AlixPartners

MANUFACTURING OVERVIEW: CY2024 – Q3

December 2nd, 2024

PREAMBLE

This Manufacturing Overview report marks the first in a quarterly series designed to offer readers a concise evaluation of the current financial performance of manufacturers across industries and the underlying macro indicators and challenges influencing these firms. With this report, we aim to equip readers with strategies to proactively address and navigate the constantly evolving challenges faced by manufacturers.

SUMMARY - Q3 2024

Manufacturing businesses are experiencing significant cost pressures due to lower revenue compared to the previous year, prompting a need to enhance operational efficiency and optimize footprint. Uncertainty from tariffs and taxes are top of mind for manufacturers.

MODEST GROWTH TREND:

Manufacturers experienced a slowdown in demand in Q2 with a modest rebound in Q3. The slowdown was driven by economic uncertainty and changing consumer preferences. In Q3, new orders picked up from the previous quarter.

EXCESS/OBSOLETE INVENTORY ISSUES:

Manufacturers continue to face challenges with excess and aging inventory due to unpredictable demand and excess purchasing of raw materials.

INTEREST RATE CONCERNS:

High interest rates raised the cost of goods sold for manufacturers. Manufacturers experienced decreased profits if they did not pass the increased costs on to consumers.

WORKFORCE CHALLENGES:

Attracting and retaining skilled labor remains the top challenge for manufacturers. This issue is exacerbated by rising healthcare costs and an increasingly competitive labor market.

REVISING NETWORK STRATEGY POST-COVID:

Manufacturers are rethinking their network strategies to adapt to new consumer behaviors and geopolitical risks. Building a footprint to gain security in their supply.

FOCUS ON COST AND PRODUCTIVITY:

With high interest rates limiting capital investment, manufacturers are prioritizing operational improvements to enhance productivity.

KEY TRENDS AND CHALLENGES IN MANUFACTURING

01

DEMAND FLUCTUATIONS

Economic uncertainty and shifting consumer trends are forcing manufacturers to evaluate their flexibility with existing assets. The uncertainty in demand makes scaling production for specific products challenging.

02

PRICING POWER

In addition to rationalization of products, certain businesses such as consumer product companies have raised prices on core products to beat high interest rates.

03

SUPPLY CHAIN RESTRUCTURING

Given current geopolitical risks, businesses are restructuring their respective supply chains to ensure availability of material.

INDUSTRY	% OF COMPANIES THAT BEAT MARKET EBITDA ESTIMATES[1]			
	Q4' 23	**Q1' 24**	**Q2' 24**	**Q3' 24**
Aerospace & Defense	**68%**	**62%**	**68%**	**69%**
Automotive	**50%**	**48%**	**57%**	**53%**
Chemicals	**46%**	**74%**	**52%**	**56%**
Consumer Electronics	**52%**	**60%**	**62%**	**64%**
Energy & Utilities	**67%**	**58%**	**62%**	**55%**
Food & Beverage	**36%**	**79%**	**76%**	**69%**
Health & Beauty	**76%**	**76%**	**69%**	**58%**
Household Durables	**50%**	**83%**	**63%**	**52%**
Industrial & Building Products	**73%**	**69%**	**71%**	**60%**
Metal & Mining	**67%**	**65%**	**63%**	**86%**
Paper & Pulp Products	**63%**	**88%**	**53%**	**36%**

