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Current Business Trends

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West Michigan: Back to Slow Growth

Economic growth in West Michigan eased to a slower pace in November, according to the data collected during the last two weeks of the month. Our closely watched index of NEW ORDERS remained positive at +16, but the rate of expansion was well below the +26 and +27 we reported for the previous two months. In a similar move, the PRODUCTION index came in at +12, a slower rate of increase than the +23 and +29 reported for September and October. Because of labor problems in the West Coast ports, the LEAD TIMES index edged up to +16 from +8. The EMPLOYMENT index is still expanding, but this month's report of +16 is well below the +34 we reported two months ago. The comments from survey participants continue to highlight the problem of finding enough qualified workers. Our index of the LONG TERM BUSINESS OUTLOOK rose to +50 from +43, and other comments still express no major concerns about the future.

Looking at individual industry groups, the office furniture business continues to see stronger sales. Other industries reported mixed results. For instance, capital equipment firms generally came in strong, but two firms were hit by a considerable drop in new business coming in for 2015. The same scenario came from the industrial distributors, several of which reported brisk business but others blamed seasonal conditions for the slower pace. Any firm related to aerospace is holding its own. Finally, our auto parts producers generally remain strong, but several have noted the first downturn in business in several months.

At the national level, the December 1, 2014 report from ISM, our parent organization, came in slightly stronger than last month. NEW ORDERS edged up to +23 from +20, and PRODUCTION rose to +23 from +21. ISM's EMPLOYMENT index, still stuck in single digits, eased to +5 from +7. The overall PMI remained strong but eased modestly to 58.7 from 59.0. In confirmation, the U.S. PMI from Markit.com, the international British consulting firm, also eased modestly to 54.8, down from 55.9. However, the survey author notes that "...the pace of growth has slowed for three successive months, taking it down to the slowest pace since January."

According to the J.P. Morgan Global Manufacturing PMI released on December 1, the growth of NEW ORDERS for the world index slowed to a 16-month low. The rate of expansion for the global PMI slowed to 51.8, a 14-month low. The U.S. economy remains strong, but the stagnation in Europe continues to dominate the international economic news. The Eurozone PMI report released on December 1 from Markit.com continues to slide toward recession, although this month's number is still marginally positive at 50.1. Chris Williamson, the chief economist at Markit, has probably said it best:

"With the final PMI coming in below the flash reading, the situation in Euro area manufacturing is worse than previously thought. Not only is the performance of the sector the worst seen since mid-2013, there is a risk that

renewed rot is spreading across the region from the core. The sector has more or less stagnated since August, but we are now seeing, for the first time in nearly eighteen months, the three largest economies all suffering manufacturing downturns. Germany's export engine has stalled, causing the steepest deterioration of NEW ORDERS since December 2012, and new business is also falling in both France and Italy, boding ill for production in coming months. Spain, Ireland and the Netherlands remain bright spots, but the worry is that these countries will, like Greece and Austria, struggle to continue to expand unless demand picks up in the region's largest member states."

Why is the European economy hesitating? At this time, the origin of the weakness appears to be dysfunctional governments, politicians, and leaders. Throughout Europe, there is a growing fear of the unrest in the Ukraine. A few days ago, former Soviet leader Mikhail Gorbachev noted that the Cold War may be coming back. Germany is by far the largest economy in Europe, and a significant amount of press is now highlighting Germany's abrupt shift in energy policy. The new policy calls for all German nuclear plants, 17% of the nation's capacity, to be shut down over the next eight years. To replace the generating capacity, the scramble to build about a dozen coal fired plants is now underway. But the environmental movement rightly fears that these plants will contribute to air pollution. Needless to say, electric power costs are now rising.

Lastly, we cannot forget Europe's pension problem. Many of these governments have vastly overpromised baby boomers healthcare and pensions that are not properly funded. Some austerity programs were put into place a few years ago that helped quell the financial markets, but now we hear of new political movements in countries like Greece to overturn these reforms. With the economy in the U.K. now improving, the British want no part of Europe's problems. Hence, there is now a British movement to pull out of the European Community altogether.

For this month, plenty of attention has been devoted to the slump in oil prices. Crude oil prices are down, and gasoline is now selling for almost a dollar per gallon less than six months ago. For the Christmas season, this means more money in the pockets of consumers. Lower gasoline prices also raise consumer morale, and encourage more purchases of just about everything, including big ticket items like cars and houses. However, other commodities are also falling in price. For instance, iron ore is now about half the price of what it was just one year ago. Copper, lead, zinc, nickel, and palladium are all 10-15% lower in price than just a few months ago. The ominous fear is that wide-spread declines in commodity prices have preceded past recessions.

