

Are wage pressures affecting the supply chain?

With the U.S. unemployment rate at cycle-lows, the latest U.S. jobs report offered investors a bit of relief from growing fears of wage inflation. A strong advance in the number of positions filled and easing average hourly earnings suggests some slack remains in the economy. Beyond the official government data, however, our 'on the ground' perspective from the North American equity research team is telling a different story.

Over the most recent earnings season, we've noticed a trend in North American consumer companies highlighting increased wage cost pressures caused by mandated minimum wage increases, and competitive pressures in retaining employees.

Most consumer companies are also highlighting rising freight costs as an earnings headwind. These increasing freight costs were already a concern prior to the severe U.S. hurricane season and this issue has subsequently worsened since then, showing no signs of abating in the near-term. Supply chains became disrupted, and then labour began migrating towards the rebuilding efforts in the Gulf states, exacerbating a driver shortage.

Trucker J.B. Hunt noted at a conference we recently attended that out of 1200 long-haul trucks in operation, 200 are currently idle due to a lack of qualified drivers. As a result, cost pressures are being passed on to their customers, with J.B Hunt reportedly achieving 10-13% contract price increases in the coming months, as compared to 5-7% in the second half of 2017. Meanwhile, in a recent meeting, CP Rail noted some transportation lanes in the U.S. where trucking rates had increased 40%. Autonomous driving will likely soften this challenge around driver availability, however this remains a number of years away before public implementation and is unlikely to be a factor during the current cycle.

These labour and freight concerns extend beyond the consumer and Industrial sectors. Forest products companies are also calling out wage pressures where southern U.S. sawmills are having to compete with Walmart for employees, and mining companies are facing similar challenges as well.

With context, we need to see this trend play out over a longer time period before this materially impacts our investment thesis. The U.S. tax bill passed in December may have had a significant impact, as companies passed along some of the corporate tax savings to their employees through wage increases and one-time bonuses. Additionally, many jobs providing last month's surge were found in lower-level positions, which should pressure wages at a lesser extent on a national level.

Our analysts will continue to monitor these "on the ground" developments as they arise with belief that investors would be well served taking a disciplined approach in looking beyond headline reporting to combine a mosaic of different data points, leading to more informed investment decisions.

Commentaries contained herein are provided as a general source of information based on information available as of March 15, 2018 and should not be considered as personal investment advice or an offer or solicitation to buy and/or sell securities. Every effort has been made to ensure accuracy in these commentaries at the time of publication; however, accuracy cannot be guaranteed. Market conditions may change and the manager accepts no responsibility for individual investment decisions arising from the use of or reliance on the information contained herein. Investors are expected to obtain professional investment advice.

References to specific securities are presented for illustrative purposes only and should not be considered as investment advice or recommendations. The specific securities identified and described herein should not be considered as an indication of how the portfolio of any investment vehicle is or will be invested, and it should not be assumed that investments in the securities identified were or will be profitable.

AGF Investments is a group of wholly owned subsidiaries of AGF Management Limited, a Canadian reporting issuer. The subsidiaries included in AGF Investments are AGF Investments Inc. (AGFI), AGF Investments America Inc. (AGFA), AGF Asset Management (Asia) Limited (AGF AM Asia) and AGF International Advisors Company Limited (AGFIA). AGFA is a registered advisor in the U.S. AGFI is registered as a portfolio manager across Canadian securities commissions. AGFIA is regulated by the Central Bank of Ireland and registered with the Australian Securities & Investments Commission. AGF AM Asia is registered as a portfolio manager in Singapore. The subsidiaries that form AGF Investments manage a variety of mandates comprised of equity, fixed income and balanced assets.