Institute for Supply Management,
Greater Grand Rapids, Inc.
P. O. Box 230621
Grand Rapids, MI 49523-0321

News Release (For Immediate Release)

August 8, 2022

Current Business Trends

By Brian G. Long, Ph.D., C.P.M.
Director, Supply Chain Management Research
Grand Valley State University (269) 870-0428

WEST MICHIGAN ECONOMY WEAKENS TO 24-MONTH LOW

Key Participant Comments for July:

"We continue to work through the disruption of customer orders due to unscheduled automotive plant closing for a week or two at a time."

"Looks like there is a bit of a slowdown. Order entry has slowed down along with quoting activity. I think September will be a good indicator of where we are headed."

"Although some commodity pricing is going down, our suppliers are still pushing price increases to cover their rising costs for energy, freight, labor, etc."

"We continue to see shortages with electronics, chips, and wiring for CNC machinery."

"We're still seeing a shortage of rail car availability and truck drivers causing delivery delays."

Deriving a cue from the current national and world economic reports, the West Michigan economy has flattened. The July index of NEW ORDERS, our closely watched index of business improvement, fell to -3, down from June's posting of +26. The July PRODUCTION Index, which is now termed "output" by many economists, eased significantly to +7 from +31. Activity in the purchasing offices, as reflected in our index of PURCHASES, retreated modestly to +10 from +12. As a result of fewer disruptions in the industrial supply chains, the July Index of LEAD TIMES posted at +25, well below last month's +40, and decidedly lower than the reading of +93 from less than a year ago. Although many factories are still operating at or near capacity, higher commodity prices and rapidly rising transportation costs continue to restrict the profitability for many firms. Even though business conditions remain modestly positive for some survey respondents, the talk of an impending recession is resulting in many expansion plans being put on hold. If we do fall into a recession in the near future, our automotive parts producers are unlikely to slide very far. The pent-up demand for new cars will most likely keep the assembly line running for many months to come and could even bridge the entire downturn.

The U.S. Economy. The Institute for Supply Management, our parent organization, reports that the national economy is beginning to sag. ISM's NEW ORDERS Index for July came in at -3, down from last month's +1, the lowest report since the end of our most recent recession. Furthermore, the only time that the NEW ORDERS Index has turned negative is at the beginning of four of the last seven recessions. ISM's PRODUCTION (a.k.a., Output) Index posted at +8, down significantly from June's +16. After statistical adjustments, ISM's Composite Index registered at 52.8, slightly lower than last month's 53.0. Unfortunately, ISM's Composite Index has seldom reflected the future course of the industrial economy.

The July view of the U.S. economy from the newly named S&P Global, the British-based international consulting firm, is remarkably similar to the ISM report. Although S&P's seasonally adjusted U.S. Manufacturing Purchasing Managers' Index came in at a two-year low of 52.2, the report also noted that both the new orders and output indices have turned negative. The future outlook for the survey participants has also fallen to the lowest level since October 2020. Chris Williamson, Chief Business Economist at S&P Global, commented:

> "With the exception of pandemic lockdown periods, July saw U.S. manufacturers report the toughest business conditions since 2009. A growth spurt in the spring has quickly gone into reverse, with new orders for factory goods down for a second straight month in July, leading to the first drop in production for two years and sharply reduced employment growth. The rising cost of living is the most commonly cited cause of lower sales, as well as the worsening economic outlook. Companies are also taking an increasingly cautious approach to purchasing and inventories amid the gloomier outlook, and likewise appear to be cutting back on investment, with new orders falling especially sharply for business equipment and machinery in July. Supply chain problems remain a major concern but have eased, taking some pressure off prices for a variety of inputs. This has fed through to the smallest rise in the price of goods leaving the factory gate seen for nearly one and a half years, the rate of inflation cooling sharply to add to signs that inflation has peaked."

