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News Release (For Immediate Release)

June 4, 2012

Current Business Trends

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GR Manufacturing Slows Slightly

Modest growth, but slightly slower. For the month ended May 31, 2012, that's the latest word on the industrial economy in the Greater Grand Rapids area. NEW ORDERS our closely-watched index of business improvement, moderated to +20, down from +24. However, the PRODUCTION index, while remaining positive, eased considerably to +5, down from +25. The EMPLOYMENT index tapered off to +12 from +20. Staff reductions were reported by 13% of the survey respondents. The RAW MATERIALS INVENTORY index came in at -12, indicating that some firms are starting to liquidate inventories built over the past six months in anticipation of higher prices. Overall, our current statistics remain positive, but slightly less robust than what we would like to see. Although the local economy is still growing, the future is starting to look less certain than it did a few months ago.

Within our local industrial groups, automotive parts producers continue to lead the pack. With the uptick in production schedules, this industry should keep our statistics positive for a few more months. The office furniture business remains soft, but there are signs that several of the firms are stabilizing at the current level. Business conditions for the industrial distributors remain positive. Capital equipment firms continue their stable performance, largely due to the uptick in automotive. Individual comments quoted at the end of this report are still generally upbeat, yet several respondents have turned much more cautious in the last few months.

Looking at the international economy, the JP Morgan Global Manufacturing report dated June 1, 2012 continues to depict a slowing world economy. According to the JPM author, the "...rate of expansion in global manufacturing production slowed sharply in May, as growth of total orders booked remained lackluster..." The index of NEW ORDERS backtracked to 51.4 from 51.8, and PRODUCTION slid to 51.0 from 53.1. The overall indexes for the Eurozone and the UK fell to three year lows. Besides the US, the only countries to show modest growth were Ireland and Japan. The statistics in China continued to soften. JPM's global index remains marginally positive at 50.6, yet this is possible only because the economy in the US is strong enough to offset the weakness from the rest of the world.

In the last three years, we have all added "sovereign debt crisis" to our vocabularies. Across the Atlantic, the news continues to change on a daily basis. Most of Europe is now in a shallow recession based almost exclusively on the turmoil in the eurozone capital markets. As we have warned in the past, this crisis will inhibit world economic growth for months or even years

to come before it is fully resolved. France has elected a new government which intends to roll back some of the recently enacted fiscal reforms, and that does not bode well for the future. However, the big day to watch is June 17, when the Greeks will vote again to try to form a new government. It is possible that this election could turn out to be one of the most important events in economic history. The leading left wing opposition party wants to reverse the terms of the bail-out package that has already been agreed upon with the Europeans, especially Germany. If this happens, then it will probably mean that Greece will be forced out of the euro, resulting in economic turmoil. If the Greek elections go in the opposite direction, the country faces several years of austere restructuring of salaries and pensions. Either way, riots and economic instability are probable. If things get really bad, we also can't rule out a military junta taking over, not unlike the junta that ruled the country 1967-1974 during another time of crisis.

In addition to the Greek crisis, other European countries have problems of their own. Spain has been in the news most recently, but Portugal, Italy, and Ireland have similar problems. The outcome of the Greek election may well form the pattern for resolving the problems of these other countries. If the problems cannot be resolved, the euro could collapse. This upheaval and uncertainty is at the core of the European recession now unfolding. Throughout Europe, investors are simply afraid to invest and consumers are unwilling to buy while this huge cloud of uncertainty hangs over Europe and the world.

Jobs: In a political season, most politicians can't go 30 seconds without inserting this word into the discussion. Most economists agree that about 200,000 new jobs are needed per month to absorb population increases and to make a significant contribution to economic growth. Hence, last week's report that only 69,000 jobs were created in May was not good news. The national unemployment rate pushed up to 8.2%. The same report noted that job creation for the previous month had to be revised downward to 77,000 from 115,000. If this trend continues, the unemployment rate will follow suit and go higher.

In our local surveys, the job growth in the industrial sector has tapered off over the past few months. The main reason for the slow job growth continues to be the lack of qualified candidates. In fact, by some measures, help wanted advertising has increased to a HIGHER level than before the recession began. Contributing to the uncertainty are other major problems of the future, especially regarding taxes and the business environment.

Consumer confidence is either falling or rising, depending on the data source. Last week, The Conference Board reported a drop to 64.9 (1985=100), down from 68.7. However, on May 25, the University of Michigan Sentiment Index rose to a four year high of 79.3, up from 76.4. Over time, both of these indexes usually track each other. Right now, it appears that consumers are just as confused as economists about which direction the economy is going.

