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Current Business Trends

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DESPITE POSITIVE NUMBERS, CONFIDENCE CONTINUES TO FADE

Key Participant Comments for June:

"Sales are softening a bit. We're still doing well, but there appears to be some headwinds in the future. "

"We are now being hit by the Superfund Tax from several of our suppliers."

"Prices for raw materials are starting to come down."

"The market continues to sell products well. However, the production costs continue to rise making for tighter finances at the business level."

"We are gaining a little bit on the ability to hire people."

Although the national and international industrial markets show signs of slowing, the West Michigan economy remains tenuously positive. NEW ORDERS, our index of business improvement, edged up to +26 in June from +14. A stronger move came from June's PRODUCTION Index, which bounced to +31 from +7. The widely-publicized snarls in the world's logistics systems appear to be waning, so the index of PURCHASES flattened to +0 from +20. In addition, the June index of LEAD TIMES posted at +40, a significant improvement over the June 2021 near-record reading of +89. However, with a war still raging in Europe and numerous problems still tangling the world's logistics networks, the industrial world will not return to normal for many months. Automotive production remains constrained by the on-going chip shortage, though our local firms are still busy despite running at reduced capacity. Over the past two months, many of our survey respondents have grown significantly concerned that a recession may be headed our way.

The U.S. Economy. According to the July 1 press release from the Institute for Supply Management (ISM), our parent organization, the NEW ORDERS Index for June declined from +15 to +1, a significant retreat. However, because of modest improvement in supply chain conditions, ISM's PRODUCTION (a.k.a., Output) Index posted at +16, up from +7. Although still positive, ISM's composite index, which combines six of the survey's key factors, fell from 56.1 to 53.0, the lowest the index has been since June 2020.

A similar view of the U.S. economy comes from the British international consulting firm now called S&P Global, or SPG. June's seasonally adjusted U.S. Manufacturing Purchasing Managers' Index for SPG came in at a two-year low of 52.7, a considerable drop from last month's reading of 57.5. The SPG Index of New Orders turned negative for the first time in 26 months, and the Factory Output Index fell to "near stagnation." Although the Order Backlog Index remains strong, previous history warns that cancellations can wipe out the backlog very quickly. SPG's Business Confidence Index sank to the lowest level since October 2020. Chris Williamson, Chief Business Economist at S&P Global, commented:

> "The PMI survey has fallen in June to a level indicative of the manufacturing sector acting as a drag on GDP, with that drag set to intensify as we move through the summer. Forward-looking indicators such as business expectations, new order inflows, backlogs of work and purchasing of inputs have all deteriorated markedly to suggest an increased risk of an industrial downturn. Demand growth is cooling from households amid the cost-of-living crisis, and capital spending by companies is also showing signs of moderating due to tightening financial conditions and the gloomier outlook. However, most marked has been a steep drop in orders for inputs by manufacturers, which hints at an inventory correction. Some welcome news is that the drop in demand for inputs has brought some pressure off supply chains and calmed prices for a wide variety of goods, which should help alleviate broader inflationary pressures in coming months."

The World Economy. According to the most recent J.P. Morgan Worldwide Manufacturing Index, the June PMI for the world economy dropped to 52.2, a 22-month low, despite the rebound in China. However, all of the major economies of the world are still marginally positive. Exceptions include Turkey, Poland, and the Czech Republic. The June PMI for Canada, our largest trading partner, dropped to a 17-month low of 54.6, down from May's 56.8. By contrast, the June PMI for Mexico, our second largest trading partner, edged up to 52.2 from 50.6. Because of the continued relaxation of COVID-19 restrictions, the PMI for China, our third largest trading customer, rose to 51.7 from 48.1 in May. Olya Borichevska, Global Economist at J.P. Morgan, noted:

> "Global factory output returned to growth in June, as an easing in COVID restrictions in China started a recovery in the world's largest manufacturing economy. However, several underlying weaknesses and headwinds remained, including tapering growth of new order intakes, lower business confidence, elevated inflationary pressures, and stretched global supply chains. Apart from the subdued demand environment, business optimism dipped to a two-year low, inflationary pressure remained elevated, and supply chains also stayed stretched. That said, weaker increases in input costs, output prices and supplier delivery times indicated that the pressure on these factors was passed its peak."

