



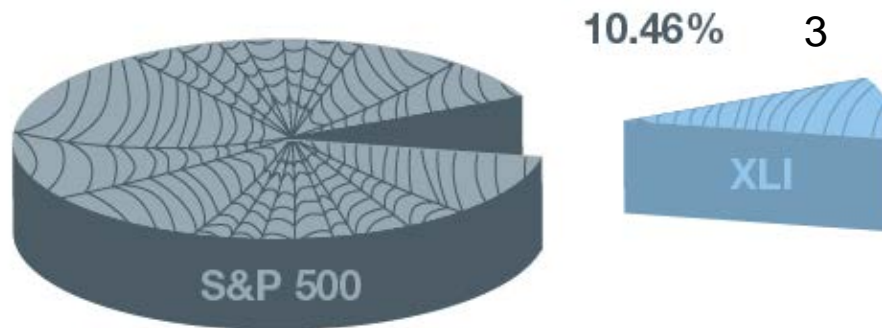
## Industrial Sector Overview

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# The Industrial Sector?



- A category of stocks that relate to producing goods used in constructions and manufacturing. 1
- Of the 9 S&P 500 sectors, Industrials had the closest S&P 500 correlation rate of .92 over the last 10 years. 2



Percentage is the estimate weight of the index components in the S&P 500 as of 06/30/12.

#### Industry Breakdown

1.	Aerospace & Defense	25.28%
2.	Machinery	21.47%
3.	Industrial Conglomerates	20.25%
4.	Air Freight & Logistics	9.37%
5.	Road & Rail	9.00%
6.	Commercial Services & Supplies	4.38%
7.	Electrical Equipment	3.61%
8.	Trading Companies & Distributors	2.03%
9.	Construction & Engineering	1.27%
10.	Thriffs & Mortgage Finance	1.26%
11.	Household Durables	1.09%
12.	Airlines	0.58%
13.	Building Products	0.41%

#### All Holdings and Weightings

General Electric	12.20%
United Parcel Service	5.74%
United Technologies	5.34%
3M	4.76%
Union Pacific	4.61%
Caterpillar	4.41%
Boeing	4.34%
Honeywell	3.43%
Emerson Electric	2.70%
Deere	2.68%

# Industry Groups- GICS Code: 20



As of 09/18/12: XLI weights 10.09% of S&P 500.  
There are 60 companies in this sector. 4

- Capital Goods- 2010
- Commercial & Professional Services- 2020
- Transportation- 2030

# Capital Goods



- Aerospace & Defense
- Engineering & Construction
- Electrical Equipment
- Industrial Conglomerates
- Machinery
- Building Products
- Trading Companies & Distributors

# Commercial & Professional Services



- Commercial Services & Supplies
  - Commercial Printing
  - Environmental Services
  - Offices Services & Supplies
- Professional Services
  - Human Resource & Employment Services
  - Research & Consulting Services

# Transportation



- Air Freight & Logistics
- Airlines
- Road
- Rail
- Sea

# Sector Sensitivity



- Very sensitive to overall economic conditions
- Mostly cyclical industry
- Broad base of companies



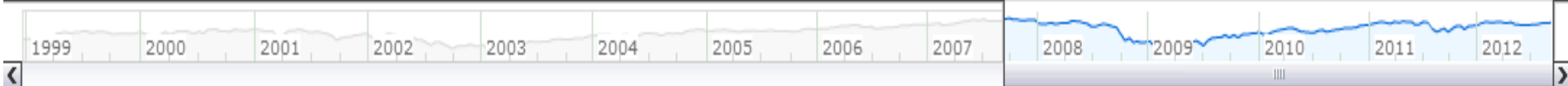
# S&P 500 Vs. \$XLI



Zoom: [1d](#) [5d](#) [1m](#) [3m](#) [6m](#) [YTD](#) [1y](#) [5y](#) [10y](#) [All](#)