QoQ Change | *Positive* | *Negative or flat*

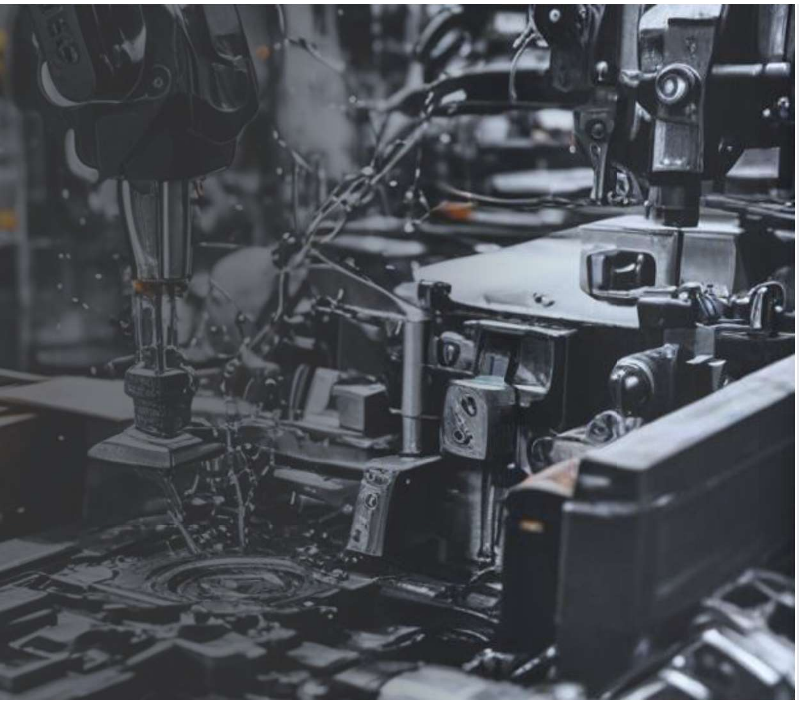
Source: Companies within Industries include Top 40 global public companies by Revenue, (1) based on market consensus on EBITDA estimates vs actuals, calculation based on only companies with available data

KEY TRENDS AND CHALLENGES

COMPANIES ARE STARTING TO SEE A MODEST REBOUND IN REVENUE WITH A STABLE GROSS MARGIN

	REVENUE TTM				GROSS MARGIN TTM				INVENTORY TURNOVER			
INDUSTRY	Q4' 23	Q1' 24	Q2' 24	Q3' 24	Q4' 23	Q1' 24	Q2' 24	Q3' 24	Q4' 23	Q1' 24	Q2' 24	Q3' 24
Aerospace & Defense	++	+	+	+	+	+	+	+	+	-	-	-
Automotive	++	-	-	+	+	+	+	+	+	-	-	+
Chemicals	+	-	-	+	+	+	+	+	+	-	+	+
Consumer Electronics	+	-	-	++	+	+	+	+	+	-	-	-
Energy & Utilities	+	-	+	-	+	+	+	-	+	-	+	-
Food & Beverage	+	-	-	-	+	+	+	+	-	-	-	+
Health & Beauty	+	-	-	-	+	+	+	+	+	-	-	-
Household Durables	+	-	-	+	+	+	+	-	-	-	+	+
Industrial & Building Products	+	-	-	+	+	+	+	+	+	-	-	-
Metal & Mining	+	-	-	+	+	+	+	-	+	-	-	+
Paper & Pulp Products	+	-	-	+	-	+	+	-	-	-	-	+

QoQ Trend Legend
"++" OR "- -" Change in Revenue & Gross Margin exceed +/-5% | Change in Inventory Turn exceeds +/- 0.5
"+" OR "- " Change in Revenue & Gross Margin within +/-5% | Change in Inventory Turn within +/- 0.5



COMMENTS

- Most industries saw a modest recovery in revenue, despite being pressured by market uncertainty.
- Gross margin across industries are generally trending upward, likely driven by the recovery of commodity prices, and the passing on of costs to customers, particularly in the consumer goods sector.

Source: Companies within Industries include Top 40 global public companies by Revenue; metric trend based on median in industry group

