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CURRENT BUSINESS TRENDS

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Growth rate slows, but remains positive. That's the latest word on the Greater Grand Rapids industrial economy, according to the data collected in the last two weeks of May. NEW ORDERS, our index of business improvement, moderated to +19, down from +29. In a similar move, the PRODUCTION index eased to +26 from +35. Activity in the purchasing offices, our index of PURCHASES, eased considerably to +25 from +51. Fortunately, the EMPLOYMENT index remained fairly strong at +43, down modestly from +46. However, Economics 101 tells us that employment is almost always a laggard. Given that many other indicators have pointed to slower growth for the second half of 2011, this month’s numbers are not a total surprise. It is worth repeating that all of our numbers are still positive. If this situation changes in coming months, then it may become necessary to reassess the future projection. Furthermore, some analysts now say that the housing downturn may slip further, and a full recovery could take eight to ten years.

Turning as we always do to individual industries, the office furniture sector is still positive, although some firms are clearly doing better than others. Most of our auto parts suppliers remain stable, although some report production to be a little slower because of reduced production schedules. Overall, the performance for the industrial distributors came in fairly positive for the month of May. Although some capital equipment firms reported business conditions to be the same as last month, other firms continue to improve. Similar to last month, the respondent comments at the end of this report remain positive, but there are still some cautions comments.

At the national level, the results are a little more pessimistic. The June 1, 2011 press release from the Institute for Supply Management, our parent organization, reported that NEW ORDERS backtracked sharply to +14 from +41. Although the index is still positive by double digits, the growth rate has moderated considerably. In a similar move, ISM’s PRODUCTION index eased to +16 from +38. The EMPLOYMENT index moderated to +22 from +29. ISM’s overall index of manufacturing fell considerably to 53.5 from 60.4, one of the sharpest reversals since 2008. However, the US industrial economy is now in its 22nd consecutive month of expansion, and some backtracking is to be expected.

At the international level, the J.P. Morgan Global Manufacturing report released on June 1 remained modestly positive but backtracked to its lowest level since September of 2010. JPM’s worldwide index of NEW ORDERS eased to 51.8 from 53.8. In addition to the US, growth moderated in the Eurozone, China, and India. Trade volumes hit an eight month low. The Japanese PMI rose sharply in May, indicating that recovery is now underway. JPM’s index of EMPLOYMENT remained positive but backtracked to 53.7 from 55.1. The JPM international index of PRICES retreated sharply to 66.8 from 72.3. Lest there be any doubt, it is obvious that the entire world economy is starting to slow. At the same time, there is still no evidence that another recession is at hand, unless some surprise is out there waiting for us.

For the housing industry, the bad news seems to keep on coming, even though it is now almost five years since the onset of the housing crisis. The S&P/Case-Shiller Home Price Indices, the leading measure of U.S. home prices, show that the U.S. National Home Price Index declined by 4.2% in the first quarter of 2011. After five continuous months of decline, Case-Shiller is now declaring that, “This month’s report is marked by the confirmation of a double-dip in home prices across much of the nation.” Furthermore, the report states, “Home prices continue on their downward spiral with no relief in sight.” Ouch! The author further credits the rebound in prices seen in 2009 and 2010 to the first-time home buyer’s tax credit. Fortunately, the Case-Shiller report is a national report, and almost no one in our local markets is quite this pessimistic. Whereas there is evidence that our local housing prices are now stabilizing at the present level, no one is predicting that there will be any significant increase in housing prices for many months or years to come. Nationwide, we are now building about a quarter as many homes as we did in 2006. The huge layoffs in this industry are generally permanent. Despite lower mortgage rates, credit remains VERY tight, with the average down payment now about 23%. Thank you, Dodd-Frank.

To no one’s surprise, the disaster in Japan finally caught up with the auto industry in May, although the results were not nearly as bad as some of the pessimistic projections. For the Detroit 3, sales at Ford were down by 0.3%, and General Motors fell 1%. Chrysler actually gained 10%. But the Japanese brands took a considerable hit, with Honda down 23%, Toyota down 33%, and Nissan retreating 9%. For the industry as a whole, sales fell 4%. According to industry projections, this trend will probably continue for a couple more months. If the sales situation does not deteriorate further, the overall economic impact will be minimal.