Sep 21, 2007 - Sep 14, 2012

● S&P500 -1.25% ● XLI -4.50%



# \$WM Vs. \$BA



# Competitive Landscape



- U.S. offers best industrial products in the world
- Conglomerate ruled industry
- Many barriers to entry

# Global Events



- Industrials can be heavily damaged by global economic worries
- Energy Resources
- Political Risk
- Weather

# Valuation Matrixes



- Most relevant valuation matrixes<sup>5</sup>
  - P/E Ratio- 12.6
  - P/B Ratio- 2.76
  - P/EG Ratio- 1.00



# Other Relevant Points



- Free Cash Flow Growth Rate- 8.0%<sup>6</sup>
  - Previous 10 years average- 16.1%
- Inventories Growth Rate- 18.2%<sup>6</sup>
  - Previous 10 years average- 8.0%
- Median Market Cap 12.14 Billion<sup>7</sup>

# Sector Performance

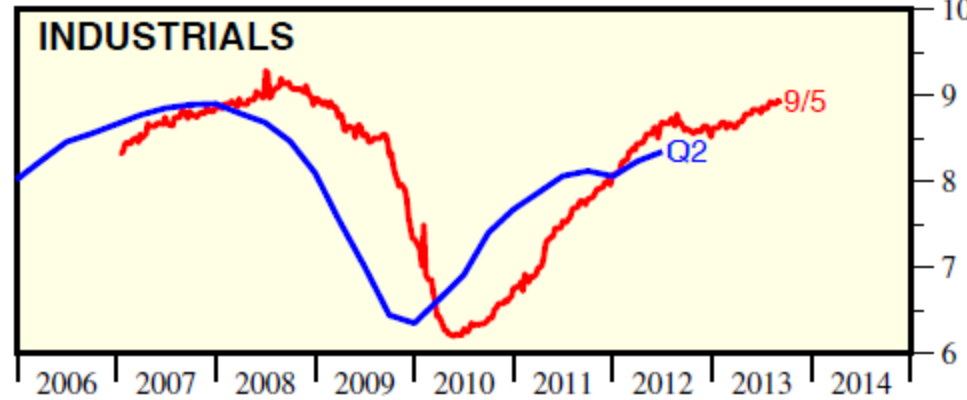
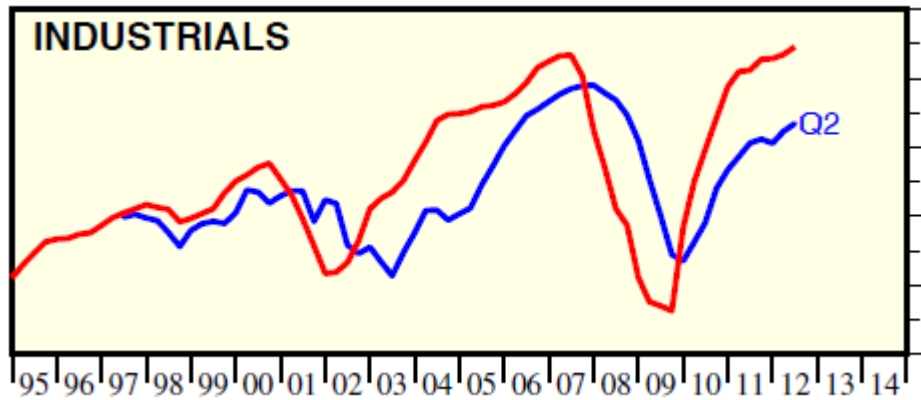