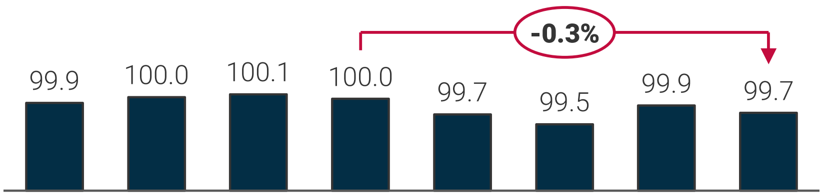
MACRO KPI (USA) - PRODUCTION AND CAPACITY

WHILE PRODUCTION OUTPUT REMAINED FLAT, Q3 WITNESSED A SLIGHT INCREASE IN NEW ORDERS

CALENDAR QUARTER BY QUARTER CHANGE

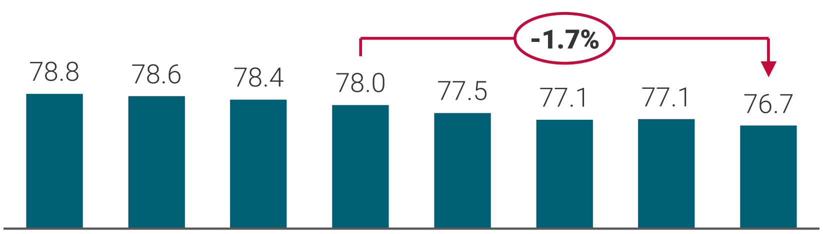
HIGHLIGHTS

Manufacturing production *(Indexed to 2017 production)*



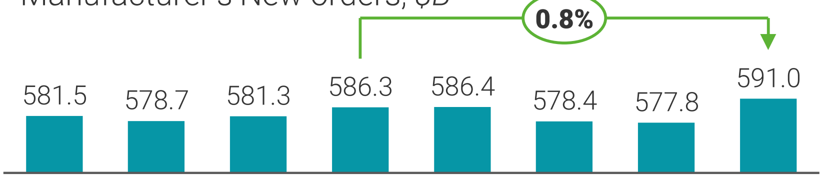
- Since recovering from a COVID dip, manufacturing production has had a slight decrease due to overall drag
- As interest rates ease, manufacturing production is expected to increase

Manufacturing capacity utilization, %



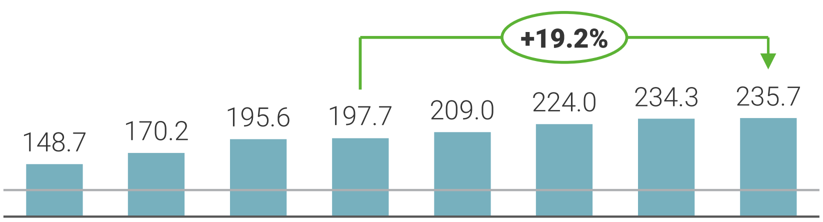
- Capacity utilization for the manufacturing sector has been trending down since investments have increased capacity without an increase in overall manufacturing production
- Potential in-coming government tariffs could drive increased domestic capacity utilization in impacted industries

Manufacturer's New orders, *$B*



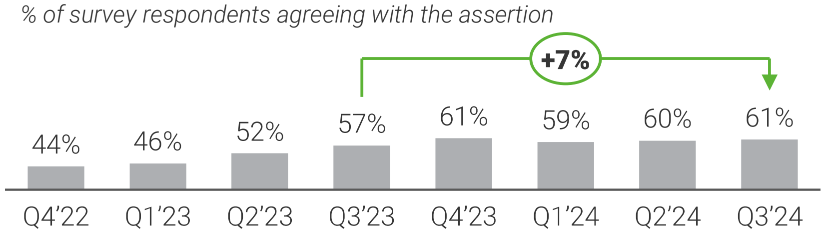
- Investment in US Manufacturing has been moderate and is expected to be strong in upcoming years; however, sector specific challenges could arise from geopolitical risks, supply chain issues, and labor shortages

Private fixed investment, *$B*



- Investments has jumped from the ~$90B average pre-COVID, with further acceleration spurred by the passage of the CHIPs act (increased investment in the semi-conductor industry)
- Climate related investments may face headwinds after recent election results

Unfavorable business climate (taxes, regulations, etc.),
% of survey respondents agreeing with the assertion



- Recent changes to R&D expensing and upcoming expiration of provisions of the 2017 Tax Cuts & Jobs Act can drive up tax related costs for companies
- Recent election results could have significant impact to business climate pending implemented policies

