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Current Business Trends

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Back to a Two Year High

Good news is always welcome, and according to the latest survey conducted during the last two weeks of April, the West Michigan economy is surprisingly strong. NEW ORDERS, our index of business improvement bounced to +35, up nicely from +21. However, the PRODUCTION index remained very strong but eased to +29 from +31. Activity in the purchasing offices, the index of PURCHASES, came in virtually unchanged at +26. The stronger April sales reports pulled the FINISHED GOODS INVENTORIES index down to -4. The fear of more price increases probably helped drive the RAW MATERIALS INVENTORIES index up to +16 from +9. Overall, the second quarter of 2017 has begun on a strong note.

Looking at individual industries, most auto parts suppliers are still positive, although several respondents have voiced concerns about softening auto sales. The office furniture business is still experiencing a spring rally, and smaller firms are outpacing their larger counterparts. The capital equipment market has turned mixed, but the bias is to the up side. Just like many months in the past, the performance for the industrial distributors continues to be mixed.

There are now some apparent signs that the Trump rally may be running out of steam. For April, our West Michigan index of the SHORT TERM BUSINESS OUTLOOK, which asks local firms about the perception for the next three to six months, remained positive but backtracked to +32 from +37. Looking out three to five years, the LONG TERM BUSINESS OUTLOOK also remained positive but edged down to a near-record low of +35 from +47.

The May 1 report from the Institute for Supply Management, our parent organization, remains positive, although the pace of advancement has slowed. NEW ORDERS, ISM'S index of business improvement, eased modestly to +27 from +35. However, the PRODUCTION index accelerated to +31 from +21. ISM's index of EMPLOYMENT remained strong but backtracked to +11 from +16. ISM's overall index for April eased to 54.8, down from the lofty 57.2 reported last month. At 54.8, the U.S. PMI is still strong but not nearly as strong as the PMI reports coming from the European countries.

The April survey of the U.S. manufacturing conducted by Markit.com, the British economics consulting firm, remains positive but less robust. NEW ORDERS moderated to the slowest pace since September 2016. The Markit PMI for the U.S. came in at 52.8, down slightly from 53.3. Comments from Chris Williamson, the chief business economist for Markit, continues to be cautious:

"Manufacturers reported that growth of production and order books have slowed markedly since peaking in January, with April seeing the weakest improvements for seven months. The signs of slowing growth are most evident in the domestic consumer sector, but investment goods manufacturers continue to fare

well, enjoying stronger capital equipment spending from the energy sector in particular. Exports have also perked up, with April seeing the steepest increase in foreign orders for eight months. Price pressures have meanwhile risen to a two-and-a-half year high, which is likely to feed through to final prices paid for goods consumers in coming months."

The May 2 report from the J.P. Morgan Global Manufacturing survey of 31 nations slowed to a three month low. JPM's overall index eased modestly to 52.8 from a 69-month high of 53.0. In most cases, developed nations recorded stronger rates of improvement than emerging markets. The rate of increase in new export business edged higher. For the Eurozone, business conditions are significantly better. The latest Eurozone PMI is now up to 56.7, and survey readings indicate that manufacturing is growing at an annual rate of approximately 4 to 5 percent. The PMI for countries like Germany, Austria, Netherlands, Italy, and France are now at or near six-year highs. Greece remains in the doldrums. Despite some nervousness over the upcoming French election, European business disposition remains cautiously positive. David Hensley, the survey author, further noted:

"The start of the second quarter saw a slight loss of growth momentum in the global manufacturing sector. Rates of increase eased for both production and new orders, although the outlook remains positive given a backdrop of solid business confidence and rising backlogs of work. The continued upturn is also feeding through to the labour market, with jobs added for the eighth straight month."

In other economic news, the Department of Commerce estimates that GDP for the first quarter of 2017 grew by only 0.7 percent. Whereas some of the weakness can be attributed to unfavorable weather throughout the south and mid-section of country, a few analysts have noted that the past few years have followed a pattern of weak first quarter growth followed by offsetting quarters for the rest of the year. Hence, the estimates for the second quarter GDP are running as high as 4.5 percent.