The slowing economy and the slackening of demand have produced some good news for inflation. Last month, we indicated that prices for steel were beginning to moderate, and this trend continued for most of May. Some steel producers are still trying to push through a few higher prices, but many buyers are now negotiating a few price reductions. The index of PRICES for the Southwest Michigan survey retreated to +54 from +68. In Greater Grand Rapids, the index of PRICES eased to +53 from last month’s near-record level of +73. ISM’s index retrenched considerably to +53 from +71. Several big ticket commodities like copper, brass, stainless steel, carbon steel, and zinc were reported as falling in price for some of our local buyers.

To anyone who drives a car, it is obvious that another factor dampening economic growth is the price if fuel, both in the form of gasoline and diesel. Drawing on the experience from 2008, economists noted little change in driving behavior until the price of gasoline approached $4 per gallon. For the consumer market, this means that trips to the grocery store may now be consolidated, vacations may be taken closer to home, and fuel efficient cars are now in demand. For the industrial market, it means more fuel surcharges and/or higher freight bills. For overseas buyers, the shipping cost per container has risen considerably in recent months.

One final inhibiting factor is the worldwide financial situation, flanked by the same national, provincial, and local situations throughout most of southern Europe. This includes the seemingly endless domestic budget deficits at the national, state, and local levels. The so-called PIGS (Portugal, Ireland, Greece, and Spain) countries have spent the last three years implementing various “austerity” measures and trying to restructure debt. From our perspective across the pond, they seem to have made little headway. Because of the interdependency of the world’s economy, a significant default by any of the European countries on their debt would reverberate around the globe. Would it pull the United States into a recession? This seems unlikely, but the fact is, we don’t know. What we do know is that every flare-up over the European debt situation is followed by a 100 point or more drop in the Dow-Jones.

COMMENTS FROM SURVEY PARTICIPANTS

"Quoting activity remains high. The shortest lead time gets the order in most cases."

"We're coming into a second half (2011) slowdown. "

"The commodity boom is over for a bit."

"We are not as busy as we have been, but things are getting better. We should have a really busy summer."

"We are doing well. Capital equipment is selling."

"Automotive is slowing down across the board. I'm not sure if this is related to the crisis in Japan and/or seasonal, but could help to stop the run-up of raw material prices."

"If high oil prices don't slow the economy, we will be in for a very busy summer."

"I strongly recommend avoiding PPV efforts through commodity buying and focus on strategic make/buy and value stream analysis."

"Government contracting is an extremely challenging environment right now."

"This is still a tough business in Michigan. Manufacturing took a hard and long lasting hit here, but I have been doing it too long to change."

"Steel prices seem to be leveling off."

"Another excellent month. We are hiring again to manage the growth so as not to affect customer service. We're enjoying managing the growth again."

"Gas prices are killing us both organizationally and personally!"

"The rapid pace of price increases has stopped. Fighting for decreases are the next likely steps."

"We're making hay while the sun shines. It's a very good business climate for steel fabrication."

"As export costs go up, more commodities are staying in the United States."

"The economy still appears to be slowly recovering. The ups and downs of commodity prices are still affecting the confidence of consumers. Economic balance needs to happen. I'm seeing far too many examples of higher wages and bonuses for the wealthy, and the working class is falling farther behind. The working class is the major supporter of the economy."

"Pricing on imports is up due to the run-up of material prices and weak dollar. Steel is coming back down, but steel mills are trying to hold pricing by sending increase letters to customers."

"We have a lot of concern over continuing increases in commodities and transportation pricing. Most of these increase costs cannot be passed on to our customers."

"There has been some price fluctuation in steel and steel related items. Most cost increases are relating back to the cost of fuel. Our business involves commercial freight, so we are seeing a lot of interest in weight reduction."

"Business remains strong. There is some rumbling of things slowing down, but we are not seeing it so far in our forecast."

"If quoting activity is any indication of the future, we could have a lot of work coming soon? Hopefully, this comes true because things are currently stagnant."

"Stainless steel prices are going up again in June. Prices are historic! Copper prices are very high. Wire has tripled in price over the past year."

