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supply management

## Institute for Supply Management

Greater Grand Rapids, Inc.

P. O. Box 230621

Grand Rapids, MI 49523-0621

### CURRENT BUSINESS TRENDS

Dr. Brian G. Long, C.P.M.  
Director, Supply Chain Management Research  
Seidman College of Business  
Grand Valley State University  
(616) 331-7491

February 3, 2009

Still down, but not as sharply. That's the latest word on the Greater Grand Rapids economy, according to the data collected in the last two weeks of January. NEW ORDERS, our closely-watched index of business improvement, remained negative but came back to -28 from -57. The PRODUCTION index remained negative at -38, but also recovered modestly from last month's reading of -43. Activity in the purchasing offices, our index of PURCHASES, follow the same pattern and edged up to -53 from -59. The index of EMPLOYMENT remained almost unchanged at -36, up from -38. All in all, it is a relief that we did not sink below last month's record low performance. Furthermore, it was good to find that at least a few companies in our area had SOME new business come through the door after the first of the year. In fact, a few local firms are still actually hiring, even though not nearly enough to offset the job losses being reported by other firms.

As we look at individual industries, there are no surprises. Firms relating to the defense industry are still holding up fairly well, but those that are related to commercial aircraft are starting to feel the pinch. Possibly because of budget cycles, the business conditions for distributors were slightly improved. However, all of our other industrial groups, including office furniture, capital equipment, and automotive, were decidedly negative. Just like last month, there still isn't much of anyplace to hide.

At the national level, the February 2, 2009 press release from the Institute for Supply Management, our parent organization, closely tracked our local report. ISM's index of NEW ORDERS came back to -37 from last month's record low of -59. In a similar move, the PRODUCTION index also moderated to -41 from -53. The EMPLOYMENT index remained virtually unchanged at -44, down very slightly from -43. All of this moderation resulted in ISM's composite manufacturing index edging up to 35.6 from 32.9.

Turning to the international level, it is no surprise that the pattern is the same. The composite index for J.P. Morgan's Global Manufacturing Report dated February 2, 2009 rose modestly to 34.9 from 33.7. Since this is the first uptick for the index in twelve months, the survey author poses the notion that we may be at "...a point of stabilization or a possible turning point." However, he also notes that the global index of NEW ORDERS are still experiencing "...deep declines in the near-term." In addition to the United States, countries where the business conditions are moderating included China and the UK. Japan continues to be the country where the downturn in production is the greatest, although the biggest job cuts were reported in the Eurozone, Russia, Brazil, and Turkey.

We are now well into 2009, and most estimates are that the current downturn will probably parallel the 1981-1982 recession, wherein unemployment rose to 10.8%. According to Alexander Pope, hope springs eternal. At this time, all that most of us are hoping for is some kind of sign that we are at or near the bottom. As noted in last month's reports, the multiplicities of factors that have created this recession make the task of assessing the bottom rather difficult. That said, at least SOME of the clues can be found by following this report as well as the monthly report from ISM. Except for Alan Greenspan, few, if any, of the economists at higher levels in the government recognize the impact of the industrial market on the overall economy. In fact, most of the economic downturns in the past 60 years have been a direct result of negative business conditions exhibited in the industrial marketplace, including the accumulation of inventories. This is why the attempt to revive the economy with the "stimulus" checks that we all received last spring had little or no impact on mitigating the recession.

So what are the signs to watch? As we have noted since the inception of this survey nearly 30 years ago, the index of NEW ORDERS constitutes the best look we have at the future. We will be looking for both the local index and the ISM national index come back to zero. Once these indexes turn positive, firms will begin to order more materials and call back workers who have been laid off.

As we have noted for the past two reports, a major portion of the current recession has been caused by a collapse in commodity prices. Last summer, when prices for almost every major commodity were rising at a stratospheric rate, firms all over the world threw the religion of JIT out the window, and began buying excess inventory to hedge against the upward price spiral. Furthermore, hedge funds and other commodity speculators jumped on the speculation wagon, and ran many critical industrial commodities to five times the price levels of 2004. Worldwide, it is estimated that at least a trillion dollars has been taken out of the world economy by the collapse in commodity prices. Except for Alan Greenspan, almost none of the national economists are even making mention of this problem. Some commodities such as copper and aluminum are now selling at prices well below their production costs, resulting in mine closing and smelting capacity shutting down all over the world. Hence, the economy in a mining town is now almost as bad as the economy in an automotive town.

For the commodity collapse to be over, prices will have to come back to the 2004-2005 level, AND we will need to see the end of the liquidation in the RAW MATERIALS index in our report as well as the ISM report. For this index, the record low was set last month at -45. Given that this month's index came in at -42, we have a considerable distance to go before this indicator turns positive. ISM index of RAW MATERIALS remained steady at -24, not far from the record low of -29. On a brighter note, past history says that both the price recovery and the end of inventory liquidation SHOULD come to pass by this summer.