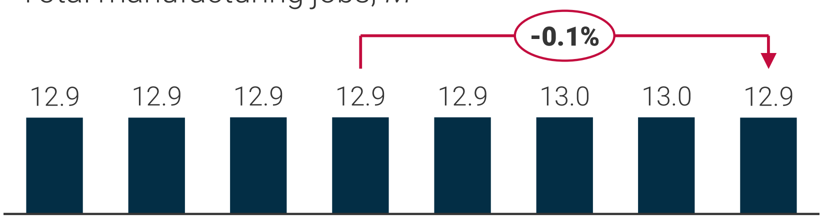
Source: National Association of Manufacturers (https://nam.org/manufacturers-outlook-survey/), Federal Reserve Economic Data (https://fred.stlouisfed.org/)

MACRO KPI (USA) - LABOR

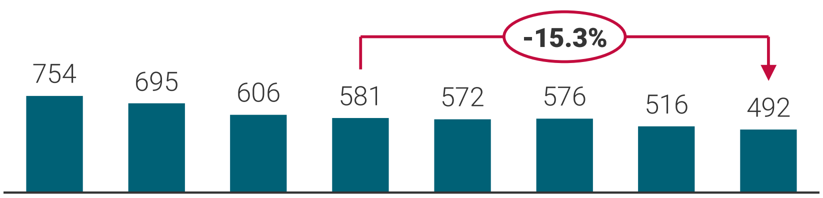
LABOR COSTS AND WORKFORCE RETENTION CHALLENGES PERSIST WITH SLIGHT SOFTENING

CALENDAR QUARTER BY QUARTER CHANGE

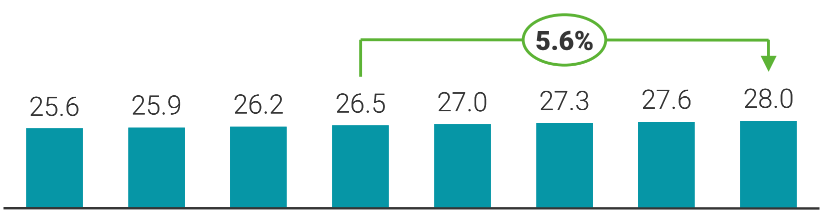
Total manufacturing jobs, *M*



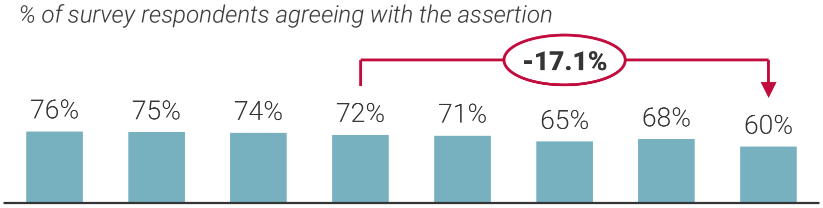
Total manufacturing job openings, *K*



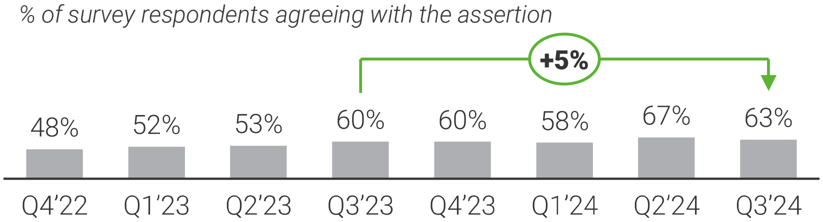
Manufacturing hourly wage rates, *$/hr*



Attracting & Retaining Workforce,
% of survey respondents agreeing with the assertion



Rising Healthcare/Insurance Costs,
% of survey respondents agreeing with the assertion



HIGHLIGHTS

- Manufacturing employment has plateaued over the last couple of years; however, potential new Tariffs and Tax Cuts for US manufacturers could lead to reshoring and create an increase in manufacturing jobs