Another piece of bad news came from a downward revision of first quarter GDP growth to 1.9% from 2.2%. Since the fourth quarter of last year came in at a growth rate of 3.0%, there is now further evidence that the already-slow economy is slowing more. Over the long term, we need to be at about a 3.0% growth rate to be comfortable.

On the positive side, auto sales for May increased by 26% over May of 2011, fueled by added dealer incentives, easier financing, and lower gasoline prices. Toyota, now fully recovered from last year's Japanese earth quake, surged ahead with an 87% gain. Honda, which was less impacted by the March, 2011 earthquake, posted a 48% gain. For the Detroit Three, Chrysler led the way with a 30% gain, but Ford was up 13% and GM managed a 11% gain. Ford has attributed the lackluster results to an inadequate supply of cars, and has now boosted production by 5%. For our local auto parts suppliers, all of this is good news. However, it

is worth repeating our past warning that these robust sales gains are NOT expected to continue for many more months. Sometime in the late summer or early fall, the supply will catch up with the pent-up demand that has been fueling sales since the Cash for Clunkers program of 2009. Hopefully we will then settle into a more stable sales pattern, as long as the rest of the economy remains stable.

Another piece of positive news comes from the local unemployment rates on the west side of Michigan. As of April, the unemployment rate in Kent and Ottawa Counties has fallen to 6.1% and in Kalamazoo County to 6.2%. Barry County came in at 5.8%. All of these readings are well below the national and state averages, and should fall further over the next couple of months.

In summary, without the European instabilities, our economy would now be much stronger. By itself, the European recession will probably limit our growth to a crawl, but should not be strong enough to drag us into another recession UNLESS there is a collapse of the euro. Some pundits believe that a Greek pull-out from the euro has already been factored in to the markets, and will be a non-even when it finally happens. Others justifiably worry about the "contagion" impact on the other countries with financial problems, namely Ireland, Italy, Spain and Portugal. Either way, we are in for many more months of uncertainty.

COMMENTS FROM SURVEY PARTICIPANTS

"As I have been saying, the economy is slipping. You see it in durable goods orders and steel lead times. The only busy markets are autos (replacement do to aging vehicles and cheap leases), oil and gas (new discoveries and fracking), exporters of items foreigners cannot yet, and too much negative news. The back half of 2012 will be bad, because of the elections, Europe, Greece, expiring Bush tax cuts, and the expiring social security stimulus. Capital gains tax increases pay for Obamacare on top of expiring tax cuts will hurt the stock market. Commodity prices already falling as a result of all of this."

"Orders have slowed slightly, but quoting is still very active. The year is projected to be much better than the forecast."

"There's no real change month on month. Things remain steady as well as the outlook."

"New orders are little soft right now. However, we have quite a few new products being launched that will keep us very busy this summer."

"Steady as she goes..."

"It looks like a busy summer ahead. I hope we can keep up."

"Inquiries have leveled out, but are still coming in. These seem to be solid inquiries."

"Pricing on steel is still coming down slowly. There continues to be increased announcements from the mills and talk of mills taking out capacity to firm pricing or get increases through to buyers."

"Business is still strong, but there is still a lot of uncertainty in the market."

"Business has softened, but we're still optimistic for second half 2012."

"We're still steadily moving on."

"It feels like things are slowing down somewhat, although we are still doing well. Is this the election year blues?"

"We had an extremely strong month, and are looking forward to the continued surge."

"We are coming to the end of another large program, so we are winding down. We anticipate a short down cycle."

"Our order intake is off, and suppliers can't make their due dates. We've had lots of late deliveries."

"It was a steady month. Demand remains high."

"The economy continues on its rollercoaster ride. The European economy continues to be a concern. What's up with ThyssenKrupp?"

"The year is looking like it will be flat compared with 2011....which is not all bad."

"We are very busy, and the State is spending money like water. It must be an election year!"

"Lead times for most goods are coming in. We can generally get access to machinery very quickly."

"This month has been pretty flat across the board. Everyone seems to be holding their breath for what will happen in Europe and its impact on the US economy."

"We are running at 100% full production! Our forecast looks strong for the next 3 months, but suppliers are starting to report a little bit of a slowdown."

"Sales continue to remain strong with controlled growth in the high single digits over a strong 2011. We remain cautiously optimistic."

