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Current Business Trends

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Modest growth continues for West Michigan

Modest growth continues. That's the latest word on the West Michigan economy, according to the data collected in the last two weeks of January of 2015. Our closely watched index of business improvement, which we call NEW ORDERS, remained unchanged at +13. The PRODUCTION index remained positive but retreated to +13 from +19. In a similar move, the EMPLOYMENT index eased to +19 from +23. However, activity in the purchasing offices, our index of PURCHASES, edged up to +17 from +13. Hence, the pattern of slow growth that we have seen since the recession recovery began over six years ago continues on track.

Although our numbers remain positive, many of our local industrial groups reported mixed results for January. The automotive parts producers continue to do well, although a couple of firms have reported that some segments of their business have flattened out or declined. Some segments of the office furniture business have also turned mixed, partially because of the rush toward the end of the year to use up budgets which shifted sales to December from January. However, Mike Dunlap's January Furniture Industry Index came in at the second best level since July of 2007. In general, the smaller office furniture firms are outpacing their larger counterparts. Among the capital equipment firms, January sales for some firms came in stronger than expected. For the industrial distributors, the results for the month were mixed.

The February 2, 2015 press release from the Institute for Supply Management, our parent organization, repeated the caution that the national economy now appears to be growing at a slower pace. ISM's index of NEW ORDERS remained unchanged at +7, but down significantly from November's +23. The PRODUCTION remained in single digits, but edged up to +9 from +7. Two of ISM's indexes, namely BACKLOG OF ORDERS and NEW EXPORT ORDERS, turned negative for the first time in many months. ISM's overall index drifted downward to 53.5%, a drop of 1.6%. The survey author notes that the slowdown in export orders brought on by the strong dollar has had an impact on some industries.

Markit.com, the international consulting firm based in London, has a similar perspective of the U.S. economy. Markit's "Purchasing Managers' Index" or PMI, remained unchanged at 53.9, which confirms the slowing noted in the ISM report. The survey author writes:

"...the sector remains in a lower gear compared to that seen last summer. Factory output growth and job creation remain well below last year's peaks, adding to the suspicion that the pace of economic expansion in the first quarter could even fall below the 2.6% rate seen in the final quarter of last year."

The J.P. Morgan report on Global Manufacturing, released on February 2, 2015, continues to depict a stagnant world economy. However, most of JPM's

December statistics came in modestly higher. The index of NEW ORDERS edged up to 52.2 from 52.0. The

PRODUCTION index rose to 52.7 from 52.0. Adding everything together, the overall PMI rose to 51.7 from 51.5. Countries doing better included Germany, Spain, the Netherlands, and Ireland, while France, Greece, Russia, and Austria were lagging.

Gasoline prices appear to be stabilizing at the present level of around \$2.00 per gallon, and the general public is very happy with the lower prices. Many consumers apparently do not think that the lower prices will last all that much longer, because surveys show that motorists are opting to save at least part of the new liquidity rather than spend it. However, for many industrial customers, lower prices for most petroleum products has resulted in windfall cost savings. Over the past few months, the prices of numerous oil-based products have fallen by 5% to 10%. Because of lower diesel prices, freight and other transportation costs have fallen. However, despite the cost savings, most firms are not investing in new plants or equipment, at least for the short run.

Industrial deflation is clearly upon us. Our index of PRICES for January fell to -16, the lowest it has been since the recovery from the Great Recession began. More troubling is the ISM index of PRICES, which fell to -30. The ISM database shows the history of the PRICES index for 805 months since January of 1948. Of those 805 monthly reports, only 21 logged an index of 30 or below. Needless to say, all of these 21 reports occurred during recessions. It is uncertain what all of this means at this time because we are in uncharted territory. For all 21 of the aforementioned reports, the price drops occurred as a result of the respective recessions. Right now, we have industrial prices falling, but no recession.