Although it is good news that all of the major countries in the Eurozone continue to post positive PMIs, the bad news is that all of these PMIs are now approaching two-year lows. The June composite PMI for the entire Eurozone posted at 52.1, down considerably from

May's 54.6. In part because of ongoing supply chain problems, the Eurozone Index of Output (a,k,a., production) turned negative for the first time since depths of initial COVID-19 lockdowns in 2020. Chris Williamson further commented:

> "Eurozone manufacturing has moved into decline in June, with production dropping for the first time for two years amid a steepening downturn in demand. Orders for goods have fallen at an accelerating rate over the past two months, dropping in June in every country surveyed with the exception of the Netherlands, and even here the rate of growth has weakened markedly in recent months. Demand is now weakening as firms report customers to be growing more cautious in relation to spending due to rising prices and the uncertain economic outlook. The downturn looks set to gain momentum in coming months. Inventories of both raw materials and unsold stock are rising due to lower-than-expected production and sales volumes respectively, hinting that an inventory correction will act as an additional drag on the sector in coming months. Backlogs of work are meanwhile falling, which is often a prelude to firms reducing operating capacity, and business confidence in the outlook has fallen to the gloomiest for just over two years. Supply for many important inputs also remains constrained, and concerns over energy and food supply have added to nervousness about the future. One upside to the recent weakening of demand is an alleviation of some supply chain constraints, which has in turn helped cool inflationary pressures for industrial goods. With the survey data indicating an increasing likelihood of the manufacturing sector slipping into a recession, these price pressures should ease further in the third quarter."

Automotive. According to the July 1 edition of *Automotive News*, the June SAAR (Seasonally Adjusted Annualized Rate) came in at 13.8 million units, a slight gain over May's 12.8 million, but still well below the typical pre-crisis rate of 16 million. Sales at Ford for the second quarter posted a modest gain of 1.8 percent. However, all of the other major brands reported declines. GM sales fell 15.4 percent, and Stellantis (Chrysler) slid 15.8 percent. Many of the foreign nameplates fared worse, with sales at Honda plunging 50.7 percent, Toyota losing 22.9 percent, Mazda sinking 42.8 percent, Nissan Group losing 38.6, Hyundai-Kia dropping 19.1 percent, and VW falling 28.8 percent. Industry-wide sales for the second quarter of 2022 closed down 21.0 percent. Jessica Caldwell, Director of Insights at Edmunds, further commented:

> "Low interest rates used to be one of few reprieves for car shoppers amid elevated prices and supply shortages. But the Fed rate hikes this year are making finance incentives far costlier for automakers, and consumers are starting to feel the pinch. Although there appears to be a steady stream of affluent consumers willing to commit to car payments that look more like mortgage payments, for most consumers the new car market is growing increasingly out of reach."

Industrial Inflation. The slight advantage of all the talk about a possible upcoming recession is that the prices for some industrial commodities may be BEGINNING to stabilize. Our local index of PRICES posted at +54 in June, down considerably from May's +71, but well ahead of the survey's 25-year average of +15. The June ISM National Index of PRICES eased to +57 from +65. In a similar move, the J.P. Morgan World Index of PRICES eased to 68.6 from 78.3. According to Timothy Fiore, chair of ISM's survey committee:

> "The Prices Index has exceeded 70 percent in 18 out of the last 19 months and been above 60 percent for 22 straight months. Continued oil and fuel price increases, packaging supplies (including corrugate), food ingredients, and petroleum-based products and petrochemicals were the primary causes of prices growth. Notably, 8.3 percent of respondents reported lower prices in June, supporting a continued slow but steady move towards price softening,"

