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CURRENT BUSINESS TRENDS

January 15, 2007 by Dr. Brian G. Long, C.P.M. (269) 323-1531

Down again. Unfortunately, that's the latest word on the Greater Grand Rapids economy, according to the data collected in the third and fourth weeks of December. NEW ORDERS, our index of future business activity, retreated to -13, down from -3. The news was no better for the PRODUCTION index, which slid to -15 from -11. Activity in the purchasing offices, which we record as our index of PURCHASES, remained below par at -16, down from -14. Even the index of EMPLOYMENT, which had remained fairly steady up until now, edged negative at -10, down from +5. Overall, this is not the way we had hoped to start 2007. However, it is worth noting that the nation as a whole is not sliding into a recession. We may, however, be sliding into a Michigan recession.

Turning as we always do to a look at individual industries, it is no surprise that our local auto parts producers were either flat or sharply down. For the office furniture business, most of the reports were flat. The term "flat" also applies to the capital equipment manufacturers, as well as the industrial distributors. The only industrial group that continues to do very well are the firms associated with defense contracting or any form of aerospace.

At the national level, the January 3 press release from the Institute for Supply Management, our parent organization, still showed the industrial economy running below par. ISM's index of NEW ORDERS remained negative at -3, only slightly better than the -5 reported last month. The PRODUCTION index came back to +0 from -4. For the fourth consecutive month, the EMPOYMENT index remained at -4, statistically about the same as the -3 in the last report. ISM's overall index flipped back above the all-important level of 50.0 to 51.4, up from 49.5. J.P. Morgan's Global Report on Manufacturing, which computes an average of business condition for 23 industrial nations, came in 53.9, up slightly from the 53.3 reported last month. For the non-manufacturing sector, the index reported in ISM's January 4 press release came in at 57.1, just slightly lower that the 58.9 reported last month. All of these numbers tend to confirm the slowing of both the national and international economies. Furthermore, there is no sign of a recession anywhere in the world, assuming that something does not worsen the situation in the Middle East.

After months of speculation, Toyota has announced that it will not build a new engine plant in Michigan, or for that matter, anywhere else. However, in part because of heavy lobbying efforts by both Kentucky and Alabama, the existing engine plants in Georgetown and Huntsville will be expanded. Toyota plans to build 30% more vehicles in North America by the end of 2008, which means that the existing assembly operations will require 30% more component parts. This is good news for our local auto parts suppliers who are already supplying Toyota, and presents an opportunity for those who do not currently have Toyota business.

However, for those firms continuing to supply the so-called Big Three, the news is not good. On December 31, the sales tallies are recorded for every year. For 2006, sales were down 8.0% at Ford, 8.7% at General Motors, and 5.5% at DamlerChrysler. The prospects for the next few months look grim, given that incentive programs have run their course, and production schedules have been cut to match the anticipated slow sales.

Turning to a brighter topic, the prospects for reduced inflation are quite good. In our Southwestern Michigan survey, the index of PRICES came in at +9, down from +18. For the Greater Grand Rapids survey, PRICES retreated to +4, down from +8. The greatest improvement was at the national level, where ISM's index of PRICES sank to -5, down from +7. Remember: Negative numbers for the index of PRICES are good! It is also significant that the lists of commodities "Up" in price is growing shorter for all three of these surveys, and the lists of commodities "Down" in price are growing longer.

Since inflation heavily influences interest rates, all of this information tends to build a case for the prospect of a rate cut sometime in the near future. However, at least one member of the FED has recently expressed concerns about RISING inflation. If he can convince the other FOMC members that inflation is still a problem, then we will probably see interest rates remain about the same for the first half of 2007. Furthermore, many economists are more concerned that any rumor of a rate cut could put pressure on the dollar in the international currency markets. A gradual decline in the value of the dollar stimulates exports, but a collapse in the dollar would cause a financial panic.

Now that 2007 is well underway, where do we go from here? First, almost everyone agrees that the uncertainty over the replacement for the Single Business Tax is seriously hurting efforts to attract new business to come to Michigan or for encouraging existing business to expand. Since businesses make expansion decisions based on projected costs and projected taxes, not knowing the future makeup of Michigan's tax structure is severely restraining business expansion just at a time when it is needed most. Second, the decline of the Big Three will continue through 2007 and beyond, resulting in further job losses throughout the state, although our side of the state will probably fare better than the state as a whole. Although the national economy will probably be slow for the first half of the year, lower oil prices as well as falling prices for other key commodities will offset the temporary weakness in the housing sector. Unfortunately, Michigan will continue to lag behind the rest of the country.

COMMENTS FROM SURVEY PARTICIPANTS

"We're flat due to the year-end, with no indication one way or another, short term or long term."

"It's still an uncertain future in the OEM 'E to order' manufacturing world, but we are stable."

"Things have slowed considerably for the holidays. Even though we had a record year, we are looking at a slow December and first quarter."

"Military sales have no end in sight. Even if (a Big IF) the USA pulls out of Iraq, our NATO allies will need to support Iraq infrastructures through USA military products. Our parts depots must be low on spares, and service parts will go on for years."

"Our sales are up 50%, over 2005!! 2007 looks to be just as good as 2006."

"A soft ending for the year. The first quarter of 2007 also looks slow."

"Hope the new year brings more orders!!"

"Will we see more extended Christmas shutdowns, such as Chrysler?"

"Status quo. This looks like a slower holiday season than last year."

"Lots of people are trying to use up year end budgets, and have pushed orders up. We'll take them!"

"We were not able to match 2005 sales in 2006. With a new focus on rep strategy, new products, and a record breaking backlog, we anticipate a strong 2007."

"We were hoping for a flurry of orders from companies whose fiscal year ends December 31. Not yet!"

"We will end 2006 with sales increases of 12-13%. We have had a good year."

"We are seeing some good signs of the economy improving ever so slightly."

"Hectic!!"

	UP	SAME	DOWN	N/A	Dec. Index	Nov. Index	Oct. Index	13 Year Average
Sales (New Orders)	24%	37%	37%	3%	-13	- 3	- 8	+16
Production	16%	45%	31%	8%	-15	-11	- 9	+16
Employment	16%	64%	26%		-10	+ 5	- 2	+10
Purchases	18%	48%	34%		-16	-14	-17	+ 9
Prices Paid (major commod.)	13%	75%	9%	3%	+ 4	+ 8	- 4	+13
Lead Times (from suppliers)	9%	81%	10%		- 1	+ 0	- 2	- 7
Purchased Materials Inv. (Raw materials & supplies)	32%	45%	15%	8%	-17	+ 0	+ 0	-10
Finished Goods Inventory	32%	45%	13%	10%	-19	- 9	-13	-11

Items in shot supply: Zinc, armor plate, some plastic resins, some particleboard, some stainless steel, large construction equipment, salt, some Allen Bradley electrical components.

Prices on the UP side: Stainless steel, zinc, corrugated, phenolic urethane, styrene, powder paint, electrical components, brass fittings, aluminum die castings, nickel, cobalt, some plastic resins.

Prices on the DOWN side: Carbon steel, copper, steel, OSB board, wood, skids, steel tubing, major electronics, computer equipment, services, some parts, some particleboard.