- Manufacturing job openings are expected to remain elevated due to skills gap, labor shortage , and aging workforce
- Reshoring may lead to increase in manufacturing job openings pending Tariffs and Tax Cuts for companies Manufacturing in United States

- Wages are expected to continue an upward trend given anticipated increase in labor demand driven by reshoring due to Tariffs and Tax Cuts and increased demand for skilled labor due to automation

- While manufacturers are still struggling to fill jobs in some areas, (e.g., skilled trades) the average number of manufacturing job openings in 2024 has dropped to ~500k from the ~830k highs during the post-COVID era (2021-2023)

- Health insurance costs are expected to continue to increase 5-8% in 2025, similar to the increases in 2024
- Manufacturing companies have struggled to pass along increases in premiums to employees

Source: National Association of Manufacturers (https://nam.org/manufacturers-outlook-survey/), Federal Reserve Economic Data (https://fred.stlouisfed.org/)

CASE STUDY

TARIFF SURGES FORCE AMERICAN LITHIUM-ION BATTERY IMPORTERS TO URGENTLY REASSESS THEIR SUPPLY CHAINS

75% OF US LITHIUM-ION BATTERY IMPORTS ORIGINATE FROM CHINA

China has developed a strategic advantage by investing heavily in battery technologies in recent years. However, these supply chains are under threat because tariffs on batteries from China have risen - and are set to rise further.

In their review of Section 301 tariffs – the statutory means by which the U.S. sets and enforces trade agreements – the Biden administration stated that the tariff on battery parts and lithium-ion batteries for EVs will increase from 7.5% to 25% this year.

The tariff rate on lithium-ion batteries for other items is expected to match this rise in 2026. With the results of the recent Presidential Election, there is high certainty that additional tariffs will be imposed.

NEARSHORING AND RESHORING: THE CASE FOR REGIONAL SUPPLY CHAINS

The expected increase in cost is making the case for companies to reduce dependency on overseas supply chains, particularly China, by moving battery production to U.S. domestic suppliers (reshoring) or regional allies (nearshoring).

Sourcing from domestic suppliers eliminates import tariffs, cuts freight expenses, and reduces lead times from weeks to days, enabling a faster response to market demands. When batteries are sourced and assembled in the U.S., the overall cost of goods sold (COGS) is typically 18% to 20% higher than when sourcing from China.

Nearshoring combines vital advantages, such as proximity and reduced geopolitical risk, but avoids significant price hikes due to labor costs.

PROPOSED APPROACHES TO TACKLING TARIFFS

Nearshoring (localize, govt. incentives, MIA/IRA/BABA)

- **Complexity:** Moderate due to same geography
- **Risk:** Finding alternative suppliers, ramp-up production delays, and higher operational costs

Source from different country/supply base

- **Complexity:** Moderate, due to establishing new supply chains and logistics
- **Risk:** Geopolitical risks, quality control issues, and production delays

