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West Michigan Current Business Trends

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GROWTH RATE RATE TURNS MODESTLY NEGATIVE

Key Take-Aways from September 2023 Statistics:

- **West Michigan Industrial Economy Turns Modestly Negative**
- **National Industrial Economy Remains Flat**
- **UAW Strike Remains a Wild Card**

	Sept.	Aug.
NEW ORDERS Index (business improvement)	- 9	- 4
PRODUCTION Index (aka "output")	- 5	+ 14
EMPLOYMENT Index	+ 0	+ 2
LEAD TIMES Index	- 13	-14

Key Participant Comments for September:

"Customer demand for the month remains strong while raw material costs sliding at an accelerated pace. Our labor market is still very tight, and retention bonuses are required to keep employees."

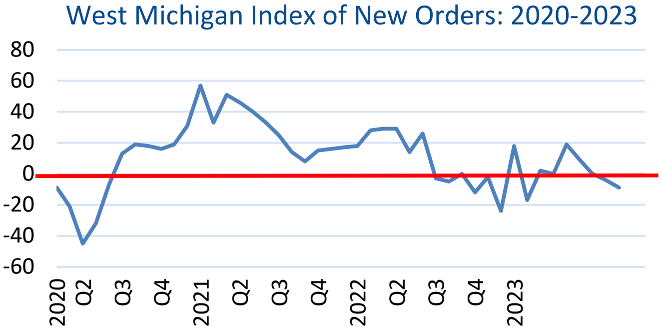
"We will hit forecast this month, but incoming orders are starting to slow. We still need to reduce inventory, so we are cutting back on purchases. The shop floor is using excess time to catch up on training and kaizen."

"The UAW strike will have a large impact on our business. If the strike continues much longer, all of our manufacturing locations and employees will be negatively impacted."

"Sales in August rebounded to an acceptable level from a slow July, but office furniture is still slow."

The Local Economy. Much as we had hoped, the West Michigan economy still shows no sign of an impending recession but is continuing to slow. That's not all bad, because the Federal Reserve wants the economy to gradually slow in order to reduce inflation. In West Michigan, we are doing our part, given that our September survey edged low enough to be termed "modestly negative." NEW ORDERS, our index of business

West Michigan Index of New Orders: 2020-2023



improvement, fell to -9 from -4. The PRODUCTION Index, which some economists label as "output," dropped sharply from +14 to -5, confirming that the August reading was probably an anomaly. The index of PURCHASES, which measures activity in purchasing offices, continued its downward slide and posted at -22, down from -17. At this time, many of our auto parts suppliers continue to voice concerns over the UAW strike against the Detroit Three auto firms. Many firms that sell to only the Detroit Three cannot easily endure a long strike. However, most of our local auto parts firms do not do business exclusively with the Detroit Three. The hawkish rhetoric of the UAW implies that the strike still has a long way to go, but neither the auto firms or the UAW (or its members) can withstand a lengthy strike. On the brighter side, past history tells us that labor negotiations can have a breakthrough at any moment resulting in a new contract and a welcome announcement that everyone will soon be back to work. Paraphrasing Shakespear, this concern about the strike could be much ado about nothing.

The U.S. Economy. According to the September survey from the Institute for Supply Management, the U.S. economy continues to be flat. ISM's NEW ORDERS Index came in at -4, slightly better than August's -6, but still marginally below the break-even point of +0. The PRODUCTION Index (a.k.a., Output) for ISM remained positive at +3, up from +1. ISM's closely-watched ORDER BACKLOG Index edged lower to -15, down from -12. The NEW EXPORT ORDERS Index modestly recovered to -5 from -7. After adding ISM's seasonal adjustments to the survey statistics, the composite index for September came in at 49.0, only a small margin below the all-important break-even point of 50.0.