On the brighter side, even though it doesn't feel like it, economic conditions have improved considerably

throughout 2014. The official U.S. unemployment rate has now declined to a seasonally adjusted rate of 5.8%, down considerably from the 7.3% rate reported just one year ago. What about the REAL unemployment rate, i.e., the rate that includes all of the underemployed people and the workers who have given up? Here again the news is good. This broader measure, reported as U-6, now stands at 11.1%, down from last months' 11.3% and considerably lower than the 13.2% rate reported a year ago.

Looking at some of the local unemployment numbers, the results are similar. For Kent County, the current unemployment rate (unadjusted) has now fallen to 4.0% from 4.5%. Of all 83 counties in Michigan, Kent County now has the lowest rate. In Kalamazoo County, the latest report posted on December 2 came in at 4.7%, considerably lower than the 7.0% rate reported a year ago. For the State of Michigan, the unadjusted rate now stands at 6.4%, considerably below the ominous 8.2% rate for the same time in 2013. By comparison, the state unemployment rate was at 14.8% in July of 2009, but as low as 3.1% in October of 2000. In short, our unemployment picture continues to improve, but we still have a gap to close before we can consider West Michigan to be back to full employment.

As promised, the Bureau of Labor Statistics posted a GDP update third quarter of 2014. The "advance estimate" of Gross Domestic Product came in at +3.5%, and many forecasters expected the numbers reported on November 25 to be about the same. However, we were surprised with an upward revision to 3.9%.

Assuming the fourth quarter remains strong, we should expect the GDP for 2014 to be one of the best in several years. Because of Black Friday discounting and a reduction in credit requirement, the November auto sales figures were again very positive. Chrysler gained 20%, GM 6%, Honda 5%, and Toyota 3%. Ford sales slipped 2% because the firm is still shifting production to the new aluminum truck bodies. Strong auto sales continue to keep our local auto parts suppliers operating at full capacity.

In other economic news, existing home sales edged up, and are now near the level of 2007. The National Home Builders Association reported that the index of builder confidence has now risen to a nine year high. Median household income is FINALLY starting to edge higher for the first time in six years. USDA reports that the number of people enrolled in the Supplemental Nutritional Assistance Program (SNAP) has actually been declining for the past two years, even though 46.2 Million people are still enrolled. However, both the U of M index of Consumer Sentiment and the Conference Board posted minor declines. Hence, at least some of the economic news is still fairly positive.

In summary, it is again worth noting that a flat or stagnant European economy will not draw the U.S. into another recession UNLESS the drop is substantial. A recent survey of internal economists pegs the chances of a U.S. recession at only 14%, although a similar survey conducted today would probably be less favorable. Otherwise, the worldwide slowdown will have a dampening effect on our local and national economy, and probably means that 2015 will be another year of slow growth.

November 2014 COMMENTS FROM SURVEY PARTICIPANT

"Many suppliers are coming in with unwarranted increases to perpetuate their stock price. There's no fundamental commodity reason for it."

"We had a large "end of year" promotion with our machine tools and moved a lot of machines. We made substantial discounts to move the equipment."

"Scrap prices continue to tumble, and are down another \$30 for November."

"Tool shops extremely busy. That's a good sign of the stronger times."

"We're doing well here."

"Were seeing our normal seasonal slowdown in November and December, but we expect sales to increase again in January."

"Business is still strong, and we're working hard to fill the first quarter of 2015."

"We recently hired two welders and one CNC machinist, but we are using subcontractor for additional welding to keep up with demand. West Coast port congestion is due to labor disputes causing long lead times for imported components."

"Currently, new PO's have stalled out, which has caused gaps in our production schedule. The sales department has a lot of quoting going on that should bring some nice PO's for next year as long as economic conditions continue to be upbeat."

"The general belief is that the bottom has been found."

"After a strong October, we are tracking 7% lower in November. This is somewhat to be expected heading into the holidays, but more than forecasted."

"Business still very brisk in the energy and rail sectors."

"We are still very bullish on the automotive business, but our non-automotive work is lagging plan."

"We're staying about the same. Next year mimics this year. Fiscal 2016 and 2017 look like a break out year if all remains stable."

"It's never easy."

"No changes from last month's reporting."

"Most customers are still in a "wait and see" attitude. We have discounted quite heavily to move machines."