Business and Consumer Confidence. The Conference Board's Index of Consumer Confidence for June fell to 98.7 from May's 103.2, the lowest the index has been in more than a year. A more pessimistic reading comes from June's University of Michigan Consumer Sentiment Index, which dropped sharply to 50.2 from 58.4, the lowest recorded level since U of M started collecting consumer sentiment data in November 1952. For our West Michigan survey of the industrial economy, the SHORT-TERM BUSINESS OUTLOOK Index for May, which asks local firms about the business perception for the next three to six months, posted at +3, slightly below May's reading of +7, but sharply below the reading of +44 reported just 13 months ago. For the LONG-TERM BUSINESS OUTLOOK Index, which queries the perception for the next three to five years, the index fell to a record low of -3, down sharply from +29 just two months ago.

GDP. On June 29, the Commerce Department reported that the third and final estimate of the Gross Domestic Product (GDP) for the first quarter of 2022 fell by an annualized rate of 1.6 percent. Although the 2022 second quarter ended on June 30, it will take until July 28 until the Bureau of Economic Analysis (BEA) will post the first estimate of growth for the second quarter. The first quarter was tainted by sporadic Omicron outbreaks, so there was hope that the second quarter would be much better. However, some of the forecasts are now growing significantly pessimistic. As of July 1, the Atlanta Fed's GDPNow second quarter estimate currently projects a quarterly drop of 2.1 percent. By sharp contrast, the Blue-Chip consensus forecast projects a growth of 2.9 percent, and the S&P estimate of 3.2 percent growth is even more optimistic. The Conference Board forecasts a second quarter growth rate of 1.9 percent. Hence, the current second quarter growth consensus is somewhere around 2.0 percent.

Summary. It is readily apparent that the U.S., and perhaps the entire world, is beginning to brace itself for a recession in the coming months. All economic activity is partially psychological, and the news broadcasts continue to mention the "R" word can lead to a self-fulfilling prophecy. Indeed, at least SOME segments of the economy are already showing significant signs of moderating. Because of mortgage rates rising from 2.5 percent to around 6.0 percent in just the past year, the average monthly interest and principal for a 30-year mortgage contract has risen from $1,942 to $2,553, or about $600 more per month. The average rate of new mortgage applications is down 21% from a year ago, so the impact on the housing market is just beginning to take hold. Among some of the key food commodities, the price of corn has fallen 22 percent, wheat 26 percent, soybeans 15 percent, and sugar 9 percent, all in the space the last 30 days. In the industrial market, the past month has seen copper fall 22 percent, zinc 21 percent, nickel 24 percent, and crude oil 14 percent. The simultaneous falling of all of these commodity prices is a clear sign that economic activity is slowing considerably. However, most commodities represent the front end of the supply chain, and it will take a long time for these lower prices to filter through to the end customer, where inflation is now at 8-9 percent. That said, it will still be the responsibility of the Federal Reserve to continue tightening. Failure to do so will result in the return of the 1970's stagflation dilemma.

JUNE COMMENTS FROM SURVEY PARTICIPANTS

“Hopefully, we have reached the peak price for many commodities.”

“It’s still a strange time in manufacturing.”

“Prices for raw materials are starting to come back down.”

“Results are similar to last month, but we’re seeing storm clouds forming on the horizon.”

“We are now being hit by the Superfund Tax from several of our suppliers.”

“Sales are softening a bit. We’re still doing well, but there appears to be some headwinds in the future. “

“A recession is coming.”

“Supply chain issues are very challenging: labor shortages, transportation issues, long lead times from suppliers, etc.”

“We continue to struggle with supply chain issues for get product delivered to the location.”

“The market continues to sell products well. However, the production costs continue to rise making for tighter finances at the business level.”

“We are gaining a little bit on the ability to hire people.”

“We feel like this economy is going to hit a stone, and it’s going to be bad. This green bias from our government needs to be dropped like a lead balloon. People need to wake up to.”