29.4%

Performance relative to S&P  
500<sup>5</sup>

## Operating Profit Margin

## Forecasted & Actual Profit Margin



Blue-Sector  
Red-S&P 500 composite

Red-Forecasted  
Operating Profit Margin

Profit Margin- 8.22% <sup>5</sup>

As of 6/30/12



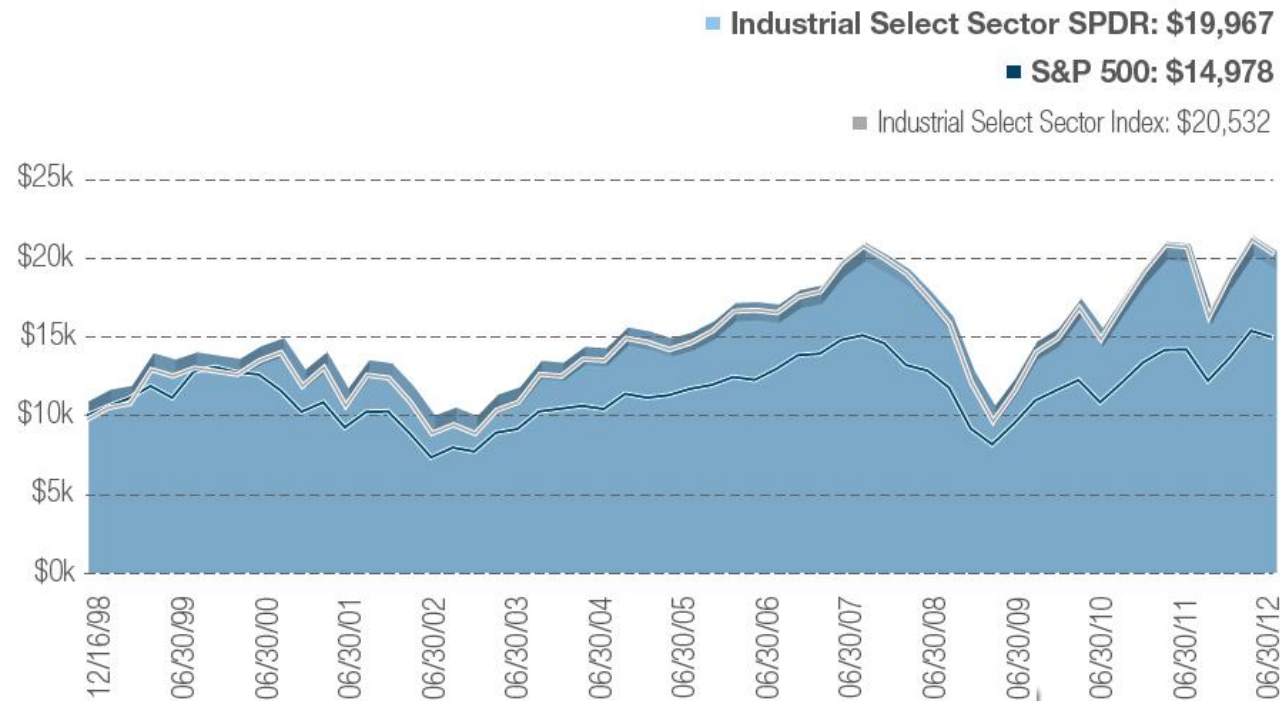
# Historical Stock Volatility



## Industrial Select Sector SPDR vs. the S&P 500 Index

### Comparison of change in value of a \$10,000 Investment

(since commencement of investment operations)



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- Beta ( $\beta$ )= 1.0

- **Aerospace & Defense stocks (DEFNS)**

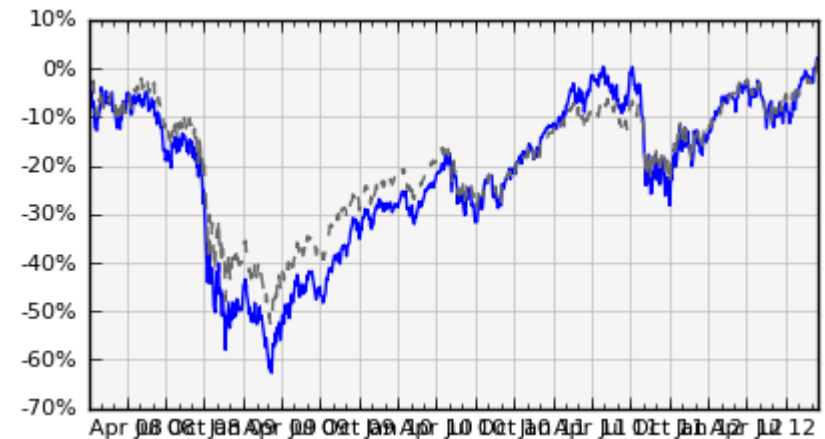
- 25.28% of sector
- Recent performance: ↓ 0.3% vs S&P 500