	UP	SAME	DOWN	N/A	May Index	Apr. Index	Mar. Index	20 Year Average
Sales (New Orders)	35%	43%	18%	4%	+17	+29	+38	+29
Production	35%	51%	9%	5%	+26	+35	+39	+13
Employment	47%	49%	4%		+43	+46	+37	+ 8
Purchases	38%	49%	13%		+25	+51	+34	+ 7
Prices Paid (major commod.)	58%	35%	5%	2%	+53	+73	+73	+35
Lead Times (from suppliers)	42%	50%	4%	4%	+38	+34	+39	+11
Purchased Materials Inv. (Raw materials & supplies)	25%	61%	9%	5%	+16	+24	+27	- 5
Finished Goods Inventory	15%	50%	22%	13%	- 7	+ 9	+10	-10

Items in short supply: Some structural steel, montan wax, butadiene, PP, paraffinic oil, PVC resin, vehicle parts, heavy equipment, outsource machining capacity, rubber, products using rubber, knit gloves, PTFE fiber, anything coming from Asia.

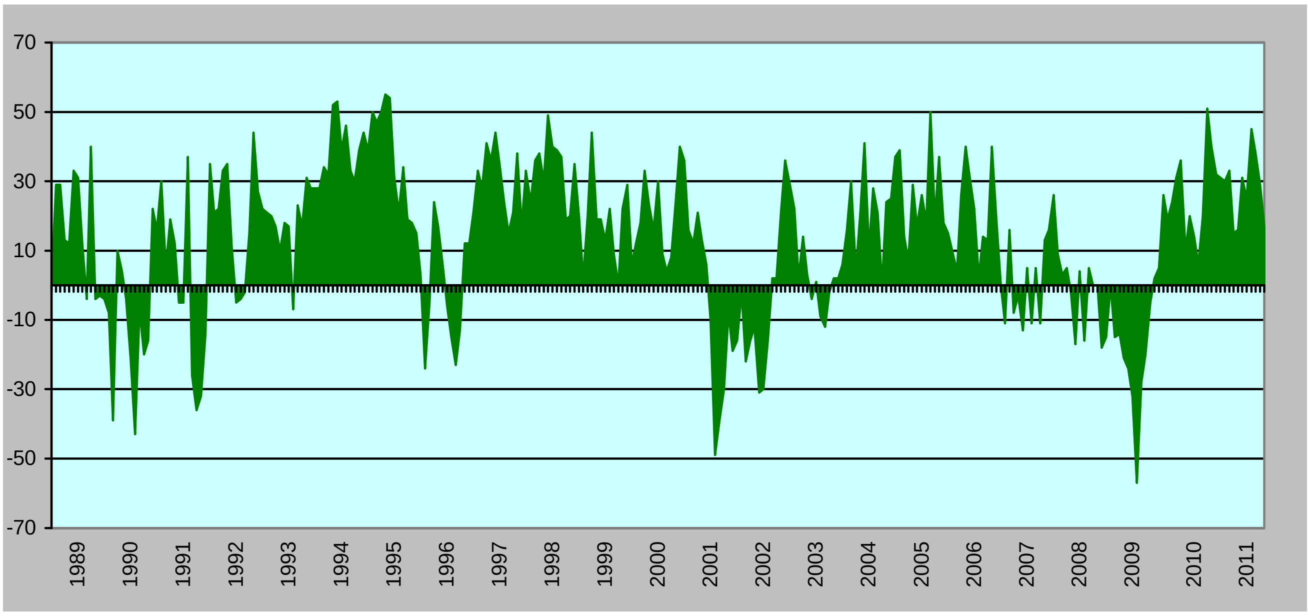
Prices on the UP side: Polypropylene, copper, steel, resins, red metals, fuel (diesel and gasoline), powder paint, hardware, motors, sprockets, bearings, stainless steel, wire has tripled, plasticizer, PVC resin, SEBS resin, paraffinic oil, UV absorbers, light stabilizers, antioxidants, anti-statics, aluminum, nickel, polycarbonate resin, bronze, brass, finish materials, polycast resin, aluminum extrusion, carbon steel, HR steel, CR steel, hydraulic oil, paper products, transportation and freight costs, salt, grader blades, metal sheeting, rubber products, adhesives, acrylic, oil based products, paints and coating, import items, fuel surcharges, brass fittings, composition seals, resin sand, fabric.

Prices on the DOWN side: Some carbon steel, some stainless steel, sheet steel, some copper, brass, scrap carbon steel, bituminous materials, aggregates, construction services, zinc, scrap steel.

Index of New Orders - Greater Grand Rapids 1988 - 2011

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	+17	for the month of May, 2011
Previous Month	+29	for the month of April, 2011
One Year Ago	+40	for the month of May, 2010
Record Low	-57	for the month of December, 2008
Record High	+55	for the month of September, 1994



Index of New Orders: 2005-2011 Only