Since our last report, the Greek government has been taken over by a far left party that promises to eliminate the austerity program put in place to overcome the debt crisis which began five years ago. However, the interest rate on Greek bonds has risen to about 11% to 12%, compared to the 5% rate of six months ago when the economic situation seemed to be stabilizing. The creditors (primarily German) are still insistent that the Greek government honor the previous agreement, setting the stage for a major confrontation. Most observers feel that there is room for at least some compromise, but the myriad of egos and personalities that will need to find common ground make predicting an outcome almost impossible. For Greece, the worst case would be to default, which would almost certainly be followed by the "Grexit," i.e., the exit from the Eurozone currency back to the 2,500 year old Greek drachma. If this were to occur, it would create a few months of tension in the financial markets. A military junta took over the government in 1967 and did not offer free elections again until 1974. If the internal situation seriously deteriorated as a result of the Grexit, it is speculated that the military would take

control again. Again, we can hope that wiser minds will somehow prevail.

In other economic news, it has been widely reported that unforeseen problems are now developing because of the U.S. dollar which has been rising in value. To the casual observer, the strengthening of the dollar would seem to be positive. However, the strong dollar has made our exports more expensive to the rest of the world, resulting in lower demand. In a different light, the currency escalation has hurt the income statement for firms with overseas operations. This includes about half of the S&P 500. As the dollar rises, all U.S. goods cost more for foreign buyers, including farm commodities like soybeans which are about 60% dependent on exports. Conversely, foreign goods become cheaper, putting pressure on our domestic producers to keep prices low—or lower. The Federal Reserve HAS been planning on slowing raising interest rates later in the year, but doing so may exacerbate the situation.

Another pleasant surprise from late 2014 has been the steady improvement in the West Michigan unemployment numbers. The Kent County jobless rate fell to 3.4%, the lowest it has been in 17 years. For Kalamazoo County, the rate of 3.9% unemployment was last seen in July of 2002. Ottawa County came in at 3.6%. Some of the municipal units posting good numbers include the City of Kentwood at 3.1%, City of Portage, 3.0%, Plainfield Township, 2.2%, and the Allegan segment of Holland at 1.7%. With the current national unemployment rate of 5.6% and the State of Michigan level of 6.3%, these statistics are clearly positive.

January 2015 COMMENTS FROM SURVEY PARTICIPANTS

“Hot start to the new year!”

“We are entering the slow time of year for our business.”

“The road networks continues to deteriorate at a faster pace than improvements can be made. Within 10 years, nearly 50% of the roads will be in poor condition. Legislatures have decided to leave it up to the voters with a transportation funding proposal that has so many twists and turns that voters will find it hard to decipher. Could be interesting!”

“We are working through a bow wave right now.”

“Material prices continue to slide. I’m surprised how fast and how much prices have come down.”

“Inquiries are picking for up first quarter. I hope the world economy follows suit.”

“We are seeking cost reduction activity through VAVE while commodities are low in price.”

“We see a slight softening.”

“We are still doing well here and expect more of the same for 2015.”

“Our 3-5 year outlook is very strong. We are looking to cut a lot of cost out of this year’s budget.”

“Business is booming. We are trying to catch up in our shop.”

“We have a strong start to 2015!”

“Year is off to slow start, but lots of projects are being quoted for potential work in 2015.”

“Sales are up versus December as expected, but under sales plan. A big increase in new order entry should boost the second half of month along with February.”

“For oil based products, we are beginning to see 5-10% reductions in finished goods made from base oil.”

For auto sales, January turned out to be one of the strongest months in recent years. Leading the pack of the major brands was General Motors, up 18.3%, followed by both Ford and Toyota gaining 15.6%. Closely behind came Nissan, up 15.1%, shadowed by American Honda adding 11.5%, while Chrysler came up 10.8%. Most analysts credited the stellar performance to the sharp fall in gasoline prices, because most of the uptick was attributed to light truck sales. GM’s light duty truck sales were up 42% over last year, boosted by the introduction of two midsize pick-up trucks in recent months. GM’s sales of SUVs were up 36%. Not to be left behind, Honda’s CR-V crossover posted a 27% increase. Other factors contributing to the strong sales report included generous year-end incentives and relaxed credit standards.