- **Industrial Conglomerates (CONGL)**

- 21.27% of sector
- Recent performance: ↓ 0.2% vs S&P 500

- **Farming, Mining & Construction Machinery stocks (TRCTR)**

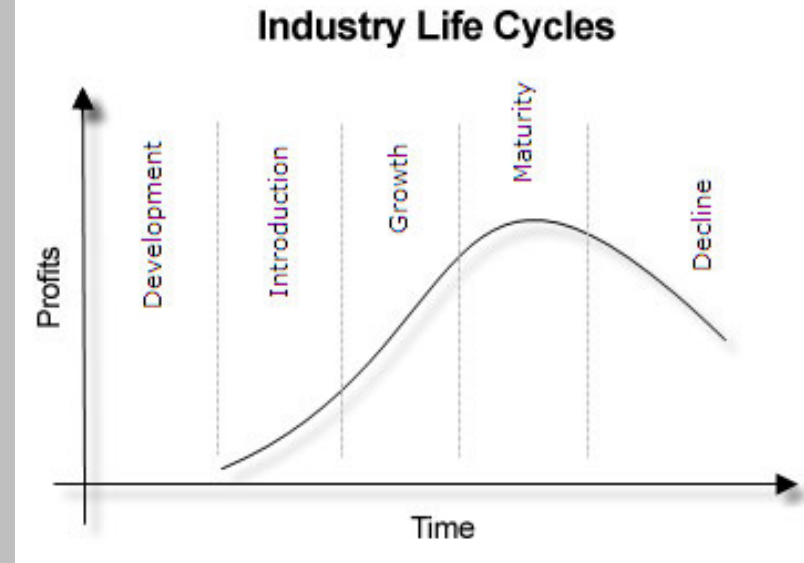
- 21.47% of sector
- Recent performance: ↓ 2.9% vs S&P 500



# Industry Life Cycle



- The Industrial sector is 100% positively correlated with the economy
- When the economy is booming, the Industrial sector does well
- When the economy is in decline, the Industrial sector suffers



- While it is opinion based, we feel the industrial section is headed into a decline



- **The Baltic Dry Index is a number issued daily by the London based Baltic Exchange. It is an overall assessment of how well or how poorly world-wide trade is going.**
  - The YTD total is currently reaching an all time low at -58.46%

