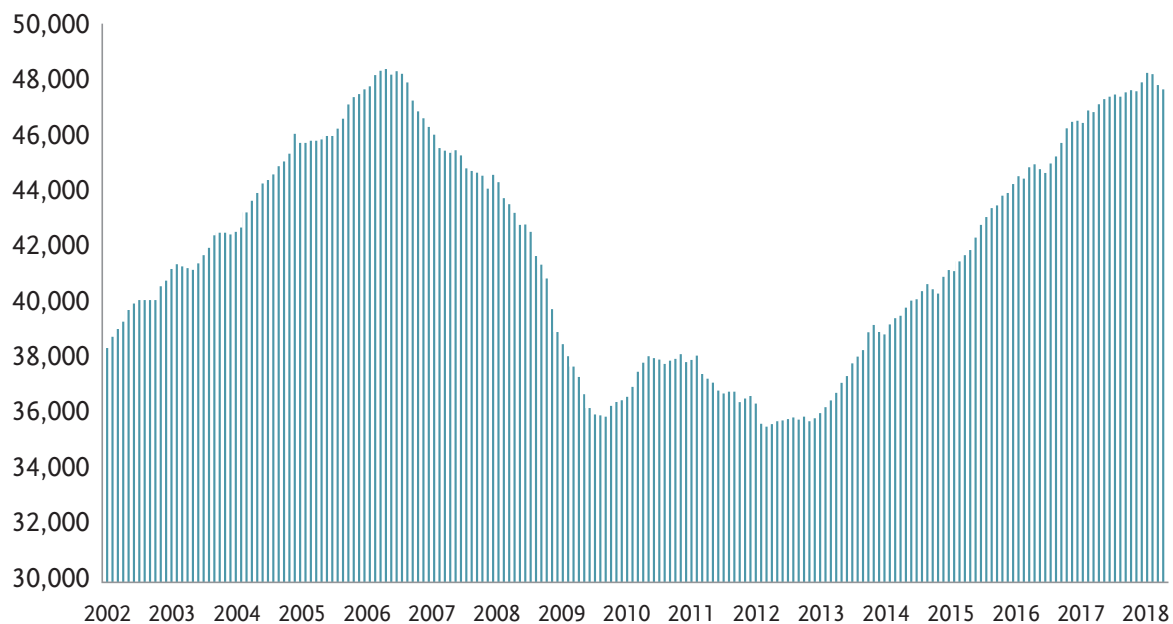


Source: Bureau of Labor Statistics.

More Than Just Tariff Noise? Appliance Shipment Weakness

In June, the Association of Home Appliance Manufacturers reported that total appliance shipments to U.S. dealers fell nearly 10% y/y, while volumes for major appliances fell 4%. It was the second consecutive month of industry-wide declines and the trend continues to point lower; LTM sales growth has slowed to just 1%. This deceleration was confirmed by industry-leader Whirlpool, which reported a 2Q18 sales decline of 2% in North America due to a 9% decline in volumes. In short, pricing gains have been insufficient to offset the decline in unit volumes.

Trailing 12-Month AHAM t-6 Shipments

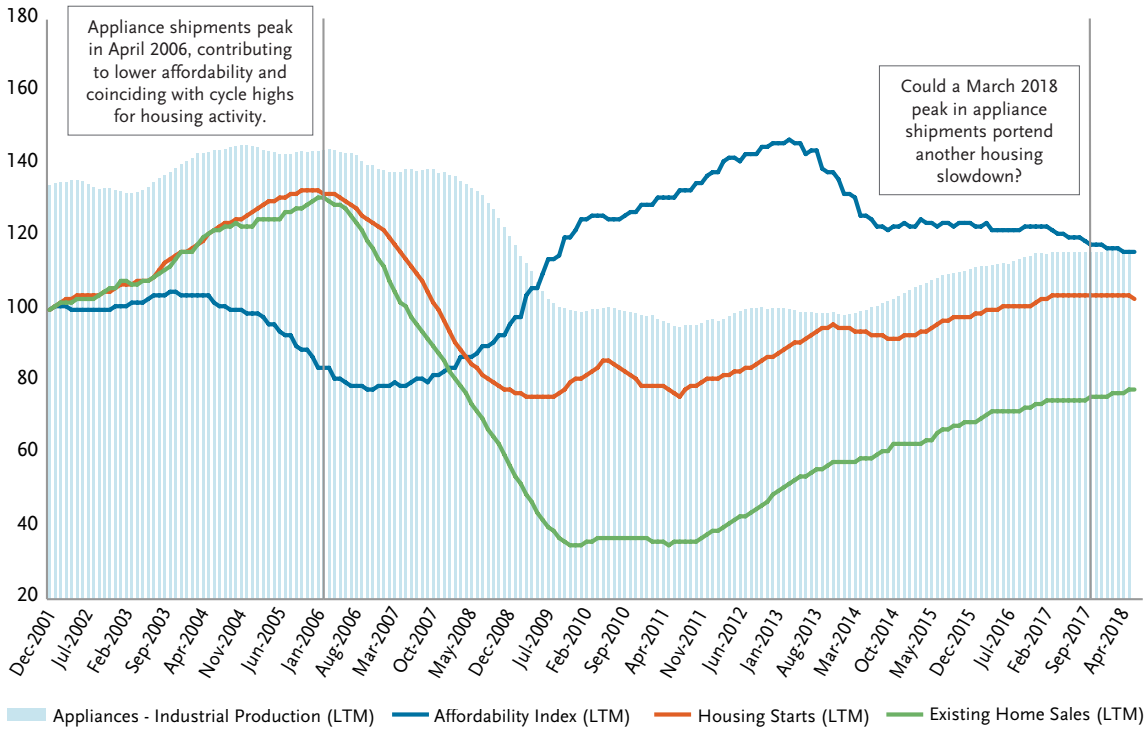


Source: Credit Suisse, Association of Household Appliance Manufacturers

It's tempting to point a finger at recent tariffs as the sole driver of this volume weakness, but insidious cyclicality is also at play. Whirlpool estimates that roughly 50% of category sales are from replacement activity, which is driven by a 10-12 year equipment lifecycle. The fact that major appliance shipments peaked in March 2018 – almost 12 years to the month since the prior April 2006 peak – seems more than coincidental.

Aside from replacement, the other half of category revenue comes from a combination of new construction, existing home sales, and remodels. These sources of demand are more pro-cyclical, and thus likely to be price inelastic when it comes to appliances (or a slew of other building products, for that matter). Consumers already face the worst home affordability conditions since August 2008, and the uptick in appliance prices will exacerbate sticker shock. It should come as no surprise that June new home sales were the lowest in eight months, and housing starts fell more than 12% from the prior year.

Appliance Shipments & Housing Cycle



Source: Bloomberg

Looking ahead, tariffs on Chinese production could ratchet up the decibel level further. Appliance manufacturers will continue to scramble to protect margins, even as expanded domestic production will ultimately make the market more price-competitive. In the interim, consumers will remain stressed by rising prices, and that stress is likely to dampen demand even more. As the chorus of trade concerns continues to build, the ruckus could generate material instability in the housing market – and may get loud enough to cause permanent damage. ■

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