Looking ahead, the economic weakness in Europe and other countries continues to be a concern. The United States now stands alone as one of the few major countries showing positive growth, but we do not know how much longer we can carry the flag. It is worth repeating that a significant recession throughout the rest of the world would eventually spill over into the United States. However, our economy continues to have enough momentum to carry us forward for the next few months. European stagnation may dampen our domestic economy, but it would take a full-blown European recession before the U.S. would be drawn in. Last but not least, we must pay attention to industrial deflation. Having SOME industrial prices coming down may be a good thing for the short term, but having ALL industrial prices fall could spell economic trouble.

“Business looks strong for the next few months.”

“We are expecting to see project activity in the petroleum markets decline based on the low oil prices.”

“The West Coast port labor disputes and bad weather are increasing our lead times, especially from the international vendors.”

“We are very concerned about West Coast ports slowdown.”

“It is starting to look like steel pricing is becoming volatile.”

“Port congestion as we approach Chinese New Year is significantly worse this year compared to prior years. We’re hoping Obama tells the West Coast Longshoremen to get back to work!”

“We are off to a good start for 2015.”

“December was up significantly over November, and brought the year to a nice close. Overall the year ended up flat compared to 2013. But, as 2013 was a good year, so was 2014. We just didn’t grow from previous year. I would not be disappointed to see 2015 maintain these numbers. January, however, is off to a slower start.”

“2014 was strong, but planned growth in 2015 is more modest-- but we are still planning growth.”

“Demand slowing a bit.”

“We are optimistic that 2015 will be another solid year.”

“Historically, the first quarter is our slow period, and so far, February and March are trending slower. We expect things to be busier in the second quarter and beyond.”

“Falling fuel prices are causing a slowdown in the energy sector and giving pause for concern how long this will last.”

January 2015 Survey Statistics

	UP	SAME	DOWN	N/A	Jan. Index	Dec. Index	Nov. Index	20 Year Average
Sales (New Orders)	30%	51%	17%	2%	+13	+13	+16	+29
Production	24%	57%	11%	8%	+13	+19	+12	+13
Employment	24%	71%	5%		+19	+23	+16	+ 8
Purchases	28%	61%	11%		+17	+13	+16	+ 7
Prices Paid (major commod.)	5%	70%	21%	4%	-16	+ 0	+ 5	+35
Lead Times (from suppliers)	20%	75%	5%		+12	+12	+16	+11
Purchased Materials Inv. (Raw materials & supplies)	22%	66%	7%	5%	+15	- 3	- 1	- 5
Finished Goods Inventory	9%	66%	16%	9%	- 7	- 6	- 9	-10
Short Term Business Outlook (Next 3-6 months)	29%	62%	9%		+20	+24	+14	-
Long Term Business Outlook (Next 3-5 years)	40%	51%	5%	4%	+35	+40	+43	-

Items in short supply: Hydrochloric acid, ocean container space, stainless steel, electronic components, skilled welders, electronic components, amines, machine shop time, anything coming from a West Coast Port.

Prices on the UP side: Ocean freight, stainless steel, aluminum, pigment, bituminous paving materials, salt, guardrail, contracting, some steel, stainless steel, freight, minor incremental first of year increases.

Prices on the DOWN side: Steel*, copper, china steel, plastics, rubber, steel, electrical components, oils, lubricants, oil based components, pig iron, natural gas, coal, most plastics, most metal grades, energy related materials, powder paint, plastic components, steel scrap, industrial gases, polypropylene, fuel, some industrial gases, PVC resin, plasticizer, SEBS resin, paraffinic oil, reseller computers, monitors, memory, gas, energy related commodities, resin, copper, carbon steel, metal surcharges, caustic soda, gasoline, transportation costs, foundry coke, commodity metals, metal containing chemicals, transportation costs.

*Note: All items marked with an asterisk are reported as BOTH up AND down by different survey participants.