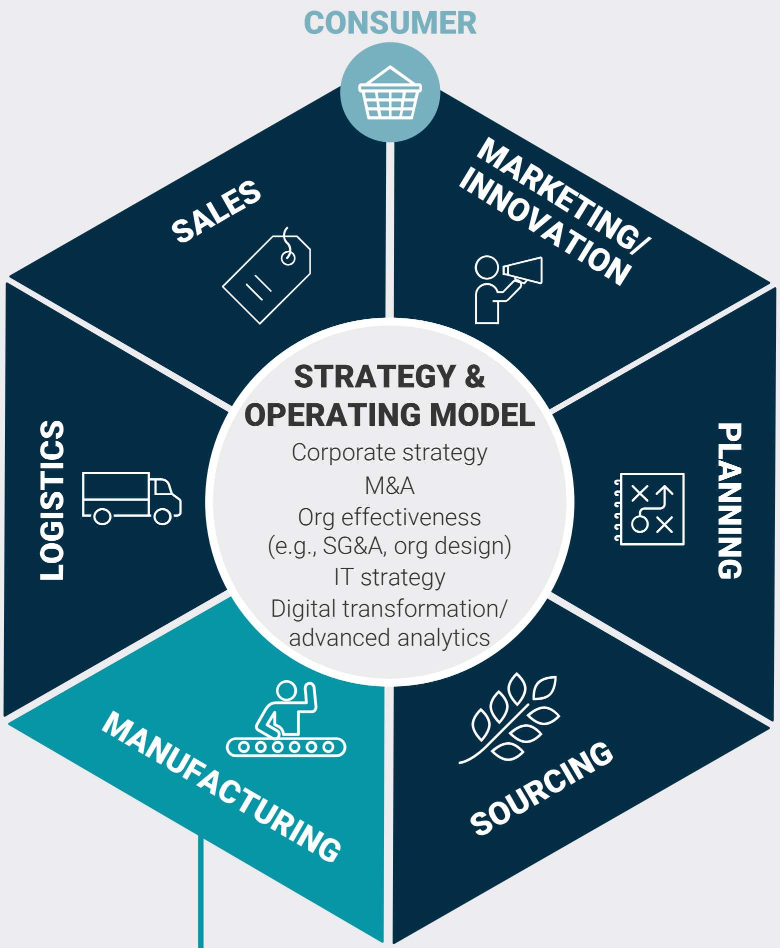
Build factory in USA (financial aid, sell addl' capacity)

- **Complexity:** Very high, due to large-scale investment and setup time
- **Risk:** High financial risk, project delays, and long-term commitment for success

Source: AlixPartners Article – Powering Change: As tariffs on batteries surge, U.S. companies must rethink supply chains (Published September 2024)

AlixPartners has core competencies across the value chain including planning, sourcing, manufacturing, logistics and sales & marketing

Sample areas of AlixPartners capabilities across industries



MANUFACTURING

- Shop floor productivity improvement (e.g., OEE, CI)
- Automation/Smart Factory
- Manufacturing footprint optimization
- Plant closure/(re)open
- Co-pack/co-man cost optimization
- Manufacturing strategy, make/buy

MARKETING/ INNOVATION

- Marketing mix, effectiveness
- Digital, B2B, DTC, eComm
- New Product Development/innovation
- Portfolio management/SKU rationalization
- Category management
- Customer and product profitability optimization
- Trade spend optimization
- Brand management
- Design to value

PLANNING

- S&OP/IBP
- Demand planning/forecasting
- Supply planning
- Digital strategy
- Order management
- SC operating model

SOURCING

- Strategic sourcing (direct/indirect)
- Procurement excellence
- Supply risk management and resilience
- Supplier relationship
- Commodity price management

SALES

- New market entry, route-to-market model
- Omni-channel strategy
- Sales force effectiveness (own, distributor)
- Commercial excellence
- Pricing effectiveness
- Customer service

LOGISTICS

- Transportation management (inbound, middle/last mile, load efficiency, fleet)
- Warehouse & fulfillment improvement (e.g., DC productivity, load optimization, service level improvement)
- Distribution network planning/footprint optimization
- Supply chain sourcing (e.g., 3PL eval, contracting, cost assessment)
- Inventory optimization

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ABOUT US:

For more than 40 years, AlixPartners has helped businesses around the world respond quickly and decisively to their most critical challenges – circumstances as diverse as urgent performance improvement, accelerated transformation, complex restructuring and risk mitigation.

These are the moments when everything is on the line – a sudden shift in the market, an unexpected performance decline, a time-sensitive deal, a fork in-the-road decision. But it’s not what we do that makes a difference, it’s how we do it.

Tackling situations when time is of the essence is part of our DNA – so we adopt an action-oriented approach at all times. We work in small, highly qualified teams with specific industry and functional expertise, and we operate at pace, moving quickly from analysis to implementation. We stand shoulder to shoulder with our clients until the job is done, and only measure our success in terms of the results we deliver.

Our approach enables us to help our clients confront and overcome truly future-defining challenges. We partner with you to make the right decisions and take the right actions. And we are right by your side. When it really matters.