

# THE NUMBERS TELL OUR STORY

Who better to tell *EW* readers where the electrical economy has been and where it's going in the future than Herm Isenstein, the electrical market's pre-eminent economist.

**H**erm Isenstein has analyzed the electrical wholesaling industry's economic cycles for 30 years as president of DISC Corp., Orange, Conn. Since founding DISC in 1985, he has provided a generation of industry executives with the sales forecasts they need to measure market share and guide their companies. We recently got Herm's take on the economic cycles that have the most dramatic impact on the electrical market.

**In your 30 years of analyzing market data in the electrical wholesaling market for DISC Corp., has the basic mix of end user markets that electrical distributors serve changed very much?**

Technology has changed many of the products that distributors and manufacturers now sell, but distributors still serve four major end markets – the contractor, industrial, institutional and utility markets. These end markets have different cycles which respond to the cycles in the overall economy.

Even though there have been a whole raft of product changes, and other vast changes in technology, these major segments are very predictable to the extent that we are able to predict the key economic drivers of the electrical industry. If I know with a high degree of certainty how non-residential construction and residential construction are going to change, then I can tell you with a high degree of confidence how each of the key segments served by distributors is going to change and I can dig fairly deep

into the geographic layers. That is powerful information in the hands of an intelligent manager.

**DISC gave the electrical wholesaling industry ample early warning of the Great Recession. What did you see in your data that enabled you to make that judgment?**

The biggest impact for the electrical industry was in 2009

when industry sales tanked by more than 20%. We were seeing things as early as 2007 and 2008 in the overall U.S. economy that were big red flags. We weren't the only ones seeing it; there were warning signs all over the place. We saw a lot of credit being extended and over-extended. This gave rise to a bubble and a lot of people bought into that bubble. When you have a bubble, somebody is going to punch a hole in it and it is going to burst. Then it's just a ques-



tion of how fast and how far down it goes.

What set us apart from other people in the electrical industry is how we analyze the industry. We don't nod our heads when a key economic indicator like construction changes up or down. We are able to take that change and quantify how the demand for electrical distributor products is going to change. We know what makes the industry change and by how much. So when construction plunges by more than 20% as it did in 2009, we know within a few percentage points just how much industry sales are going to change.

We all know that it is not one factor but several factors that influence how the industry is going to behave. We are able to account for each of them in a very measurable way.

**By Jim Lucy, Chief Editor**



The bubble was there for all to see. Our value added is that we know what the key economic drivers are and we know how much the industry will change when those drivers change. The hard part is to do a good job in forecasting the key drivers.

**Were there any other economic events or business cycles in your 30 years with DISC that had as big of an impact on the electrical wholesaling industry?**

The American economy was coming off a huge burst of inflation in 1974 and the electrical industry had a great year. But that bubble burst. And in 1975 industry sales fell 10% which, at that time, was a record decline

and very painful for the industry. We had never experienced that previously. I can recall Kurt Kuhlman, the general manager of my division at GE, saying it was the worst day of his life when he had to lay off so many people. But as with all cycles, we recovered — 1976 and 1977 were decent years — and 1978 sales grew by fully 25%. At the NAED conferences that year everyone was all smiles.

But for distributors and vendors, the tough part is trying to stay ahead of the curve or at least stay with it so you can adequately manage your resources both on the upswing and downswing. That's the huge challenge facing decision makers in this construction-driven industry. It's all about catching the

cycle and managing your business on those terms. Our challenge at DISC is to give you the clear warning signals, up or down.

**Despite the current dip in oil prices, most economists seem to agree that the United States will be a bigger player in the oil and natural gas markets. If this country doesn't have to import as much oil and can export more of what it produces, what impact will it have on the electrical market?**

That is such a hot issue now. We have laws in place that restrict oil exports and that holds back growth in the American economy. We could be a big-time player

## MEET HERM ISENSTEIN

Herm Isenstein began building DISC's foundation in his native New Hampshire when his older brother, Stan, advised him to change his major from political science to economics at the University of New Hampshire (UNH). The chairman at UNH's Economics Dept., Professor Bill Henry, mentored Herm, and after he graduated from UNH, Henry advised him to fulfill his military commitment as an infantry officer and then return to do graduate work. Herm chose a small school with a strong economics department — the University of Rhode Island — where he was awarded a research fellowship and a full tuition paid scholarship.

