

CURRENT BUSINESS TRENDS

February 15, 2007

by Dr. Brian G. Long, C.P.M.

(269) 323-1531

Back to flat. That's the latest word on the Greater Grand Rapids economy, according to the data collected in the third and fourth weeks of January. Our index of business improvement, which we call **NEW ORDERS**, bounced up to +5 from -13. However, the **PRODUCTION** index remained negative at -11, only a little above the -15 we reported last month. In a similar pattern, activity in the purchasing offices, which we record as our index of **PURCHASES**, remained negative but edged up to -12 from -16. **EMPLOYMENT** followed the same pattern, and moderated to -6 from -10. Overall, the good news is that the temporary slide from our last report has stopped. The slight improvement in **NEW ORDERS** will probably improve our other statistics over the next couple of months. However, we may hover around this same "flat" economic performance level for the next few months.

Looking at individual industries, it is no real surprise to find that the majority of our auto parts suppliers turned in negative reports. Production schedules have been cut for 2007, and the fear looms for even more cuts. The reports from office furniture firms were slightly positive, and most firms are doing well. Industry groups that reported widely mixed business conditions include capital equipment, where some firms still have a good backlog, but others see their backlogs disappearing. For distributors, the month was generally flat.

At the national level, the February 1 press release from the Institute for Supply Management, our parent organization, remained below par. ISM's index of **NEW ORDERS** remained negative at -1, only slightly better than the -3 reported last month. The **PRODUCTION** index turned back to negative at -3, down from +0. For what is now the fifth consecutive month, the **EMPLOYMENT** index remained at -4, unchanged from the previous month. ISM's overall index dipped to 49.4, down from 51.4. Since any index below the all-important level of 50.0 depicts economic contraction, it can now be implied that the industrial side of the U.S. economy is **SLIGHTLY** negative. However, ISM's January 5 press release of non-manufacturing activity showed **NEW ORDERS** for the service sector edging up to +5 from +4. ISM's composite non-manufacturing index advanced to 59.0 from 56.7.

At the international level, the J.P. Morgan survey of world manufacturing shows a similar pattern. **NEW ORDERS** eased modestly to 53.1, down from 54.0. JPM's overall index fell to 52.4 from 53.4, confirming the slight slowing of manufacturing activity around the world. However, JPM's non-manufacturing index edged modestly higher to 56.4 from 56.2, confirming the pattern of the ISM survey.

By now, all of the business periodicals have spread the news of the loss of 13,000 jobs in Daimler-Chrysler's version of the St. Valentine's Day Massacre. With no major Daimler-Chrysler production on this side of the state, the **LOCAL** impact of this announcement will be minimal. Since our side of the state produces automotive components, our economic well-being in the automotive sector is tied to automotive sales and automotive production. Since the so-called Big Three have already announced production cuts, our local automotive firms have already been adjusting to the impact for some time.

Unfortunately, the news on the sales side of automotive is not good, and may foreshadow more production cuts. In the February 1 press releases for the January sales period, Ford posted a sales decline of 19%. For General Motors, the decline was 16.6%. Chrysler posted a year-over-year sales increase of 3.2%, but most of this increase came from the sales of 2006 vehicles still on dealer lots. Even now, nearly half of the 2006 production run for some Chrysler lines remains unsold, even though the 2007 models have now been out for five months. However, much as we have come to expect, Toyota sales for the same period were up 9.5%. One major West Michigan auto parts producer, who now has 20% of their business with Japanese nameplates, says that they plan to move most of their business in this direction over the next 10 years in order to survive and prosper.

On the inflation side, many of the survey respondents reported a flurry of attempts to raise prices on or about January 1, 2007. Most of these requests (or demands) for price increases were rejected. However, a few slipped through, resulting in the index of **PRICES** for the ISM national survey edging up to +6 from -5, and the Grand Rapids survey rising to +5 from -1. In Southwestern Michigan, the index moderated to +4 from +9. What is **MORE** significant is that the list of items reported on "down" side in all three surveys continues to grow, and includes big-ticket items like copper, brass, aluminum, plastic resins, carbon steel, petroleum products, and transportation services. Cost reductions for these types of commodities have a significant impact on the bottom lines for many firms.