For West Michigan employment, spring has again arrived. Of the 83 counties in Michigan, Ottawa County currently boasts the lowest unemployment rate of 2.8 percent, follow by 3.0 percent for Kent County. Kalamazoo County garnered fifth place with a rate of 3.5 percent. Because these numbers are NOT seasonally adjusted, at least some of the improved numbers are the result of cyclical variation. The West Michigan index of EMPLOYMENT came in at +25, a two year high. All of this means that many firms are still adding staff, even though there are signs that both the automotive and office furniture industries are topping out.

The current wave of industrial inflation shows no sign of subsiding anytime soon. Our local index of PRICES

remained at the lofty level of +38, very near a six-year high. Just as last month, not a single firm reported a significant level of falling prices, and the list of commodities climbing in price continues to grow. At the national level, ISM's index of PRICES moderated slightly to +37, down from +41. J.P. Morgan's International index of PRICES remains stuck at a fairly lofty 60.0.

Will the current round of industrial inflation spill over into the consumer market? Probably not. About fifty years ago, it only took a few months before industrial inflation would be reflected in prices for most of the high-ticket consumer goods such as appliances and automobiles. Additional inflation for other goods would quickly follow. But we experienced a similar wave of industrial inflation in early 2011, and the impact on consumer inflation was negligible. After a few short months, most prices came back to normal. We simply live in a different world wherein foreign competition tends to thwart the temptation for many manufacturers to raise prices.

Unfortunately for our local auto parts suppliers, the spring year-over-year sales drop in light vehicle sales continues to accelerate. For April, there wasn't much of any place to hide. According to the monthly posting by Automotive News, sales for Ford posted a decline of 7.1 percent, followed by a 6.6 percent drop at Fiat-Chrysler. General Motors, which had managed a small gain last month, slipped 5.8 percent in April. Among the other major brands, Honda dropped 7.0 percent, Nissan yielded by 1.5 percent. Toyota eased 4.4 percent, but Subaru bucked the trend and gained 3.9 percent. All of this resulted in a drop of 4.7 percent for the entire industry, marking the fourth consecutive monthly setback for U.S. sales and longest losing streak since the beginning of the 2009 Great Recession.

In an otherwise strong economy, why are auto sales sagging? Several reasons. First, because of sales pressure from their parent companies, dealer inventories have now risen to a 90-day supply, well above the ideal level of 60 days. The industry analysts note that light truck and

crossover sales are no longer filling the gap created by sharply falling car sales. For instance, April car (non-truck or SUV) sales fell by 13 percent for GM and 21 percent for Ford. This trend is clearly not positive. Furthermore, a wave of vehicles coming off lease is now depressing the used car market as well as creating a lower cost alternative to the new car market. Even though rebates and other incentives continue to rise, the market is no longer responding like it did a few years ago. After dipping back into sub-prime lending, some of the lending institutions are starting to retighten their lending standards. For West Michigan, all of this means that production schedules for several local firms may begin to taper.

Despite optimistic rhetoric from GM and other automotive executives about the remainder of the 2017 sales season, the fact remains that market saturation is finally starting to set in. We have previously noted that the current market can absorb about 15.5 million cars per year, and any excess is at the expense of future sales. The public now demands higher quality cars and truck, and the industry has made great strides in meeting the demand. However, the down side is that high-quality cars last much longer than their counterparts of 20 years ago. Furthermore, the number of miles Americans are driving has yet to fully recover from the Great Recession.

In summary, the post-election rally may have run its course, but positive news from Washington can keep the ball rolling. Our local statistics remain strong, and at least for now, there is no sign that we are sliding toward a recession. But caution flags are out. For West Michigan, we need to keep a close eye on auto sales, because slower sales will eventually spill over into reduced production schedules for an industry that has been booming since the infamous "Cash for Clunkers" incentive program of 2009. The markets are still hoping for decreased regulation and lower taxes, but progress in Washington has been slow. A significant cut in business taxes would be greeted with enthusiasm, but Washington deadlock could slow the growth for the last half of 2017.