After graduating with honors he landed a job as a general economist at the U.S. Department of Agriculture in Washington, D.C. In that capacity he had the opportunity to work in three key areas that were the mainstay of his career.

He worked with a team of economists analyzing and forecasting the general economy, which served as the framework for commodity specialists to develop their outlook for demand for key agricultural commodities.

He was part of a four-member task force to analyze the interdependence between the manufacturing sector and agricultural sector and how changes in the overall economy impacted each. Little did he know at the time that this analytical approach would be the basis for his now widely used MarketTrack program showing end-market demand for electrical distributor products.

Third, he projected how the agricultural industry would look in the next 15 years and 25 years. This was well received and was instrumental in his gaining admission into the graduate division at the University of Chicago.

While at the University of Chicago he received an MBA from the Graduate School of Business. He was also in the doctoral program in the economics department where he had the opportunity to study under several Nobel Prize winners, including the famed economist, Milton Friedman. One of his classmates, Bob Lucas, went on to win the Nobel Prize in Economics.

He returned to Washington, D.C., and for several years worked in the Department of Commerce in conjunction with the State Department preparing position papers for the U.S. delegation to the Organization for Economic Cooperation and Development (OECD) in Paris, France.

Herm left Washington to accept a position as an economist with the Iranian Oil Operating Companies based in Tehran, Iran. He spent four years in Tehran where he served as an advisor to the Operating Companies' efforts to promote economic development for the overall Iranian economy. At the same time, he worked with a team of economists

and engineers analyzing capital investment projects in oil producing and refining operations.

Returning from Iran in 1974, Herm went to work for GE Supply where he developed techniques to quantify the underlying relationship between the electrical industry and its key economic drivers. Cleanly segmenting the industry's major markets led to improved resource allocation and simplified the planning process. This analysis and the resulting forecasts were available to managers at GE Supply and GE's manufacturing divisions. The positive feedback he got at GE for his interpretation of how the industry is segmented and how it behaves gave him the confidence to start DISC Corp. and to provide economic forecasts and analysis to the entire electrical market.



Herm Isenstein

in the global energy market. A freer hand to export our surplus oil and gas would promote growth in the American economy and that would, of course, promote growth in the electrical industry.

There is a direct impact on the electrical industry here. Just witness how much electrical industry sales jumped in those areas with the increase in shale exploration. DISC can measure the impact and in our latest April MSA analysis we can see the strong impact of the ups and downs of exploration on electrical industry sales in areas like Fargo, El Paso, Tulsa, etc.

For the electrical industry the battle ground is always at the local level. So I prefer to look at the direct impact of energy exploration in terms of how it directly affects the areas served by distributors directly, not so much at the national level.

And, of course, demand for one industry's output requires inputs from another industry, creating a rippling effect across

all industries. Electrical distributors serve over 900 different industries and, in one way or another, whatever happens in the energy industry is going to affect electrical distributors across the board.

**One philosophical note, Nassim Nicholas Taleb made a name for himself with his bestseller, "The Black Swan: The Impact of the Highly Improbable." As an economist, what are the toughest economic cycles/environments to analyze? What sort of Black Swan economic events keep you up at night?**

That's a very hard question. Black Swan – isn't that like, expect the unexpected? In the electrical industry it's all about trying to figure out where you've been, where you are now and where you're going. In this industry there is a paucity of industry data and little or no hard product data. So it's hard for vendors, reps and distributors to know with

certainty what the past looks like and what the future holds. I like to think that DISC has contributed to everyone's understanding about the industry's past, present and future. But I'd like to make a solid contribution on the product front and with a little hard data I think I can do a lot with it.

But truthfully, what keeps me up at night is the responsibility I feel whenever I release a new outlook. I recognize many businesses rely on what I project and their profitability as well as the welfare of their employees are influenced in some way. It's not only a matter of pushing the send button and letting the numbers drop out. I revisit every update three ways to Sunday before I let go. And I know I am going to miss sometimes. I just want to be confident that I am steering the industry in the right direction and we are in the right ball park. I want to continue to do that.

*(Continued on page 36)*



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