The World Economy. Any casual observer of the current news cycle could easily suspect that the J.P. Morgan Worldwide Manufacturing Report would signal increased economic stress. The JPM PMI for July eased to 51.1, marginally above the all-important break-even point of 50.0. As a result of stagnating, the report further noted that new orders contracted, international trade flows continued to retrench, and the pace of job creation flattened. The July PMI for Canada, our largest trading partner, eased to a 25-month low of 52.5, down from 54.6. The July PMI for Mexico, our second largest trading partner, fell sharply to 48.5 from June's 52.2. The PMI for China, our third largest trading customer, slipped from 51.7 in June to 50.4 in July. Like many other surveys, the "Caixin China" report cited declining orders and reduced production as causes for the slower performance. Bennett Parrish, Global Economist at J.P. Morgan, further noted:

> "The Global Manufacturing output PMI fell 2.4pts to 50.0 in July. The underlying dynamics survey are tracking levels typically reserved for recessions, with the new orders PMI dipping below 50 and jobs growth near-stalling. While supply chain bottleneck pressures appear to be abating, as evidenced by shortening delivery times and fading price pressures, these improvements largely reflect a softening in the pace of demand growth as a consequence of last quarter's surge in consumer prices."

Needless to say, many European countries now feel like they have painted themselves into a corner. Most countries in Europe and even the U.S. naively believed that opening trade with Russia was in everyone's best interest. Russia is now using trade, especially natural gas, as an economic weapon. Even though our domestic price of natural gas is nearly four times higher than it was just a few months ago, the European natural gas prices are about eight times higher than ours. Furthermore, Russia is now threatening to cut off gas supplies to Europe altogether. To keep homes from freezing next winter, industrial use of natural gas may need to be halted altogether. As previously noted, it may be a little late, but most European countries are now reevaluating their trade policies with Russia. Although all of the major economies in the Eurozone posted positive PMIs as little as two months ago, only the PMIs for Austria and the Netherlands remain positive as of July. Chris Williamson further commented:

> "Eurozone manufacturing is sinking into an increasingly steep downturn, adding to the region's recession risks. New orders are already falling at a pace which, excluding pandemic lockdown months, is the sharpest since the debt crisis in 2012, with worse likely to come. Production is falling at especially worrying rates in Germany, Italy and France, but is also now in decline in all other surveyed countries except the Netherlands, and even here the rate of growth has slowed sharply. Lower than anticipated sales, reflected in accelerating rates of decline of new orders and exports, have led to the largest rise in unsold stocks of finished goods ever recorded by the survey. Increasing numbers of producers are consequently cutting production in line with the deteriorating demand environment, as well as scaling back both their purchases of inputs and hiring of staff. One upside to the weakened demand environment is an easing of supply constraints, with the incidence of delays now the lowest since late-2020. This has in turn helped bring price pressures down considerably in the manufacturing sector. The notable exception is energy, where concerns are mounting regarding the impact of gas supply limitations in the months ahead. The energy crisis adds to the risks that not only will weaker demand and destocking cause manufacturing production to decline at an increased rate in the coming months, but reduced energy supply will act as an additional drag on the sector."

Automotive. Most of the major news channels continue to lament the chip shortage and the resulting impact on auto sales. Although the resulting decline in auto production continues to be a drag on the West Michigan economy, the demand for automobiles remains strong. According to the July 5 edition of *Automotive News*, the July SAAR (Seasonally Adjusted Annualized Rate) came in at 11.8 million units, down from 12.7 million units a year earlier. However, the chip shortage has not had an equal impact on all of the major brands. July sales at Ford rose 36.8 percent from June, the only major brand to post a significant gain. By sharp contrast, sales American Honda fell 47.4 percent. Of the other firms still reporting monthly, Toyota sales for July fell 27.3 percent, Volvo dropped 40.7 percent, and Hyundai-Kia eased 10.8 percent. The average for all of the reporting firms for July was down by 14.8 percent. Cox Automotive Senior Economist Charlie Chesbrough commented:

> "There are plenty of headwinds pushing against a notable recovery in sales volumes. Rising interest rates and low consumer sentiment are keeping many potential buyers out of the market. At the same time, higher prices for both gasoline and vehicles are making affordability an even greater challenge. Tight supply, however, continues to be the biggest obstacle over the near term, and there is little evidence of supply returning to normal."