In summary, business conditions for the west side of the state remain flat, but are much stronger than those on the east side, where numerous plant closures are making the economy much weaker. Manufacturing activity is slowing for the nation as a whole, as well as the rest of the world. It is worth repeating that there is still no sign that the national economy is sliding into a recession, although the growth rate for all of 2007 will probably be down. It is also possible that we may have a Michigan recession, but West Michigan will come out ahead of the rest of the state.

COMMENTS FROM SURVEY PARTICIPANTS

"We are concerned about the outlook for 2007. Sales for January so far are very slow."

"January has been slow, but we are seeing some strength in the future."

"It's going to be a tough year AGAIN for automotive."

"The residential building industry is still slow."

"Production remains down but, will be picking up soon as an influx of new orders hit the floor."

"January looked real strong. However, we are headed into our traditional slow period."

"Our sales are right on forecast this month."

"A lot of quotes, but no new orders. Sure hope this changes soon!"

"The results from this year's first product shows are encouraging. We have a major show coming in February, which may determine how the entire year will bode for us. Our foreign market is expanding into new geographic regions."

"Flat describes it best. Many inquiries, but no funding."

"Transportation funds are declining 20-30%. Operating costs are up around 20%, employees are down by 7-8%. We are just trying to maintain adequate level of service."

"Out backlog looks pretty good. We are doing pretty well, but are reluctant to hire."

"Sales are good. Unfortunately, profit is lacking. Automotive is a tough racket to be in."

"I always forget that our industry 'slows down this time every year.' It seems slower however. It's not as much fun anymore!"

"We see a slight dip in sales. Some days are good and others are way off. Forecasting is difficult."

"We are projecting a possible 25% increase in sales for 2007."

"We continue to experience approximately 4% price increases from suppliers even though most commodities are stable."

"Price increase requests have been put on the table for select components such as pumps and motors. We have been successful in refusing the increases for several years, and companies are continuing to try to pass them on. Softening raw materials have given us some leverage in denying the increases, but the threat of competition is a bigger deterrent. We have had good success keeping prices steady and even getting reduction when the current suppliers realize they will lose the business."

"Tourism has been hit hard with the state's economy and lack of snow over the holidays."

"We are having capacity issues with our suppliers, which is driving up the cost."

	UP	SAME	DOWN	N/A	Jan. Index	Dec. Index	Nov. Index	13 Year Average
Sales (New Orders)	33%	36%	28%	3%	+ 5	-13	- 3	+16
Production	17%	44%	28%	11%	-11	-15	-11	+16
Employment	22%	50%	28%		- 6	-10	+ 5	+10
Purchases	19%	50%	31%		-12	-16	-14	+ 9
Prices Paid (major commod.)	19%	70%	11%		+ 8	+ 4	+ 8	+13
Lead Times (from suppliers)	11%	83%	6%		+ 5	- 1	+ 0	- 7
Purchased Materials Inv. (Raw materials & supplies)	22%	51%	19%	8%	+ 3	-17	+ 0	-10
Finished Goods Inventory	17%	58%	11%	14%	+ 6	-19	- 9	-11

Items in shot supply: Castings, melanine, 2007 trucks, construction equipment, pearlescent pigment, new orders, xylitol.

Prices on the UP side: Stainless steel, styrene, some aluminum, stainless steel, brass fittings, polyethylene, resins, nickel, powder paint, brass, bronze, fiberglass, vehicles, paper products, emulsions, truck parts, sand, salt, corrugated, metal, limestone, traffic signs, polypropylene, plasticizer.

Prices on the DOWN side: Carbon steel, copper, steel, OSB board, labels, polypropylene, glass, carbon steel, brass bar, aluminum bar, some aluminum, natural gas, oil, copper, foam, aluminum extrusions, die castings, gasoline, trucking costs, computers/technology, metal sheeting, PVC, particleboard.