Latest Unemployment Reports

(Note: Data are NOT seasonally adjusted)

	Dec. 2014	Nov. 2014	Aug. 2009	20 Year Low
State of Michigan	5.6%	5.7%	14.8%	3.1%
Kent County	3.4%	3.5%	11.9%	2.1%
Kalamazoo County	3.9%	4.1%	11.1%	2.1%
Calhoun County	4.6%	4.6%	12.8%	2.7%
Ottawa County	3.6%	3.8%	13.3%	1.8%
Barry County	4.1%	3.8%	10.9%	2.2%
Kalamazoo City	5.5%	5.8%	15.2%	3.2%
Portage City	3.0%	3.1%	8.7%	1.3%
Grand Rapids City	4.8%	5.0%	16.1%	3.0%
Kentwood City	3.1%	3.2%	10.7%	1.4%
Plainfield Twp.	2.2%	2.3%	8.0%	1.4%
Holland City/Allegan	1.7%	1.6%	3.7%	0.9%
U.S. National Official Rate	5.6%	5.8%	9.7%	3.6%
U.S. U-6 Rate*	11.2%	11.4%	16.7%	8.0%

*U-6 for Michigan = 14.2% for third quarter of 2014

Index of New Orders: West Michigan

As the name implies, this index measures new business coming into the firm, and signifies business improvement or business decline. When this index is positive for an extended period of time, it implies that the firm or organization will soon need to purchase more raw materials and services, hire more people, or possibly expand facilities. Since new orders are often received weeks or even months before any money is actually paid, this index is our best view of the future.

Latest Report +13 for the month of January, 2015

Previous Month +13 for the month of December, 2014

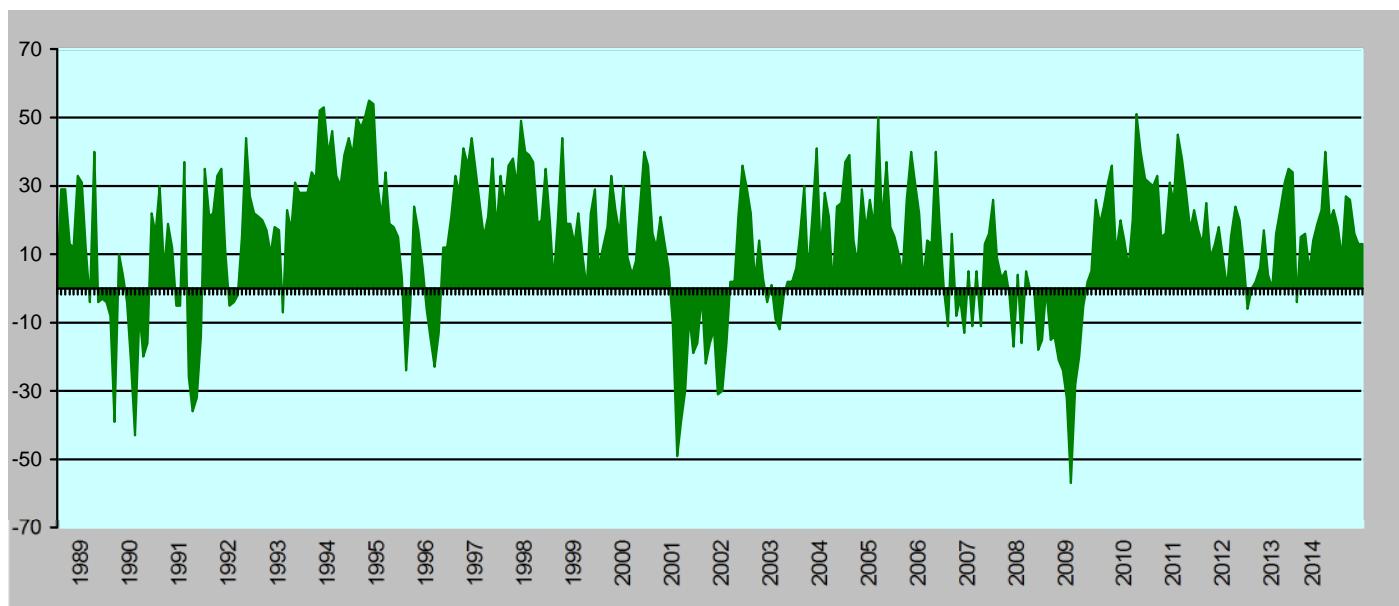
One Year Ago +14 for the month of January, 2014