Industrial Inflation. For industrial inflation, there is good news. Many "big ticket" commodities like copper, steel, lead, zinc, and oil have recently fallen in price. In the past, the bad news is that significant across-the-board drops in the prices for most major commodities has usually foreshadowed an impending recession. Our local index of PRICES eased to +31 from June's +54 and down significantly from +71 two months ago. In a similar move, July's ISM national index of PRICES fell to +20 from June's +57. In a more modest move, the J.P. Morgan world index of PRICES eased to 65.6 from 68.7. According to ISM's July report:

> "The slowing in price increases is being driven by (1) volatility in the energy markets, (2) softening in the copper, steel, aluminum and corrugate markets and (3) a significant decrease in chemical demand. Notably, 21.5 percent of respondents reported paying lower prices in July, compared to 8.3 percent in June."

Business and Consumer Confidence. The July Conference Board's index of Consumer Confidence edged lower to 95.7 (1985=100), down 2.7 points from 98.4 in June, and considerably lower than the 126.9 reported eight months ago. July's University of Michigan Consumer Sentiment Index edged up to 51.5 following June's record low of 50.0. For our West Michigan survey of the industrial economy, The SHORT-TERM BUSINESS OUTLOOK Index for July, which asks local firms about the business perception for the next three to six months, posted at -2, slightly below June's reading of +3, and well below the April reading of +20. Surprisingly, the LONG-TERM BUSINESS OUTLOOK Index, which queries the perception for the next three to five years, rose to +12, up from +3. However, the recent performance of both indices is still running well below our averages for the past eight years.

GDP. By now, most of the major news outlets have reported and re-reported that the Commerce Department's estimates for the second quarter GDP (Gross Domestic Product) declined by 0.9 percent. Since the first quarter GDP fell by an annualized rate of 1.8 percent, the second quarter drop has resulted in a few economists and some news media outlets declaring that we are now in a recession. As we heard for many years, a recession is "…two continuous quarters of negative economic growth as measured by GDP." However, for the last thirty or forty years, MOST economists have adopted a new definition for recessions. The longtime nonpartisan group called the National Bureau of Economic Research (NBER) now defines a recession as a "…significant decline in economic activity spread across the economy, lasting more than a few months." Along with GDP, this definition includes many other factors, including real income, employment, unemployment, industrial production, capital investment, and consumer spending, to name a few. Put simply, we're not there yet, but we're probably not far away from our next recession.

Summary. It goes without saying that there is a psychological aspect to almost any economic activity. With the nonstop rhetoric about an impending recession, some form of an economic downturn will be very difficult to avoid. We could actually "talk" ourselves into a recession. Reputable organizations like The Conference Board unabashedly forecast that U.S. economic growth will slow over the course of this year, and that a shallow recession will occur in "late 2022 and early 2023." We now face the risk that further inaction by the Federal Reserve could result in a return to another 1970s-style round of stagflation, wherein economic growth slows, unemployment edges higher, and a wage-price spiral forces the CPI higher and higher. At this time, it appears that the Fed has painted itself into a proverbial corner. By raising interest rates too fast, the economy will also slow too fast, and the Fed will be heavily criticized. By not raising interest rates fast enough, inflation will continue to rise far ahead of the 2 percent target, a perpetual wage-price spiral will set in…. and the Fed will be heavily criticized. To monitor our local economy, we will keep a sharp eye on the index of NEW ORDERS. In the past, when this index declines for three successive quarters, a recession has almost always followed. Another statistic to watch is our index of RAW MATERIALS INVENTORIES. In the long-time trend toward just-in-time inventory, most major firms kept their inventories low for at least the last thirty years. As a result of supply disruptions and rising prices, many firms have now built inventories excessively high by historical standards. With commodity prices now falling and supply bottlenecks receding or disappearing, many of these major firms could decide to stop future orders and live off their bloated inventories. The result could be that about a half trillion (with a "t") dollars could be pulled out of the economy in a relatively short period of time. The consequences are obvious.

JULY COMMENTS FROM SURVEY PARTICIPANTS

"It's a challenging environment."