APRIL COMMENTS FROM SURVEY PARTICIPANTS

"We have been very busy since the first of the year but our schedule is looking a little slower for May."

"Business is very good still, but our future orders have slowed down a little bit."

"March was MUCH better than February. April looks to be about normal."

"Sales are a bit unpredictable. We have some delays with new program startups, and overall uncertainty has led to our CEO to describe the current environment as 'choppy waters'."

"We are getting busier. The second and third quarters are our busiest time of year."

"Auto inventories are climbing. Plant are extending summer shutdowns. Incentives are brewing. Will we see a downturn in future the automotive build?"

"Business has been a little slower, but orders 1-3 months out are showing increases."

"Business is booming. We are trying to find more suppliers to help with the overload."

"Business is steady."

"We are still very busy, and that is a good problem."

"Business is moving along nicely."

"March was less than stellar, but April is making up for it."

"Things have been picking up slightly. New Orders are starting to break loose."

"Automotive remains strong."

"We are still nervous about changes to NAFTA. The Trump administration making things very frustrating."

"Many airlines appear to be holding off orders on existing aircraft waiting for new and more efficient versions

to begin production in coming years (737 max, 777 max, etc).

"We're performing capacity studies"

"Things are stable."

"Pricing is up in our medical packaging for the first quarter by 16% compared to the same time frame in 2016."

"Business is steady now, but we will see a pickup in the summer on the medical side, which is normal."

"Orange barrels are out, and we are very busy repairing and repaving the roadways. It will be a very busy season!"

"We've had a soft first quarter, but we see a promising second quarter ahead."

"Our plant is on its annual shutdown for repairs and upgrades for the upcoming campaign season."

"Steel price is holding steady."

"We are still doing quite well, although not quite as robust as last year."

"The first quarter of 2017 has not been good to us. Sales are down about 5%."

"Sales remain flat. We have some hopes that projects will start to shake loose at the end of the calendar year. Until then, we will focus on inventory and cost reduction."

"We are still having trouble with plastic resin manufactured by Sabic from overseas. We started off with a four week lead time at end of 2015, but at the beginning of 2016, the "quoted" lead time was up to 6-8 weeks, and ended up being longer. Now we are looking at 9-10 week lead time for material, with no real set dock date. Also, we are having trouble receiving complete orders on Sabic material. Will receive about half of the ordered quantity, and the balance will be an additional 3-4+ weeks out."

April 2017 Survey Statistics

	UP	SAME	DOWN	N/A	Apr. Index	Mar. Index	Feb. Index	25 Year Average
Sales (New Orders)	49%	35%	14%	2%	+35	+21	+25	+14
Production	40%	41%	11%	8%	+29	+31	+17	+14
Employment	32%	60%	8%		+26	+21	+12	+ 8
Purchases	37%	50%	11%		+26	+25	+19	+ 7
Prices Paid (major commod.)	40%	58%	2%		+38	+39	+27	+15
Lead Times (from suppliers)	25%	75%	2%		+25	+24	+20	+11
Purchased Materials Inv. (Raw materials & supplies)	24%	60%	8%	8%	+16	+ 9	+21	- 4
Finished Goods Inventory	14%	64%	17%	6%	- 4	- 9	+ 5	- 8
Short Term Business Outlook (Next 3-6 months)	46%	40%	14%		+32	+39	+37	-
Long Term Business Outlook (Next 3-5 years)	40%	52%	5%	3%	+35	+42	+47	-

Items in short supply: Labor, temp labor, production labor, ULTEM, titanium dioxide, cobalt based chemicals, crystal nickel chloride, some aluminum, specialty parts, sultanas.