With Washington now back to work, the new president has pushed hard for a stimulus package. Unfortunately, there is little in the package for the industrial side of the marketplace. The exceptions are those provisions that are targeted to infrastructure renewal and expansion. Locally, this would mean that considerable dollars would be spent to replace crumbling bridges, and repave or expand existing streets and highways. From an economic standpoint, investments in these kinds of infrastructure are almost always good investments. In addition to employing many construction workers, the supply chain consisting of products like cement, construction equipment, and steel rebar will be stimulated at a time when these industries desperately need it. Unfortunately, most of the money for the stimulus package is being targeted at the consumer level, where it will do little good.

## COMMENTS FROM SURVEY PARTICIPANTS

"All I here is doom and gloom. We all need to think positive, and that would help more then you realize."

"Things are starting to perk up."

"We were 1/3 of the way into a new project (3.5 million) with a European automotive firm that wanted our system in their Kansas City facility when they pulled the plug on it. Not a good thing for our business."

"Quoting activity is very steady, but new orders are down. It is a challenge, but we will weather the storm."

"We had to lay off employees for the first time in years due to the poor economy. We are hoping for things to turn around."

"We have had a 10% staff reduction. 2008 was the year for inventory reductions, and 2009 is focused on cost reductions."

"Pricing is down on a few of our products, but there certainly is no demand. We are taking another three weeks out of our production schedule in February. All management, salary, and hourly people will be placed on layoff status."

"The first quarter is actually looking busy, and we are still on the fence regarding recalling laid off workers. We're trying to keep it as lean as possible. Margins are very slim."

"A few inquires for used machines are coming in. Most requests are accompanied by the statement: 'Since there have been so many companies fail in Michigan, we should be able to get a REAL deal--right?'"

"We just laid off 30 more salaried employees, which brings the total to 60 over the past 3 months. We are told that should be it, unless unforeseen events arise."

"So far, year has been stronger than expected."

"I believe it's going to get worse for the auto industry. These are scary times for sure."

"It's purely a survival game at this point, and I'm not sure we will make it."

"We hope for new orders from the new president of the U.S."

"Even though we're down in sales right now, it is typical for this time of year. We will be back on track in March."

"I can hardly stand watching the news or reading the newspapers anymore, and I'm somewhat of a news junky!"

"Even the mining and defense sectors are showing hesitation. The recession has caught up with steel fabrication of capital equipment. We are in a holding pattern, and are waiting to see what the next four weeks bring."

"Prices went up quicker than they are coming down, and in some instances, you as the buyer have to ask for the decreases as the suppliers are not very forthcoming."

"We are running ahead of our schedule to keep our employees working."

"Business is soft. It is slightly better than last month. However, it looks like we are going to have a tough first quarter."

"To date, almost 80% of our winter maintenance budget has been used. Therefore, spring & summer operations will need to be reviewed, and some projects cancelled due to the lack of funds. This will not help stimulate the contractors in this area."

"Most of my suppliers continue to increase their fuel surcharges. I'm not sure why, with pricing for oil dropping so much."

	UP	SAME	DOWN	N/A	Jan. Index	Dec. Index	Nov. Index	20 Year Average
<b>Sales (New Orders)</b>	23%	24%	51%	2%	-28	-57	-32	+29
<b>Production</b>	15%	23%	53%	9%	-38	-43	-30	+13
<b>Employment</b>	9%	47%	45%		-36	-38	-43	+ 8
<b>Purchases</b>	9%	30%	62%		-53	-59	-40	+ 7
<b>Prices Paid (major commod.)</b>	6%	32%	55%	6%	-49	-58	-38	+35
<b>Lead Times (from suppliers)</b>	6%	53%	40%		-34	-33	-17	+11
<b>Purchased Materials Inv. (Raw materials &amp; supplies)</b>	11%	26%	53%	11%	-42	-45	-31	- 5
<b>Finished Goods Inventory</b>	11%	30%	47%	13%	-36	-24	-21	-10

**Items in short supply:** Salt, casings, jobs, and customers.

**Prices on the UP side:** Cardboard, PVC resin, veneer faces, MDF, HDF, stretch wrap, powder paint, salt, chlorides, sand, guardrail, asphalt emulsions.

**Prices on the DOWN side:** Iron castings, ferrous materials, stainless specialty bar, steel, aluminum, foam, plastic molded parts, aluminum fabrication, silicon related products, resin, phenolic urethanes, copper, recycled paper, carbon steel, fuel surcharges, fuel, Curugate polycarbonate, board stock, polypropylene banding, tape, some paper, polyethylene resin, some veneer, brass, paraffinic oil, polycast resins, diesel, computer equipment.