"Although some commodity pricing is going down, our suppliers are still pushing price increases to cover their rising costs for energy, freight, labor, etc."

"Steady. But headwinds seem to be on the horizon."

"The market continues to be strong, but similar to previous months, increased costs are offsetting additional sales."

"We are still carrying more raw materials on hand than our goal due to lead times on supply."

"We continue to work through the disruption of customer orders due to unscheduled automotive plant closing for a week or two at a time."

"I could write a lot here, but it would get into the problems with our government. So, I'm not going too."

"Sales continue to be strong. But July and August are big vacation months, we will not be able to keep up with the demand, and our backlog will grow."

"Looks like there is a bit of a slowdown. Order entry has slowed down along with quoting activity. It's possible, that many people are taking real vacations after two years of sheltering in place. I think September will be a good indicator of where we are headed."

"We're starting to see some relief on metal pricing, but scrap rates are also dropping quickly."

"Business is soft for us, but we expect a rebound in September."

"Labor and operating costs seem to be the current cost drivers. Our business is labor intense vs. automated."

"We continue to see shortages with electronics, chips and wiring for CNC machinery."

"We're still seeing a shortage of rail car availability and truck drivers causing delivery delays."

"You do not know what a vendor doesn't have in stock or available until your order it. It's making my work really hard in the world today."

July 2022 Survey Statistics

	UP	SAME	DOWN	N/A	July Index	June Index	May Index	25 Year Average
Sales (New Orders)	29%	6%	32%	0%	- 3	+26	+14	+14
Production (Gross Output)	24%	49%	17%	10%	+ 7	+31	+ 7	+14
Employment	37%	51%	10%	2%	+27	+23	+12	+ 8
Purchases	27%	56%	17%	0%	+10	+12	+ 0	+ 7
Prices Paid (major commod.)	46%	39%	15%	0%	+31	+54	+71	+15
Lead Times (from suppliers)	37%	51%	12%	0%	+25	+40	+41	+11
Purchased Materials Inv. (Raw materials & supplies)	42%	44%	12%	2%	+30	+32	+ 9	- 4
Finished Goods Inventory	24%	49%	20%	7%	+ 4	+ 3	- 4	- 8
Short Term Business Outlook (Next 3-6 months)	20%	58%	22%	2%	- 2	+ 3	+ 7	-
Long Term Business Outlook (Next 3-5 years)	27%	56%	15%	2%	+12	- 3	- 2	-

Items in short supply: Electronics, microchips, semiconductor chips, electronic components, specialty resins, steel-based products, freight. Perasan, domestic rail and trucking, aluminum, custom aluminum extrusions, some steel, fasteners, machined parts, connectors, motors, explosion proof motors, casings, rubber hose, copper wire, labor.

Prices on the UP side: Gaskets and seals, connectors, all metals, pipe fittings, aluminum, steel, freight, packaging, connectors, electronic components, powdercoat, casters, fasteners, oil and steel-based items, specialty resins (UV, pre-colored, etc.), natural gas, steel, cardboard, labor costs.

Prices on the DOWN side: Freight charges*, scrap steel, steel*, steel wire rod, stainless steel, polypropylene, sea transportation, international freight, ocean freight, imported lumber, copper, brass, aluminum*, some wood products.

*Item reported as both up AND down in price.

Latest Unemployment Reports

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

	June 2022	June 2021	Aug. 2009	20 Year Low
State of Michigan (June)	4.3%	6.3%	14.6%	3.2%
State of Michigan (Unadj.)	4.8%	6.8%	14.1%	2.9%
Kent County	4.0%	5.5%	11.9%	2.1%
Kalamazoo County	4.4%	6.0%	11.1%	2.1%
Calhoun County	5.6%	7.7%	12.8%	2.7%
Ottawa County	3.6%	4.8%	13.3%	1.8%
Barry County	4.1%	5.2%	10.9%	2.2%
Kalamazoo City	5.5%	7.4%	15.2%	3.2%
Portage City	4.1%	5.5%	8.7%	1.3%
Grand Rapids City	5.3%	7.3%	16.1%	3.0%
Kentwood City	3.7%	5.2%	10.7%	1.4%
Plainfield Twp.	3.0%	4.2%	8.0%	1.4%
U.S. Official Rate (July)	3.5%	5.9%	9.6%	3.5%
U.S. Rate (Unadjusted)	3.8%	6.1%	9.6%	3.4%
U.S. U-6 Rate (June)**	6.7%	9.6%	22.9%	6.7%