Prices on the UP side: Most resins, steel, hot rolled steel, electrical steel, aluminum, ready mix concrete, bituminous asphalt, construction equipment, heavy duty trucks, plasticizer, PVC resin, paraffinic oil, SEBS resin, corrugated, wood, copper, cobalt, polypropylene, chip packaging materials, chip partitions, contracted services., healthcare, electrical components, pumps and motors.

Prices on the DOWN side: Alloy bar, heavy plate, heavy tube, plastic resin *, polypropylene*, carbon steel*, stainless steel, nickel metal, China steel wire rod, ocean freight, cotton.

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

Latest Unemployment Reports

(Except as noted, data are **NOT** seasonally adjusted)

	Mar. 2017	Mar. 2016	Aug. 2009	20 Year Low
State of Michigan (Adj.)	4.9%	5.0%	14.6%	3.2%
State of Michigan (Unadj.)	5.3%	4.8%	14.1%	2.9%
Kent County	3.0%	3.5%	11.9%	2.1%
Kalamazoo County	3.5%	4.0%	11.1%	2.1%
Calhoun County	4.5%	5.0%	12.8%	2.7%
Ottawa County	2.8%	3.4%	13.3%	1.8%
Barry County	3.8%	4.4%	10.9%	2.2%
Kalamazoo City	4.3%	5.0%	15.2%	3.2%
Portage City	3.2%	3.7%	8.7%	1.3%
Grand Rapids City	4.0%	4.7%	16.1%	3.0%
Kentwood City	2.9%	3.3%	10.7%	1.4%
Plainfield Twp.	2.3%	2.6%	8.0%	1.4%
U.S. Official Rate (Dec.)	4.5%	5.0%	9.6%	3.8%
U.S. Rate Unadjusted	4.6%	5.1%	9.6%	3.6%
U.S. U-6 Rate**	8.9%	9.8%	16.7%	8.0%

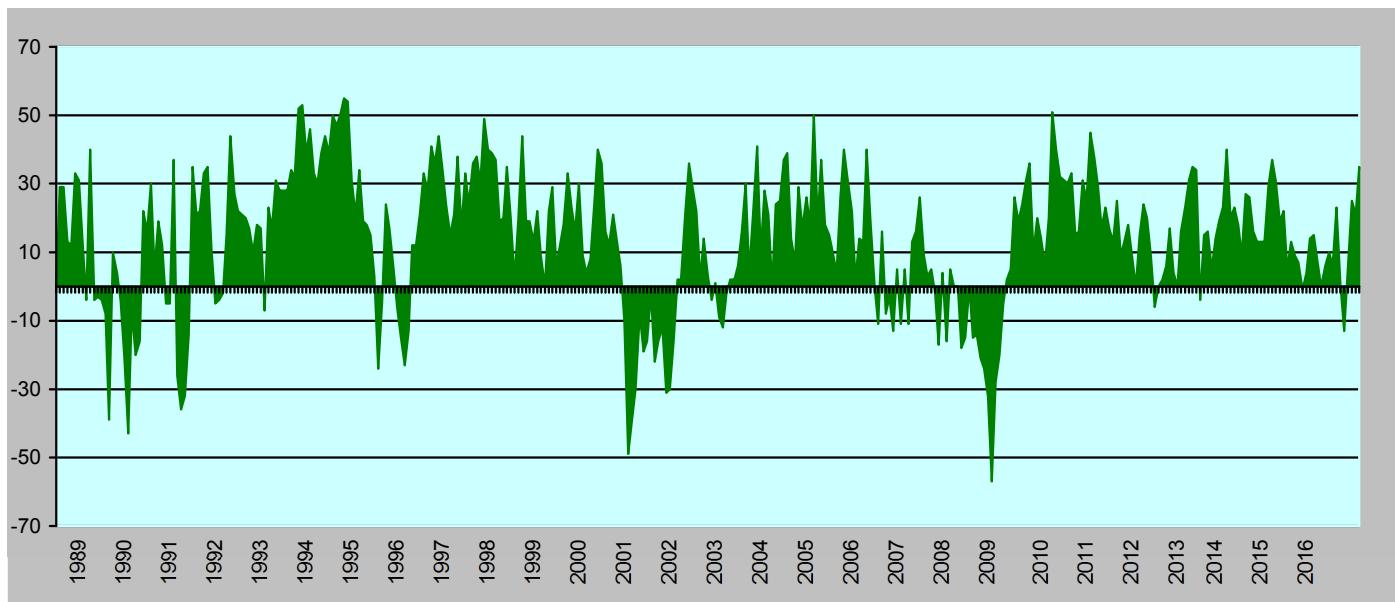
**U-6 for Michigan = 10.3% for all of 2016