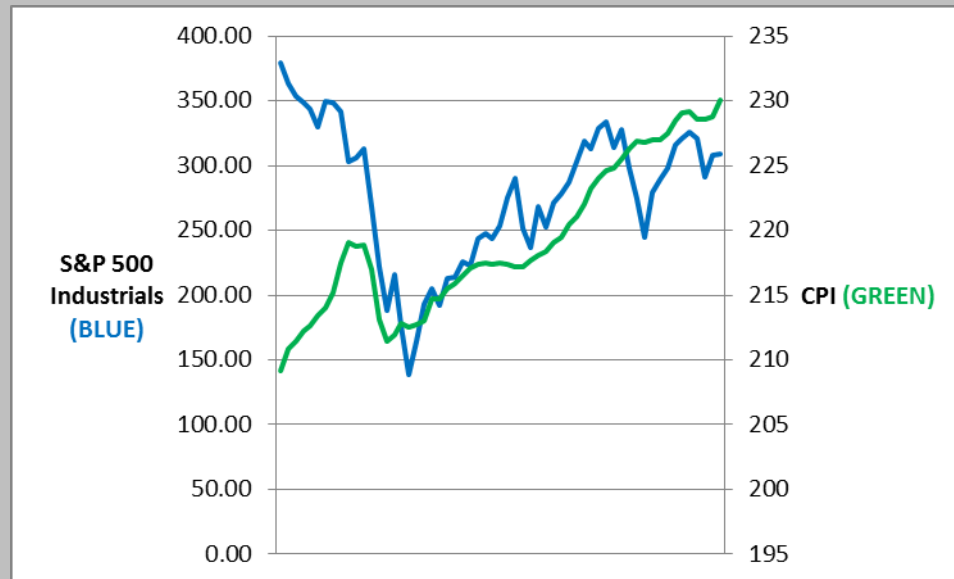


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- **This along with the current Euro crisis, the weakness of the dollar and the current problems in China prove that the economy is currently suffering. Thus the Industrial sector is on the decline.**

**\*Exception: Aerospace & Defense**

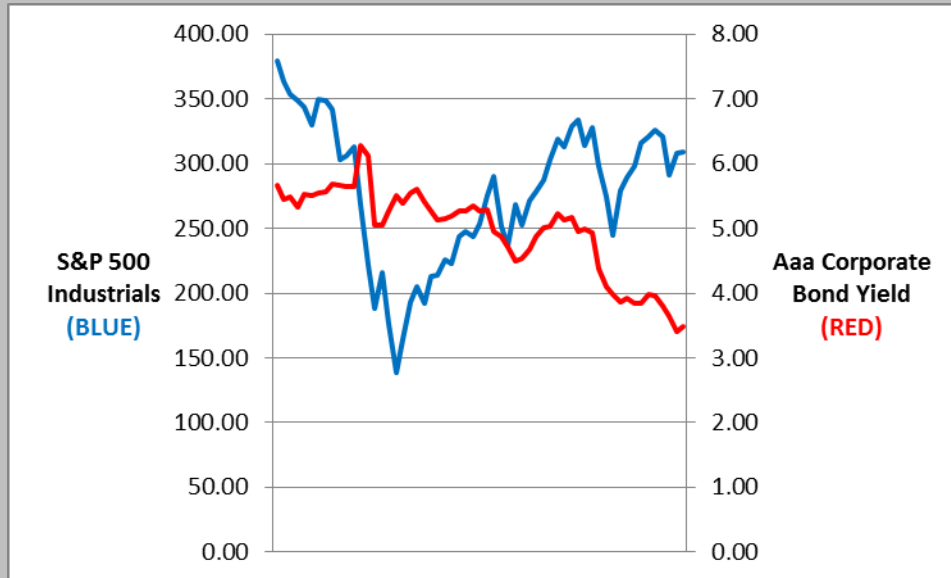
# Macroeconomy – Inflation



- QE may be a factor in increasing stock prices.
- In the short run inflation can boost stock prices.
- In the long run inflation can hurt a company's profitability.

