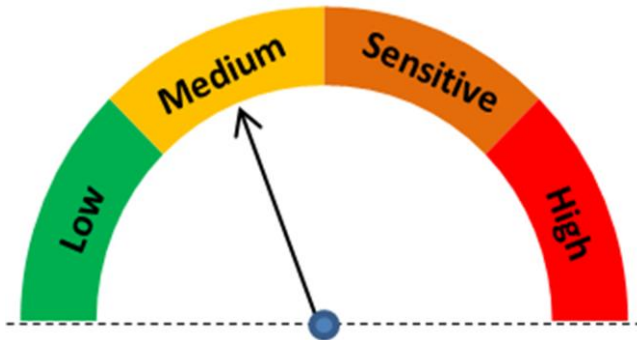


Sector Risk Rating



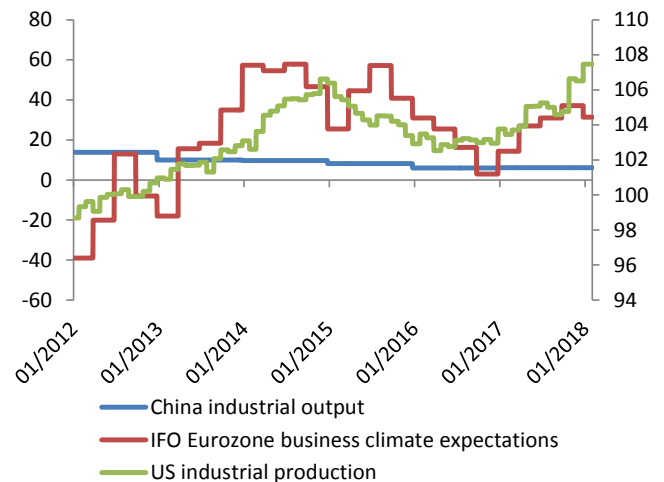
What to Watch?

- Order book momentum
- Indications of change in pricing power and input commodities volatility
- Reversal of USD weakness
- Impact of monetary policy on economic activity and inflation as key drivers for sector earnings

Motoring on with the economy

As one of the most cyclical sectors, synchronised economic growth will buoy activity in the machinery sector across all major regions. 2017 was the best year for the sector since 2011 on various accounts and the outlook remains positive: Business confidence in Europe stands at two year highs as does US industrial production. For a very export driven sector, global trade growth of +6.8% (EH forecast 2018 in nominal terms) USD weakness will support activity as about 50% of machinery exports happen in USD. All of the major end markets are expected to deliver growth: Construction equipment sales growth +3.4% y/y 2018, mining capex +7% 2018, oil & gas capex +4% globally / +11% US Independents (source all: Bloomberg consensus). The commodity sectors (oil/gas, mining) are coming out of recovery and likely to increase capex, driven by strong pricing and cash flow growth while. Construction remains buoyant albeit with the caveat of slowdown in China. New infrastructure investment, namely in the US should drive orders of construction equipment. While rising commodities and materials costs, which can account for up to 75% of the total cost base in certain sectors, pose a risk to profitability, at this point, pricing power is strong enough to protect margins. On average, solid double-digit sector earnings growth is evidence of the recovery, to +34% y/y according to Bloomberg consensus.

Key demand indicators:
Industrial production and business expectations

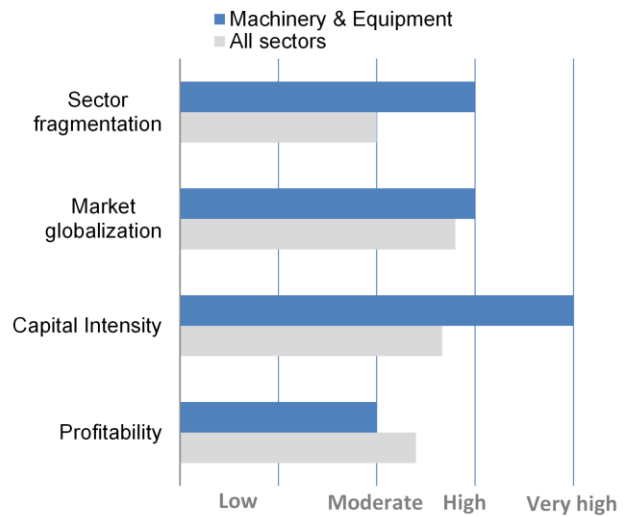


Sources: Bloomberg, IFO

Key Players

Country	Role	Sector Risk
China	#1 producer #1 exporter #2 importer	●
United States	#1 importer #2 producer #3 exporter	●
Germany	#2 exporter #3 importer	●

ID Card



Strengths

- High barriers to entry
- Long-run business cycle serves as a buffer to short term market variations
- Core of industrial innovation

Weaknesses

- Volatility in commodity driven end markets and very cyclical sectors
- Capital intensity
- Increasing dependency on riskier counterparties

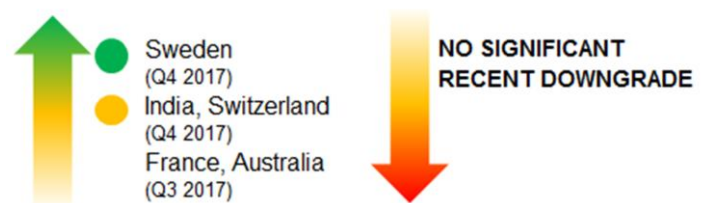
Subsectors Insight

Robotics manufacturers: The sector benefits from a secular growth trend in fab automation. Automotive is a strong driver but also electronics and other sectors

Heavy manufacturing machinery: Sustained growth in industrial manufacturing should continue to support sector order books

Specialised technologies: Global economic activity along with recovery in mining and structural demand related to clean energy and sustainable manufacturing underpin activity

Recent Sector Risk Changes



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