Index of New Orders: West Michigan

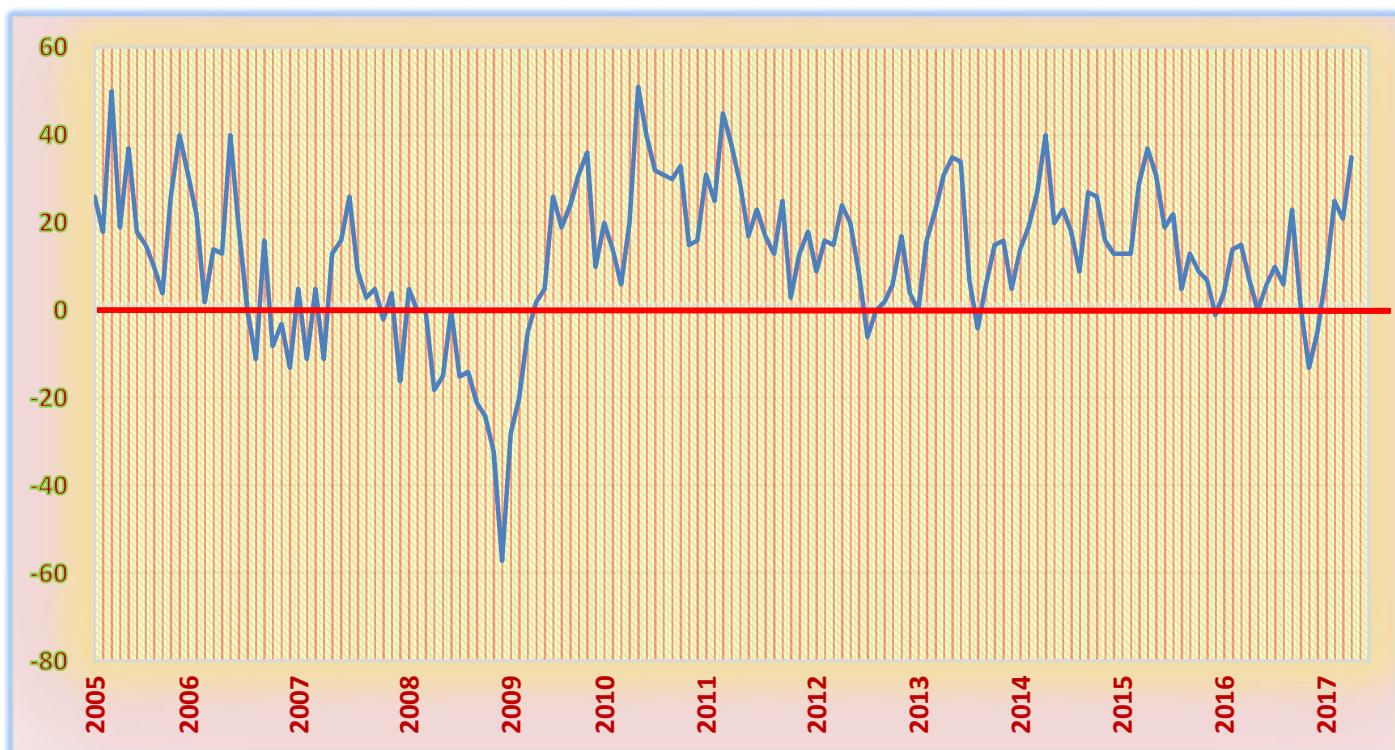
As the name implies, this index measures new business coming into the firm, and signifies business improvement or business decline. When this index is positive for an extended period of time, it implies that the firm or organization will soon need to purchase more raw materials and services, hire more 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	+35 for the month of April 2017
Previous Month	+ 21 for the month of March 2017
One Year Ago	+ 7 for the month of April 2016
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 - 2017