"We are sort of hitting a comfortable stretch with orders slowing a bit and production now caught up to date. We're anticipating first quarter orders to increase."

"We're working through a new ERP system startup, and still working out the bugs."

"We are already into winter operations! Unfortunately, if the weather is anything like it was last year local road budgets will again be stretched. Along with all the increases associated with winter operations, especially in the price of salt, maintenance will again be limited in the spring and summer, pushing overall road conditions further back. Hopefully, the road funding issues will get settled before spring."

"We are unusually busy for this time of year. Orders typically drop off about now, but are continuing strong."

"We're getting very concerned about what is going on at the West Coast Ports. This could have a serious impact on our business given that many product and components are imported."

"Inquiries are still on the down side for us, and I don't know why."

"Business is good and still going strong even with the upcoming holiday shutdown schedules. We are expanding several of our plants again!"

"We had another strong month in October. I will expect to report a down month for November since deer season has started and activity has slowed to a crawl."

"We are seeing a little spike in demand before the holidays."

"Business is finishing strong for 2014. The 3-5 year outlook is looking very strong."

November 2014 Survey Statistics

	UP	SAME	DOWN	N/A	Nov. Index	Oct. Index	Sept. Index	20 Year Average
Sales (New Orders)	29%	57%	13%	1%	+16	+26	+27	+29
Production	23%	59%	11%	7%	+12	+23	+29	+13
Employment	26%	64%	10%		+16	+25	+34	+ 8
Purchases	26%	64%	10%		+16	+20	+14	+ 7
Prices Paid (major commod.)	11%	79%	6%	4%	+ 5	+ 6	+12	+35
Lead Times (from suppliers)	19%	78%	3%		+16	+ 8	+18	+11
Purchased Materials Inv. (Raw materials & supplies)	9%	74%	10%	7%	- 1	+20	- 1	- 5
Finished Goods Inventory	11%	62%	20%	7%	- 9	+ 2	+ 1	-10
Short Term Business Outlook (Next 3-6 months)	24%	66%	10%		+14	+12	+26	-
Long Term Business Outlook (Next 3-5 years)	50%	47%	0%	3%	+50	+43	+51	-

Items in short supply: Some aluminum, imports goods, trucking charges, argon, some resins, 6061 Plate .500" and below, anything coming through west coast ports, skilled welders, CNC machinists, skilled trades, hardwood for pallets, rock salt and sodium chloride, electronic components, software engineers, labor.

Prices on the UP side: All aluminum, resins, polypropylene, black pigment, stainless steel, steel, galvanized steel, equipment, food, refined nickel metals, salt, sodium chloride, magnets, source controlled product in which suppliers own design rights, some metals.

Prices on the DOWN side: Plasticizers, paraffinic oil, steel (just a touch), carbon steel, steel surcharges, copper, scrap steel, fuel, stainless material prices, rubber, resin*.

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

Latest Unemployment Reports

(Note: Data are NOT seasonally adjusted)

	Oct. 2014	Sept. 2014	Aug. 2009	20 Year Low
State of Michigan	6.4%	6.4%	14.8%	3.1%
Kent County	4.0%	4.5%	11.9%	2.1%
Kalamazoo County	4.7%	5.3%	11.1%	2.1%
Calhoun County	5.1%	5.7%	12.8%	2.7%
Ottawa County	4.1%	4.5%	13.3%	1.8%
Barry County	4.2%	4.7%	10.9%	2.2%
Kalamazoo City	4.7%	5.3%	15.2%	3.2%
Portage City	3.6%	4.1%	8.7%	1.3%
Grand Rapids City	5.7%	6.4%	16.1%	3.0%
Kentwood City	3.6%	4.1%	10.7%	1.4%
Plainfield Twp.	2.6%	3.0%	8.0%	1.4%
Holland City/Allegan	1.7%	1.9%	3.7%	0.9%
U.S. National Official Rate	5.8%	5.9%	9.7%	3.6%
U.S. U-6 Rate*	11.5%	11.8%	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 +16 for the month of November, 2014