“Incoming orders are showing some signs of slow down, but we have a huge backlog that will carry us well into August.”

"The last 6 weeks or so business has slowed down. Our order entry is down.”

“Supply chain issues continue. If we have it in inventory, we can sell it. We are getting inquiries from customers that normally buy from someone else. If we have it, we get orders. Conversely, if we are out of something, even our best customers are shopping around."

“Things are looking better, but very fragile.”

“We are starting to see freight costs level out.”

June 2022 Survey Statistics

	UP	SAME	DOWN	N/A	June Index	May Index	Apr. Index	25 Year Average
Sales (New Orders)	43%	37%	17%	3%	+26	+14	+29	+14
Production (Gross Output)	40%	40%	9%	11%	+31	+ 7	+23	+14
Employment	40%	40%	17%	3%	+23	+12	+14	+ 8
Purchases	29%	51%	17%	3%	+12	+ 0	+20	+ 7
Prices Paid (major commod.)	60%	31%	6%	3%	+54	+71	+62	+15
Lead Times (from suppliers)	51%	35%	11%	3%	+40	+41	+59	+11
Purchased Materials Inv. (Raw materials & supplies)	43%	37%	11%	9%	+32	+ 9	+44	- 4
Finished Goods Inventory	23%	48%	20%	9%	+ 3	- 4	-17	- 8
Short Term Business Outlook (Next 3-6 months)	26%	48%	23%	3%	+ 3	+ 7	+20	-
Long Term Business Outlook (Next 3-5 years)	20%	51%	23%	6%	- 3	- 2	+29	-

Items in short supply: Paper, dry grocery items, machine repair items, silicones, trucking, aluminum materials, aluminum, pallets, electronic components, microchips, caprylic acid, roll stock (paper), fasteners, castings, electric motors (especially explosion proof), variable speed drives, steel, tube, stainless, TBA solvent, 10 Micron glass used in polypropylene, oil-based products, including DEF solution, mostly anything sources internationally, labor.

Prices on the UP side: All metals, electrical components, steel, fuel, copper, silicone and plastic resin related products, imported textiles, coffee, steel and steel products, paper, gas, microchips, freight/transportation, corrugate, all oil-based products.

Prices on the DOWN side: Aluminum*, steel coil, steel*, scrap steel, some safety related products, magnesium, heavy equipment.

*Item reported as both up AND down in price.

Latest Unemployment Reports

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

	May 2022	May 2021	Aug. 2009	20 Year Low
State of Michigan (May)	4.3%	6.2%	14.6%	3.2%
State of Michigan (Unadj.)	4.6%	6.3%	14.1%	2.9%
Kent County	3.5%	5.3%	11.9%	2.1%
Kalamazoo County	3.9%	5.6%	11.1%	2.1%
Calhoun County	4.9%	7.2%	12.8%	2.7%
Ottawa County	3.2%	4.6%	13.3%	1.8%
Barry County	3.6%	4.9%	10.9%	2.2%
Kalamazoo City	4.9%	7.0%	15.2%	3.2%
Portage City	3.6%	5.1%	8.7%	1.3%
Grand Rapids City	4.6%	7.0%	16.1%	3.0%
Kentwood City	3.3%	5.0%	10.7%	1.4%
Plainfield Twp.	2.6%	4.0%	8.0%	1.4%
U.S. Official Rate (May)	3.6%	5.8%	9.6%	3.5%
U.S. Rate (Unadjusted)	3.4%	5.5%	9.6%	3.4%
U.S. U-6 Rate (May)**	7.1%	10.1%	22.9%	7.1%