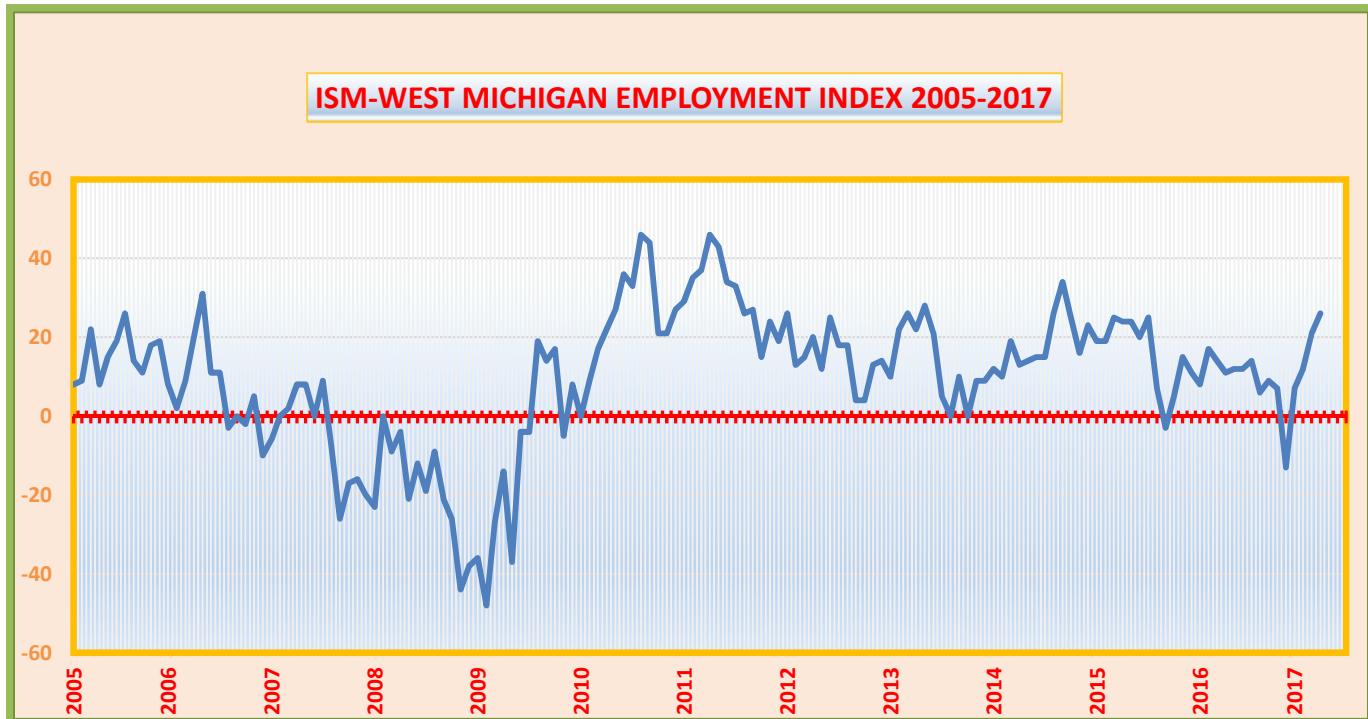


ISM-West Michigan Index of New Orders: 2005-2017 Only



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 reduction in industrial unemployment for West Michigan. Normally, there is about a month or two in lag time between this report and the payroll numbers being reflected 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 laying 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.