Record Low -57 for the month of December, 2008

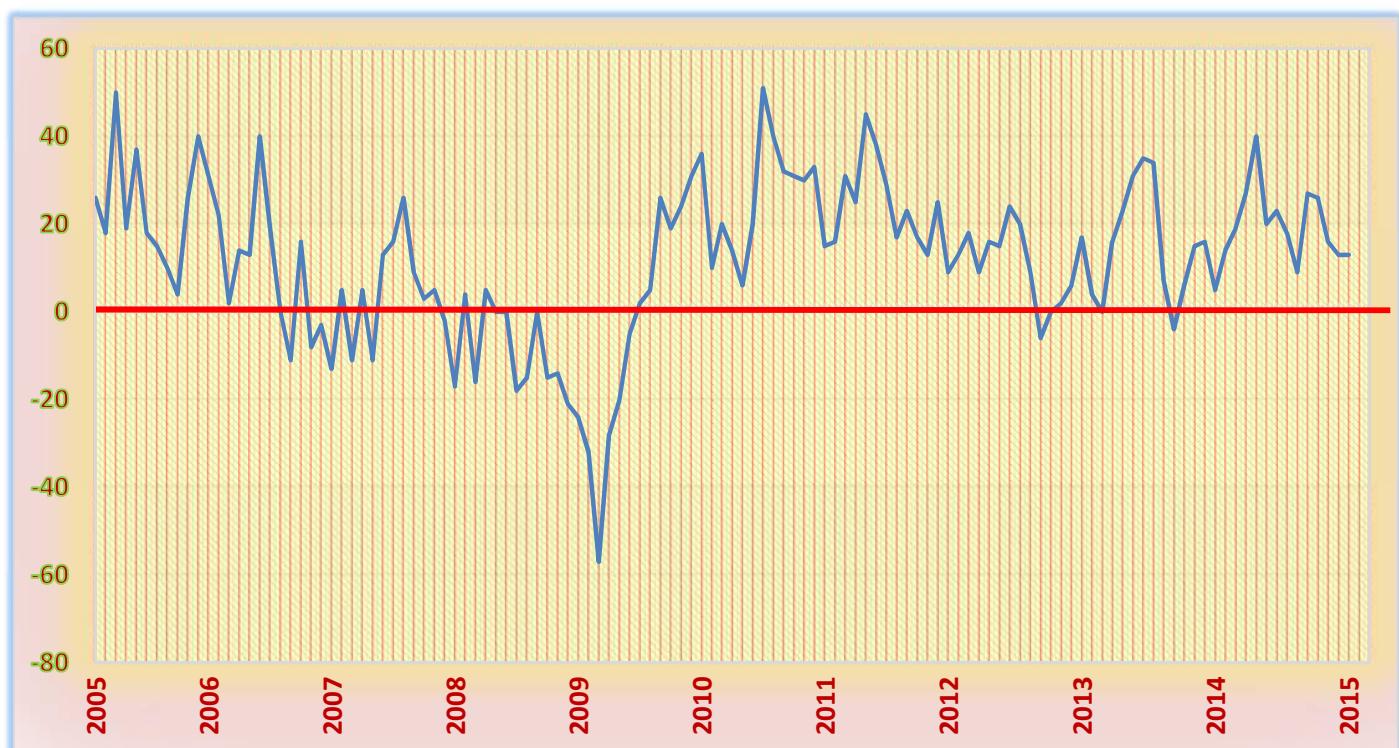
Record High +55 for the month of September, 1994