**U-6 for Michigan = 8.7% for Q2 of 2021 thru Q1 2022

Index of New Orders: West Michigan

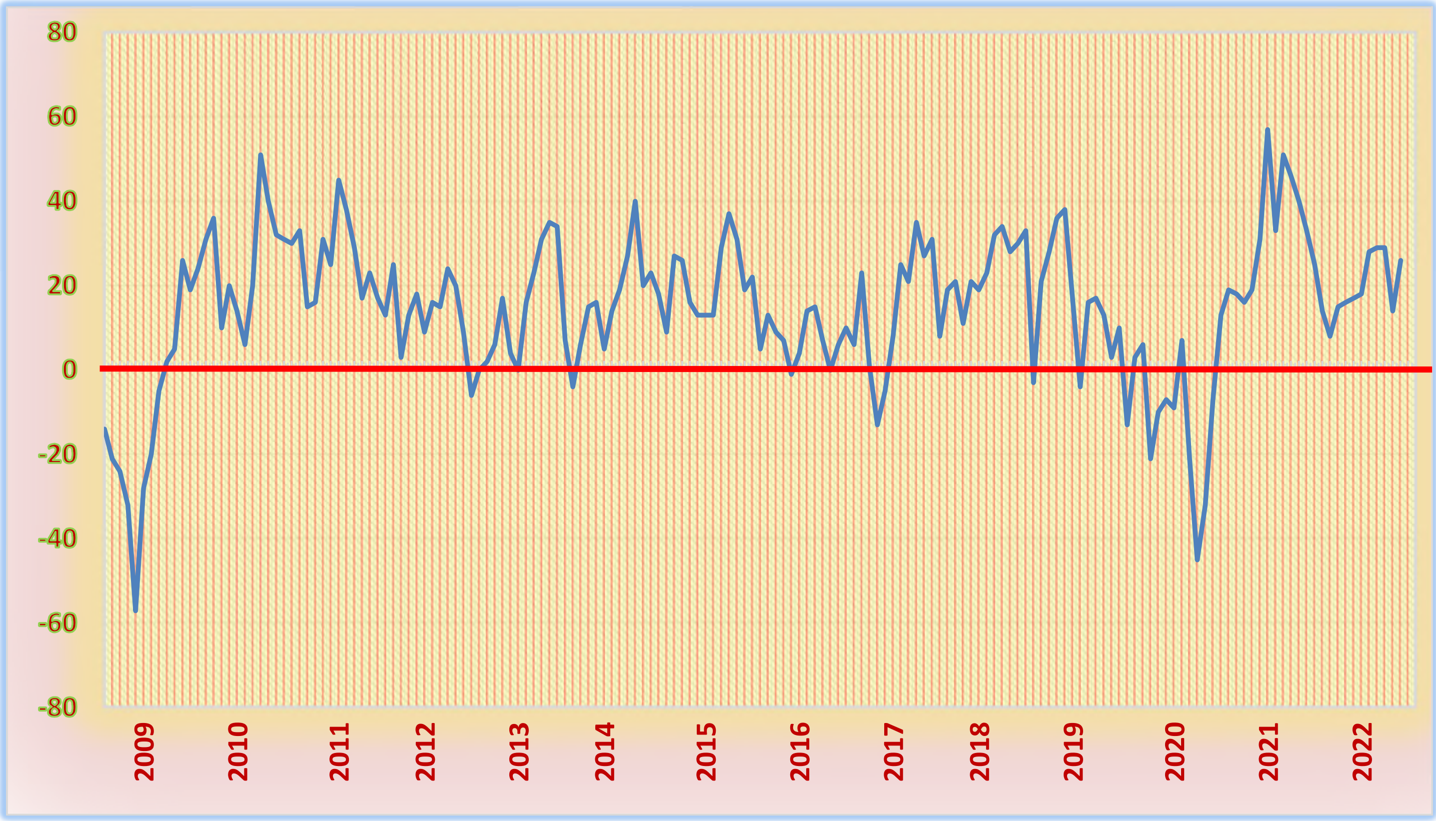
As the name implies, this index measures new business coming into the firm, and signifies business improvement or business decline. When this index is positive for an extended period of time, it implies that the firm or organization will soon need to purchase more raw materials and services, hire more 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	+ 26 for the month of June, 2022
Previous Month	+ 14 for the month of May, 2022
One Year Ago	+ 33 for the month of June, 2021
Record Low	- 57 for the month of December 2008
Record High	+ 57 for the month of January 2021