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

Index of New Orders: West Michigan

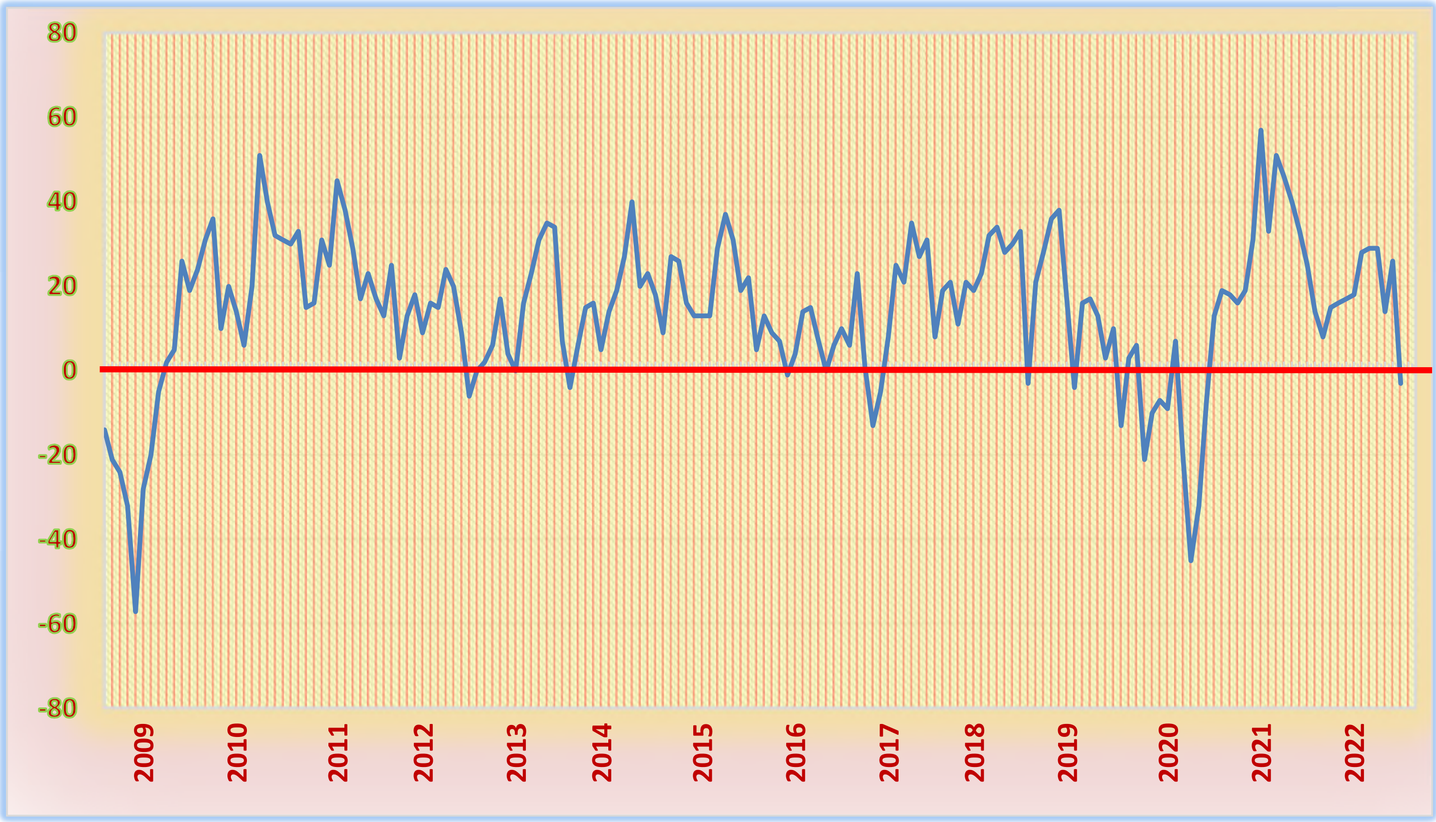
As the name implies, this index measures new business coming into the firm, and signifies business improvement or business decline. When this index is positive for an extended period of time, it implies that the firm or organization will soon need to purchase more raw materials and services, hire more 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	- 3 for the month of July, 2022
Previous Month	+ 26 for the month of June, 2022
One Year Ago	+ 46 for the month of July, 2021
Record Low	- 57 for the month of December 2008
Record High	+ 57 for the month of January 2021