A confirming view of the U.S. economy comes from the British-based economic consulting firm now called S&P Global. Although S&P's index of New Orders eased marginally in September, both the Output and Employment indices came in modestly positive. S&P's Composite PMI for September posted at 49.8, up nicely from August's 47.9. Chris Williamson, Chief Business Economist at S&P Global Market Intelligence, further commented:

> "September saw a welcome near-stabilization of business conditions in manufacturing, but a further increase in price pressures is a concern on the inflation front. Output reversed some of the loss seen in August as higher employment and improved supply availability helped factories fulfil backlogs of orders. Although the pace of production growth remains disappointingly subdued thanks to a further decline in new orders received during the month, notably from weak export markets, there are signs that the situation will improve as we head through to the end of the year. Manufacturers' expectations of future output have jumped to their highest for nearly one and a half years, supply conditions continue to improve, and the rate of order book decline has moderated considerably in recent months, in part due to fewer producers and customers reporting deliberate cost-focused inventory reduction policies. Less encouraging was the news on the inflation outlook, as producers' costs rose at the fastest rate for five months, largely on the back of higher oil prices. These increased costs are already feeding through to higher prices to customers, which will inevitably result in some renewed upward pressure on inflation."

The World Economy. The J.P. Morgan Worldwide Manufacturing Index posted at 49.1 for September, up marginally from 49.0, but still below the neutral point of 50.0. JPM's New Orders Index edged higher to 48.4 from 48.1. In a similar move, JPM's Output Index improved to 49.7 from 49.4. The PMI for Canada, our largest trading partner, eased to 47.5 from 48.0. The September PMI for Mexico, our second largest trading partner, fell to 49.8 from 51.2. The PMI for China, our third largest trading partner, eased to 50.6, down from 51.0. Bennett Parrish, Global Economist at J.P. Morgan, further commented:

> "Global manufacturing remained in the doldrums at the end of the third quarter, as output, new orders and employment all contracted. The Eurozone, UK and Canada posted steep overall downturns, with global growth lead by China and Indonesia. The US posted higher output and jobs but lower new orders. All five of the sub-indices comprising the headline PMI (output, new orders, employment, stocks of purchases and suppliers' delivery times) were at levels indicative of a deterioration in overall performance. A weaker intake of new orders was the main factor underlying lower output in September. Destocking also played a role, with inventories of both finished products and raw materials decreasing during the latest survey month."

Each month, the Hamburg Commercial Bank (HCOB) posts a report on the Eurozone economy. For September, the composite PMI posted at 43.4, down modestly from August's 43.5. The bad news is that HCOB's New Orders Index declined at the fastest rate in the survey's 26-year history. Although the Ukrainian war continues to be a factor in all of the European economies, the index is also skewed by the 39.6 PMI for Germany, the largest economy in the group. Except for Greece, the PMIs for all of the other major European countries remain negative. Some analysts continue to blame the current weakness in New Orders on "destocking," a term for the gradual liquidation of excess inventories previously accumulated as a result of rising prices and shortages. When the Berlin wall came down, many Europeans thought that war was now a thing of the past. However, analysts point to the systemic fear that Europe may be entering a new era called "Cold War, Part Two." Dr. Cyrus de la Rubia, Chief Economist at HCOB, further noted:

> "The Output PMI was well under 50.0 for the entire third quarter, so we are feeling pretty certain that the recession in manufacturing continued during this period. We probably won't see things picking up until we ring in the new year, but there are reasons to believe that the bottom of the hard-to-pin-down stocking cycle has been reached. In the race to the bottom, France and Germany are leading the way in the September PMIs. Meanwhile, Spain and Italy are pulling through somewhat less scathed. However, if you take the duration of the slowdown into account, considering official monthly production figures, Italy is the worst performer, with its manufacturing sector mired in a recession since the second half of 2022. Italy is followed by Germany, where a recession has started in the second quarter of this year. For France and Spain, we cannot confirm a technical recession yet. Given our forecast that the global manufacturing sector is bottoming out, these countries may be spared from a downturn lasting longer than two quarters."