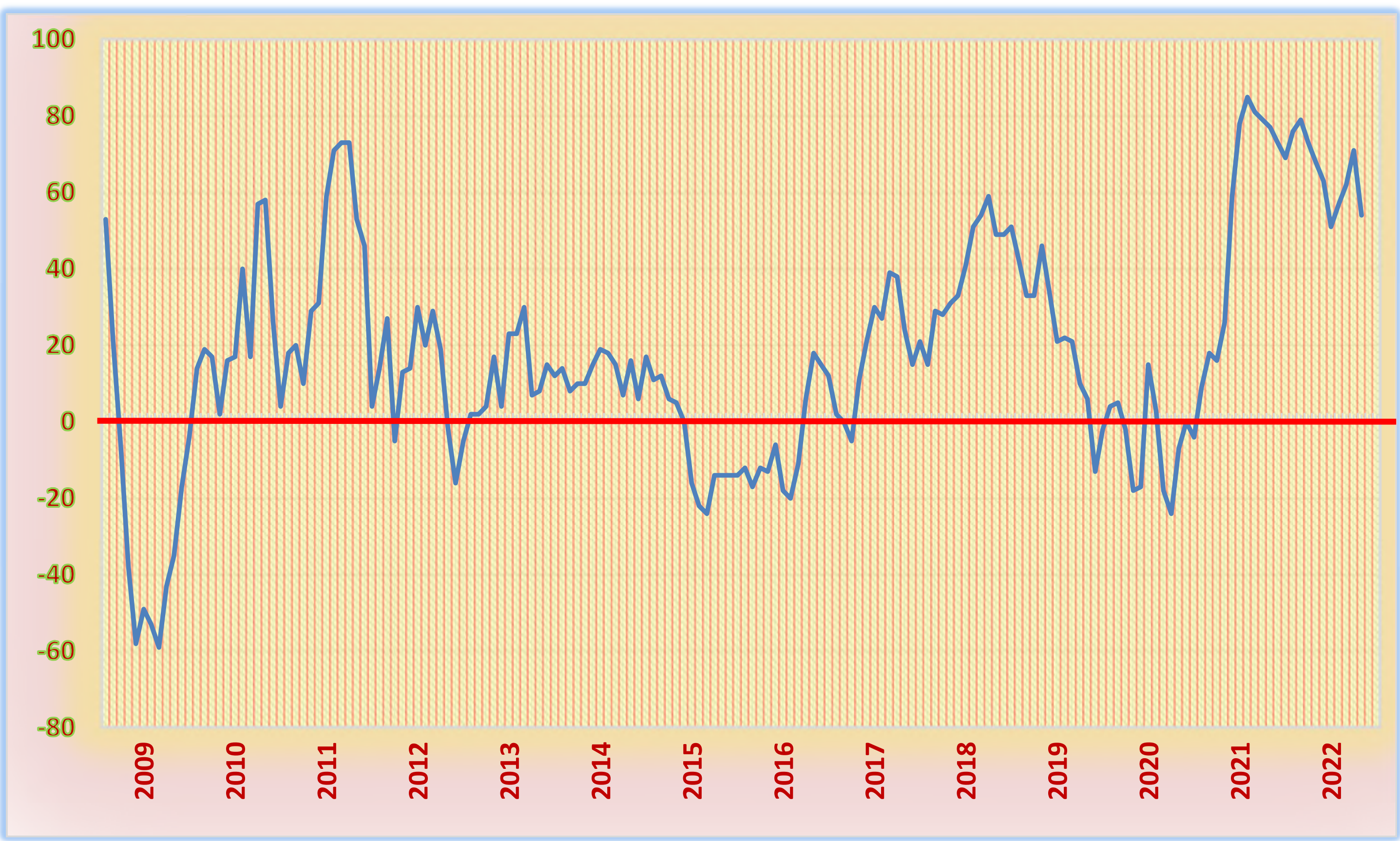
Great Recession
First Recovery + 3 in April 2009