Previous Month +26 for the month of October, 2014

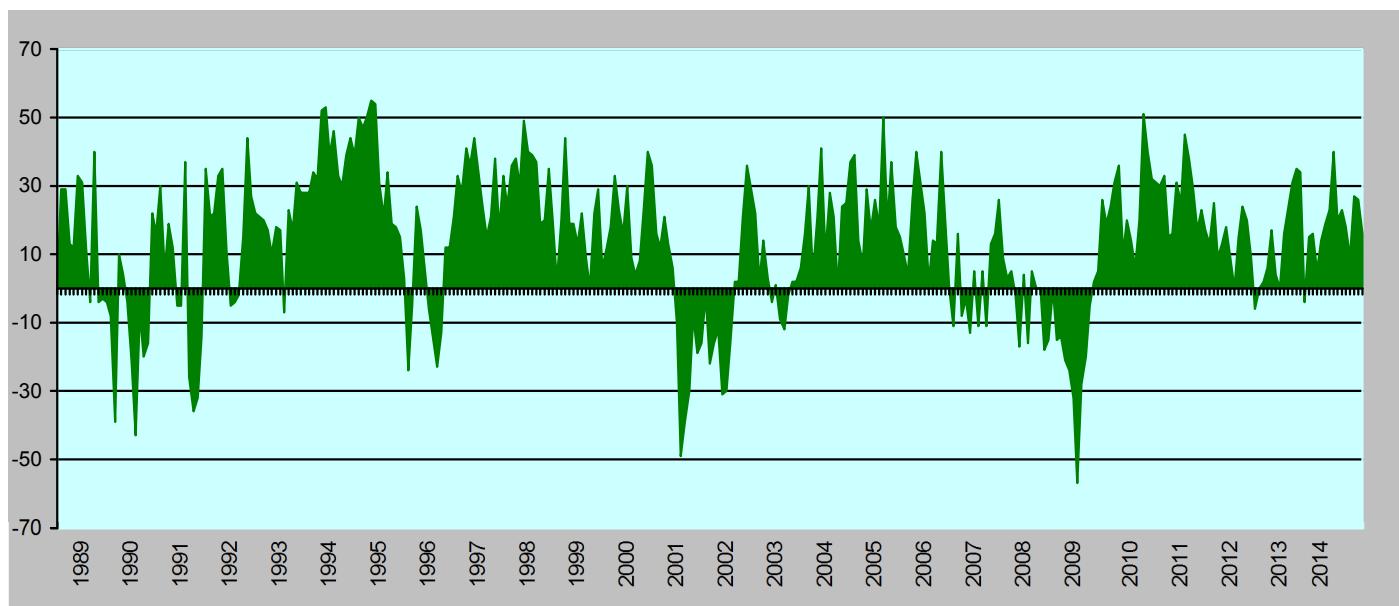
One Year Ago +16 for the month of November, 2013

Record Low -57 for the month of December, 2008

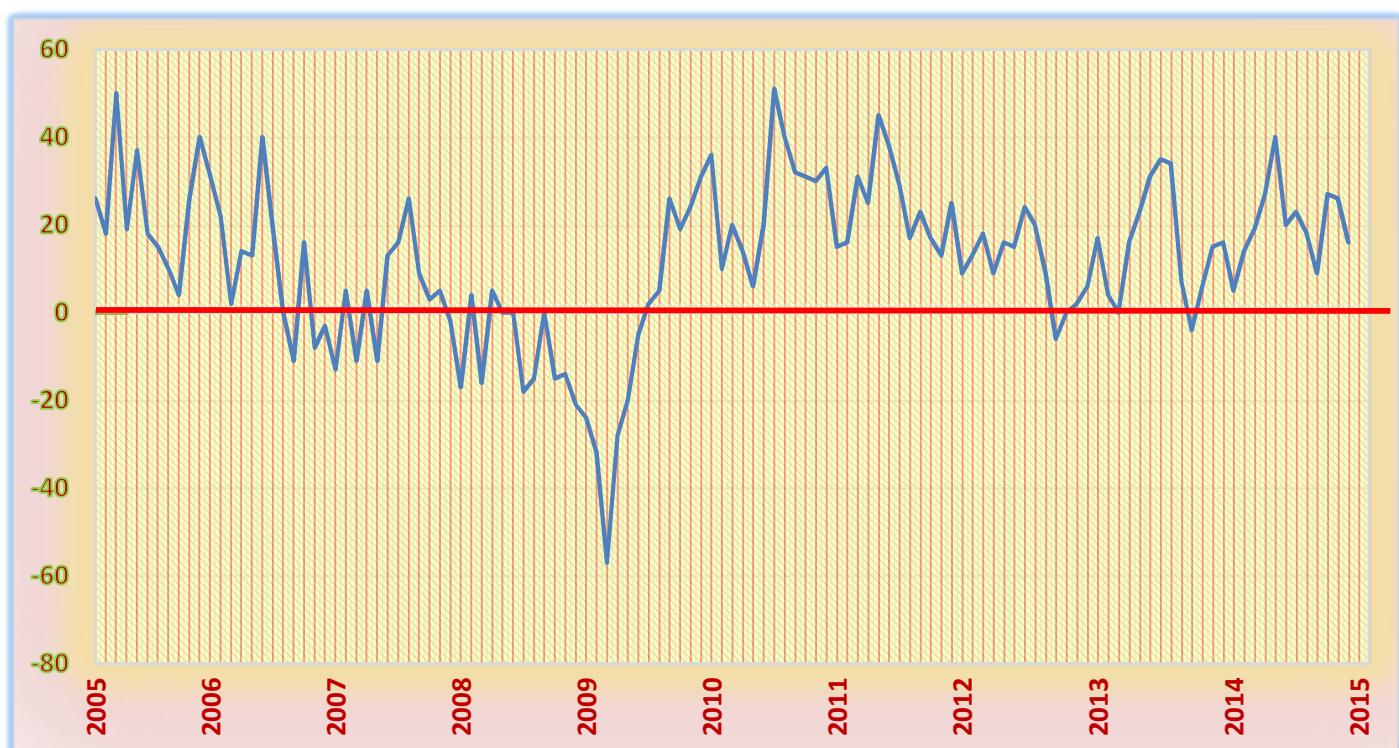
Record High +55 for the month of September, 1994