May, 2012 Survey Statistics

	UP	SAME	DOWN	N/A	May Index	Apr. Index	Mar. Index	20 Year Average
Sales (New Orders)	42%	38%	18%	2%	+20	+24	+15	+29
Production	38%	45%	13%	4%	+ 5	+25	+13	+13
Employment	27%	66%	7%		+12	+20	+15	+ 8
Purchases	35%	49%	16%		+11	+19	+14	+ 7
Prices Paid (major commod.)	24%	67%	5%	4%	- 2	+19	+29	+35
Lead Times (from suppliers)	18%	73%	7%	2%	- 4	+11	+ 2	+11
Purchased Materials Inv. (Raw materials & supplies)	27%	51%	18%	4%	-12	+ 9	+ 9	- 5
Finished Goods Inventory	16%	62%	13%	9%	- 4	+ 3	+ 2	-10

Items in short supply: Some aluminum sheets, electronic components, ductile casting capacity, some stainless steel, motor graders, air filters, limestone aggregate, some resins, ferromoly, some standard commodity bushings.

Prices on the UP side: Plastic components, aluminum sheet, powder paint, steel tube, pigment, foam rubber, aluminum, steel and gray iron, fuel, some polypropylene, plastics, poplar, ash, finishing materials, heavy equipment, limestone, some resins.

Prices on the DOWN side: Plastics,* computers, flat glass, stainless sheets, copper wire, some steel products, steel scrap, plate steel, sheet steel, carbon steel, brass, copper, polypropylene,* sand, computers, chlorides, asphalt, fuel.*

*These items are reported as both up AND down in price.

Latest Unemployment Reports

(Note: NOT seasonally adjusted)

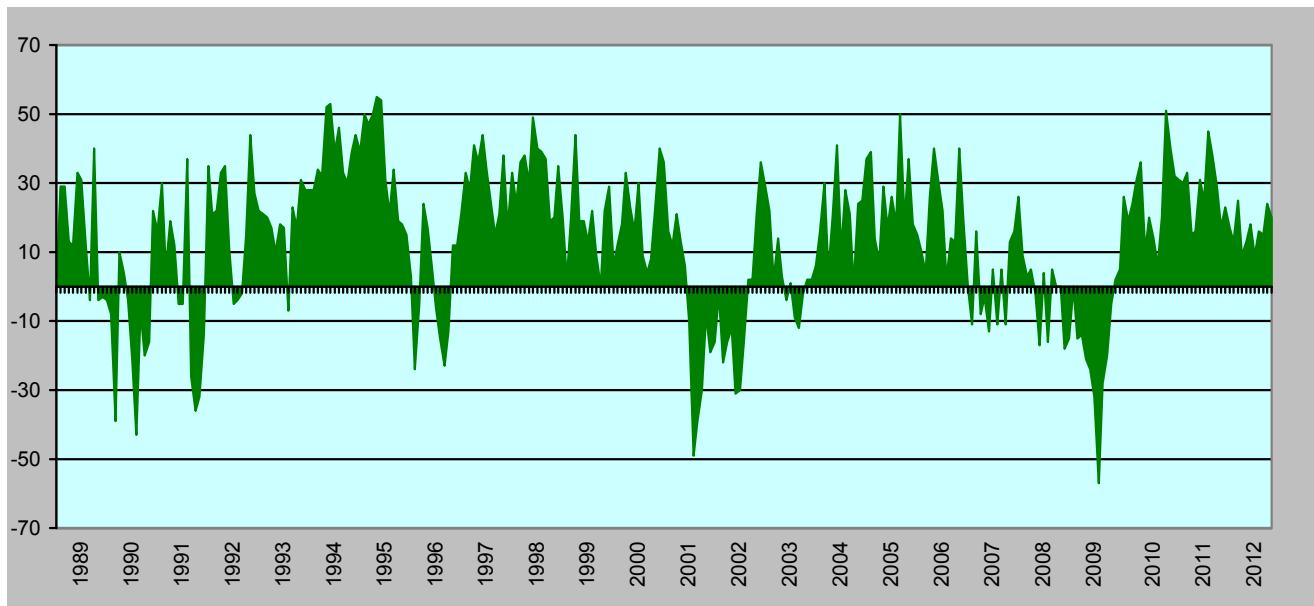
	April 2012	April 2009
State of Michigan	8.0%	12.5%
Kent County	6.1%	9.7%
Kalamazoo County	6.2%	8.8%
Ottawa County	6.1%	11.2%
Barry County	5.8%	9.2%
Kalamazoo City	8.6%	12.0%
Grand Rapids City	8.5%	13.4%
Holland City	8.0%	12.6%
U.S. National Rate	8.4%	9.0%

Index of New Orders: Greater Grand Rapids

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	+20	for the month of May, 2012
Previous Month	+24	for the month of April, 2012
One Year Ago	+17	for the month of May, 2011
Record Low	-57	for the month of December, 2008
Record High	+55	for the month of September, 1994
First Recovery	+3	for April, 2009 and forward

Index of New Orders 1988 - 2012



Index of New Orders: 2005-2012 Only