COVID-19 Recession
First Recovery +12 in July 2020

ISM-West Michigan Index of New Orders: 2008-2022

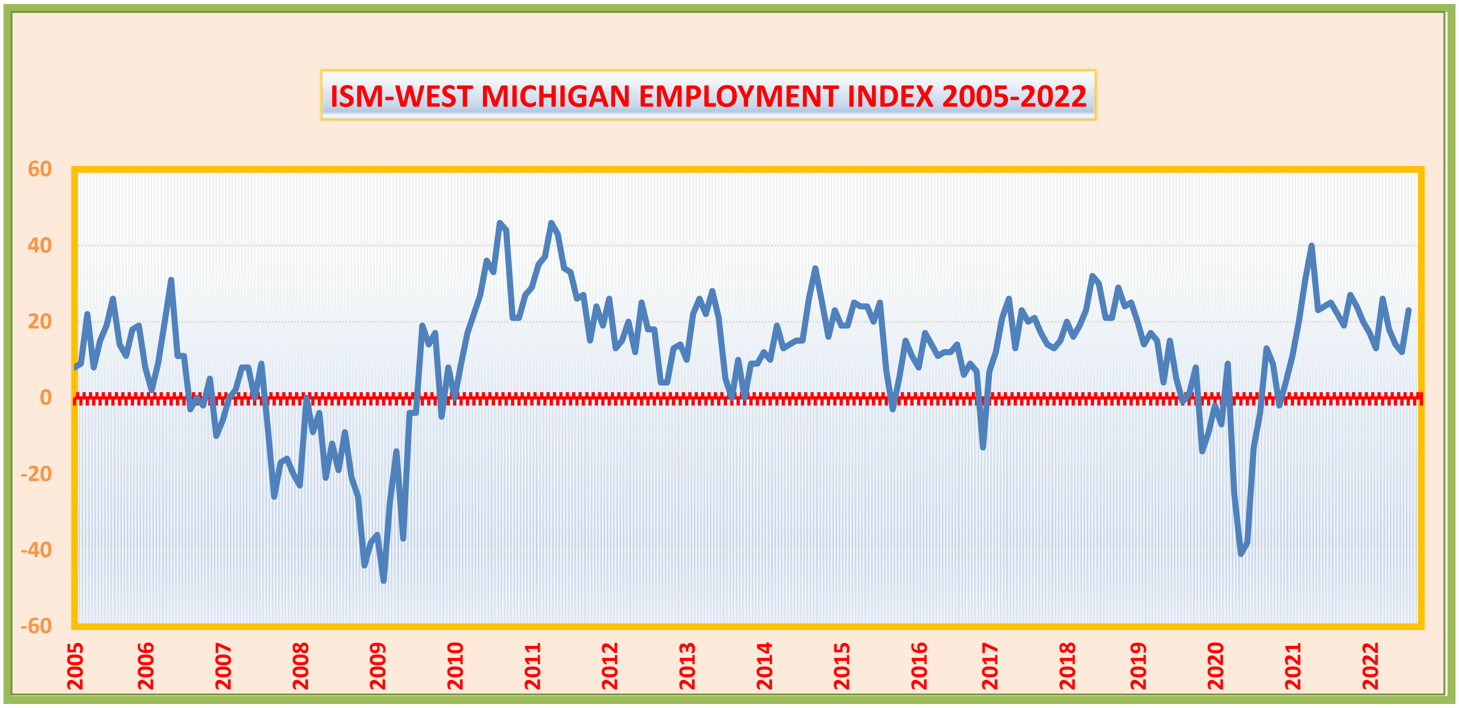


ISM-West Michigan Index of PRICES: 2008-2022



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 event 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.