First Recovery +3 in April of 2009 and forward

ISM-West Michigan Index of New Orders 1988 - 2014

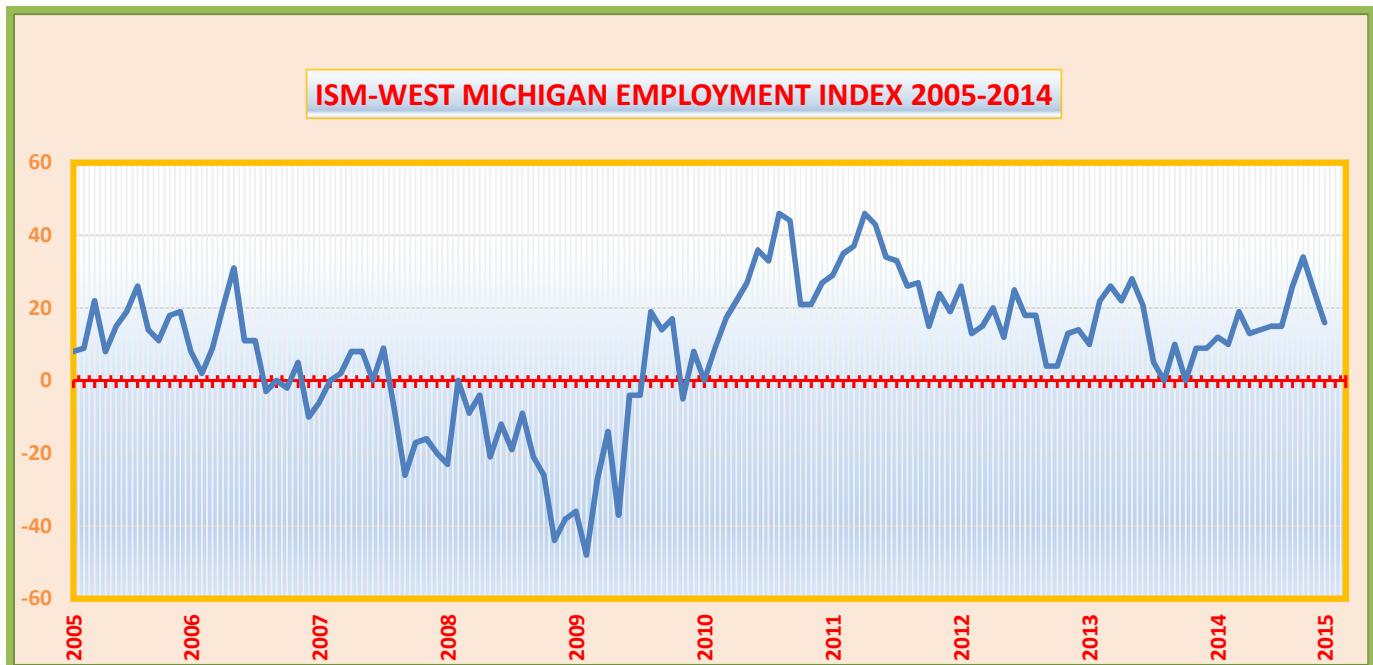


ISM-West Michigan Index of New Orders: 2005-2014 Only



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.