First Recovery +3 in April of 2009 and forward

ISM-West Michigan Index of New Orders 1988 - 2014

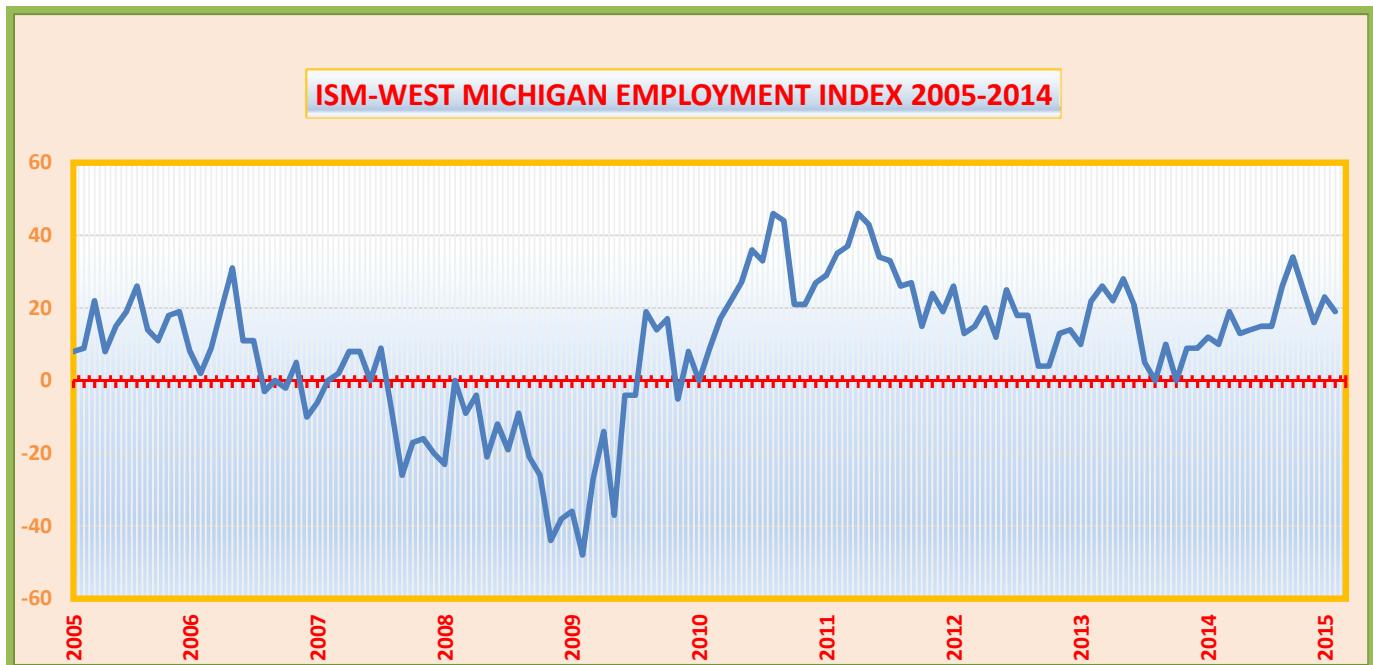


ISM-West Michigan Index of New Orders: 2005-2014 Only



ISM-West Michigan Index of Employment

The index of **EMPLOYMENT** measures the firm's increases and decreases in staffing, including permanent workers and temps. After economic downturns, it measures new hires as well as previous workers called back to work. When this index is positive for an extended period of time, it almost always signals a downturn in industrial unemployment for West Michigan. Normally, there is about a month in lag time between this report and the payroll numbers being picked up by the government statistics. However, almost all employment indexes are laggards, meaning that firms often wait until upticks in orders are confirmed before adding staff, and conversely lay off staff only after a downturn in orders appears to be certain for the foreseeable future.



ISM-West Michigan Future Business Outlook

The indexes of **LONG TERM BUSINESS OUTLOOK** and **SHORT TERM BUSINESS OUTLOOK** provide a glimpse at current and future attitudes of the business community. Traditionally, most businesses are more optimistic about the long term, although current events can result in perceptions changing very rapidly. Both short and long term attitudes reflect current business conditions, and are usually higher when sales, production, and employment are positive.