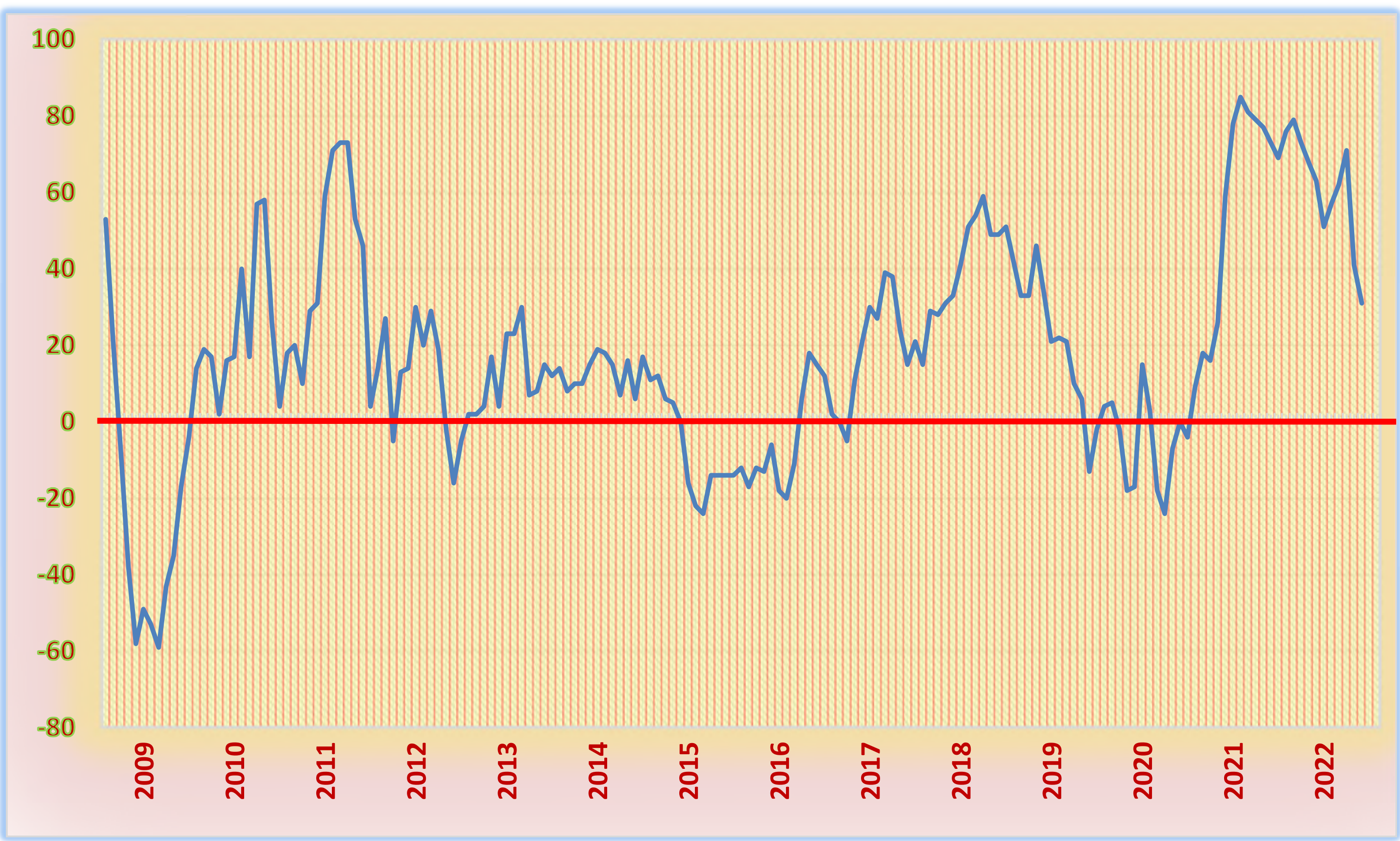
Great Recession
First Recovery + 3 in April 2009