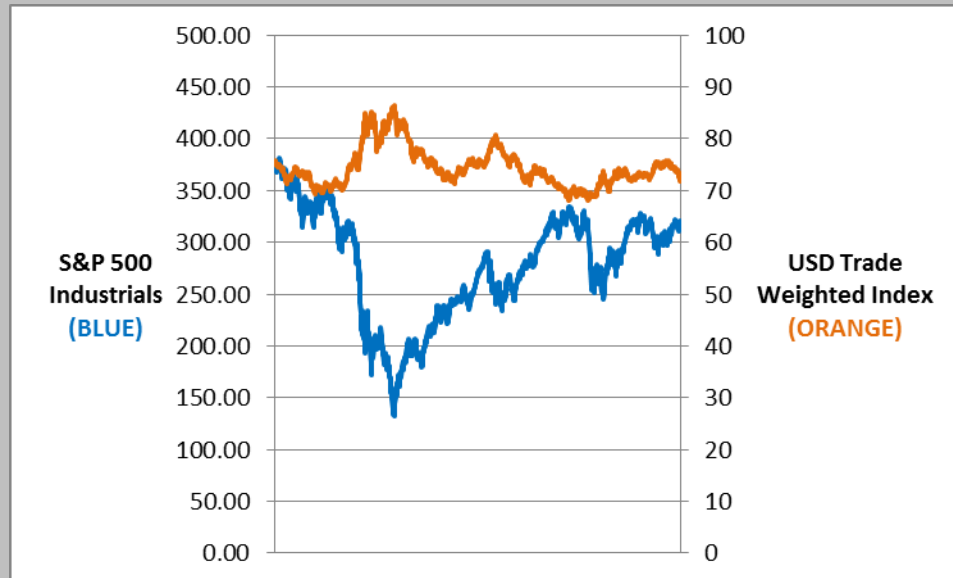
12, 13

# Macroeconomy – Interest Rates



- Lower borrowing costs = higher profits = higher growth. 12, 13
- Investors leave low yield bonds for higher returns on stocks especially stocks with high dividends.

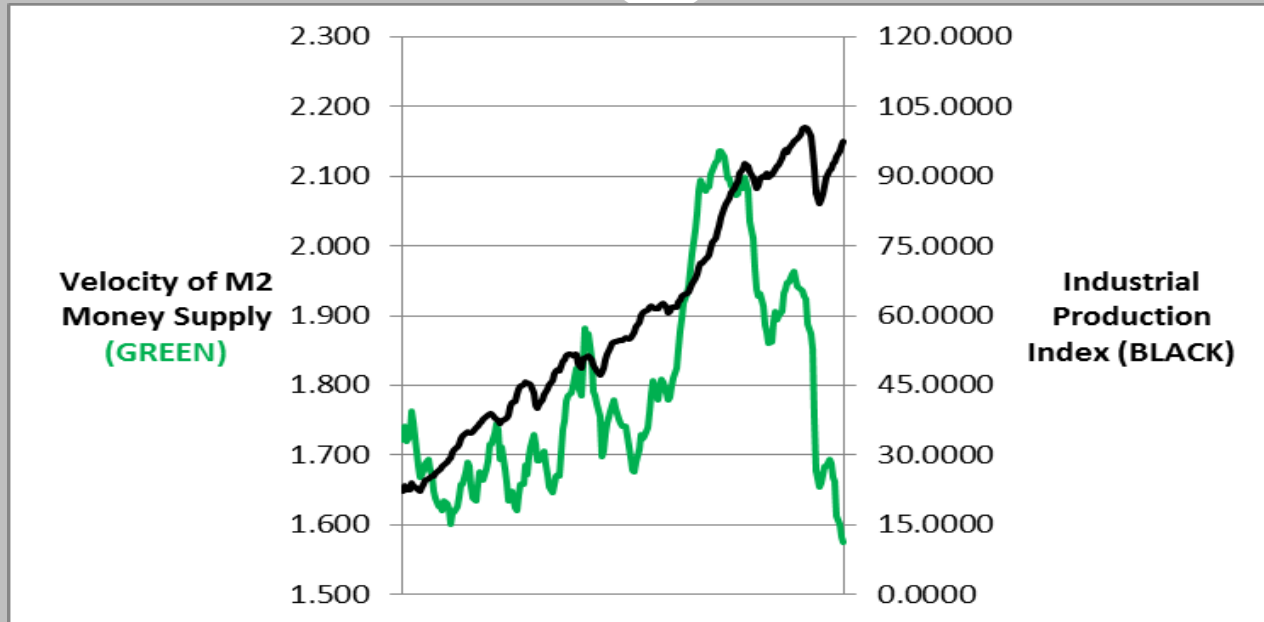
# Macroeconomy – Exchange Rates



12, 13

- Higher exchange rates lead to higher relative domestic wages and prices raw materials.
- Companies with plants in the US will see their relative costs go up when the dollar appreciates.

# Macroeconomy – Velocity of Money



- A decrease in the velocity of money causes a reduction in economic activity.
- From the graph you can see that the velocity of money has plummeted which may indicate that a sharp decline in industrial production will occur in the near future.



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