COVID-19 Recession
First Recovery +12 in July 2020

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

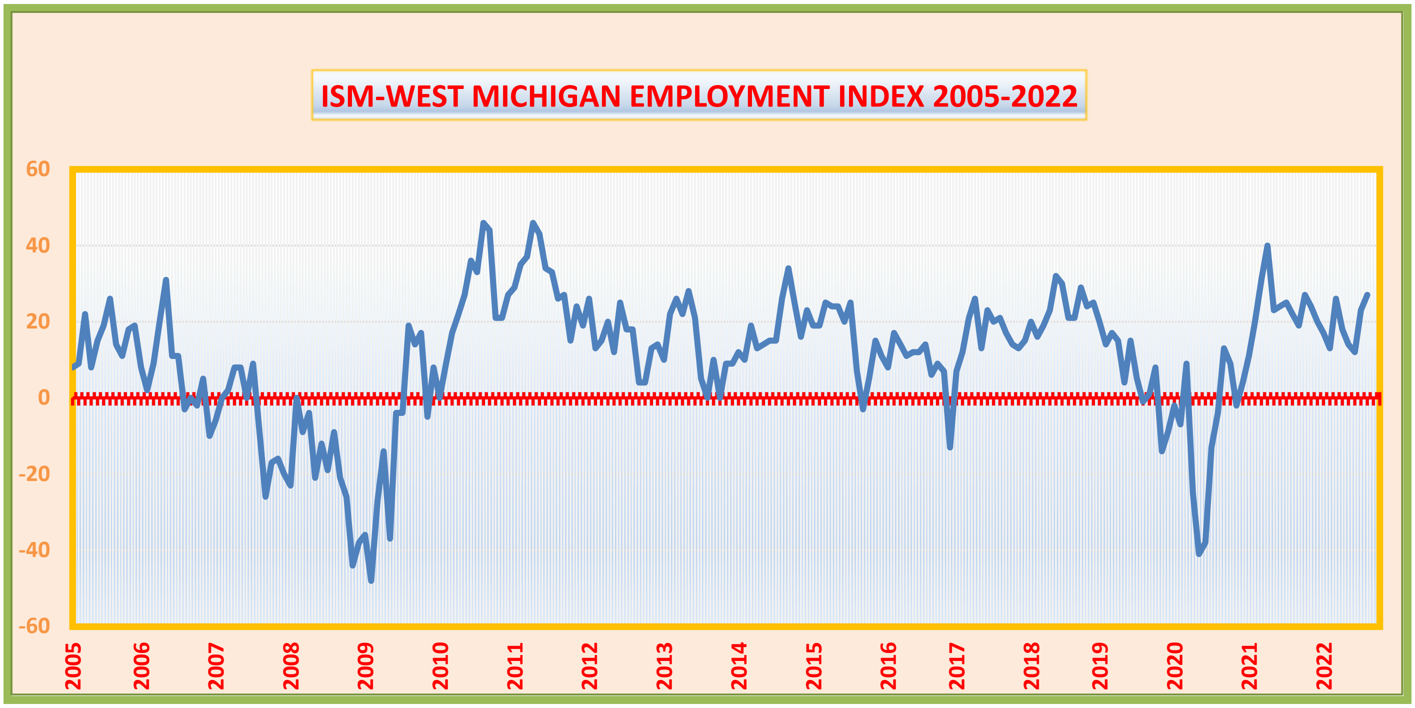


ISM-West Michigan Index of PRICES: 2008-2022



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.