Automotive. So far, the UAW strike has had little or no impact on most of our West Michigan auto parts suppliers. Given the diversity of the customer base for many local firms, it is still hopeful that a prolonged strike will do little more than dampen the local automotive economy. However, a prolonged strike, such as the record 67-day G.M. strike, will have a more obvious impact on the overall Michigan economy. Otherwise, the auto industry remains strong. The September sales reported by *Automotive News* estimates that the year-over-year SAAR (Seasonally Adjusted Annualized Rate) posted at 15.5 million, up slightly from August's 15.2 million sales level. Some manufacturers no longer report monthly sales, but ALL firms now report quarterly. Looking at sales for the major firms in the third quarter of 2023 in rank order, Honda, hardest hit by the chip shortage, gained 33.3 percent, Nissan rose 26.7 percent, General Motors added 19.4 percent, Hyundai-Kia, 15.0 percent, and Toyota, 3.8 percent. The only quarterly loser was Stellantis, down 1.3 percent, largely because of declining volume at Jeep. Jeff Schuster, head of GlobalData's automotive practice, further commented:

> "The outlook for the remainder of the year remains positive into 2024. Resilience in consumer purchases remains the driving factor that is supporting the industry and the economy."

West Michigan Unemployment. So far, the employment situation in West Michigan remains relatively stable, although a modest uptick in unemployment remains possible as we enter 2024. The West Michigan EMPLOYMENT Index flattened to +0, down marginally from August's +2. For September, 16 percent of this month's survey respondents reported staff reductions, up from 13 percent in August and 6 percent in July. At the state level, the Michigan Department of Technology, Management & Budget (DTMB) reported that the August (latest month available) seasonally adjusted year-over-year unemployment rate for Michigan edged up to 3.7 percent from 3.6 percent. For West Michigan, the August unemployment rate (unadjusted) for Kalamazoo County posted at 4.2 percent, Kent County, 3.6 percent, and Calhoun County, 4.8 percent. At 3.5 percent, Ottawa County reported the lowest county unemployment rate for West Michigan.

Business and Consumer Confidence. Just like last month, both consumer and business confidence are waning, but clearly not collapsing. According to the most recent press release, the September Conference Board

Consumer Confidence Index has fallen to 103.0 (1985=100), down from 108.7 in August. In a similar move, the September University of Michigan Index of Consumer Sentiment backtracked to 68.1 from 69.5. The survey author noted that rising interest rates, inflation, and labor unrest, consumers are "reserving judgment" about the direction of the economy. For our local survey, the SHORT-TERM BUSINESS OUTLOOK Index for September, which asks local firms about their business perceptions for the next three to six months, fell significantly to -15 from -2. The LONG-TERM BUSINESS OUTLOOK Index, which queries the perceptions for the next three to five years, downticked modestly to +15 from +19.

Industrial Inflation. For September, our West Michigan index of PRICES posted at the -5, down from the break-even point of +0. At the national level, the September ISM index of PRICES came in at -12, down from August's -4. Although the supply situation for a few commodities like higher-end electronics remains tight, most big-ticket commodity prices continue to fall. At 0.8, the S&P's Global Supply Shortage Index has fallen to its lowest level in 44 months. Commenting on the latest price trends, Usamah Bhatti at S&P Global Market Intelligence, noted:

> "The latest indicators signalled that commodity price and supply pressures remained muted at the end of the third quarter. Commodity prices were reportedly down for the fifth month in a row, though the latest reduction was the softest in this sequence. This included falls in semiconductors, aluminum, copper, iron, steel and electricity. The continued downward trend for prices has underlined a gradual easing in global input costs at manufacturers, although the latest J.P. Morgan Global Manufacturing PMI data pointed to a degree of stickiness in input prices in September. Supply chain pressures moderated to the lowest since January 2020. Only five of the monitored commodities saw reported shortfalls above the long-run trend during September, with transport, aluminum and electrical items registering the most acute shortages."

Consumer Inflation. Regrettably, moderate inflation continues to be an ongoing problem with no immediate end in sight. CPI increases, after topping out at about 8.5 percent earlier in the year, began falling and continued to fall until about July. The August data confirms that the decline has now stalled and has even started to edge higher. The August (most recent month available) CPI stands at 3.7 percent, up from 3.2 percent in July. The core CPI posted at 4.3 percent, down from 4.7 percent. Although the CPI is what most consumers use to judge inflation, the Federal Reserve continues to place more importance on their own index of Personal Consumptions Expenditures (PCE). According to the September 29th press release, the August PCE index showed all prices increasing at a rate of 3.5 percent, up from 3.4 percent. The core PCE, which excludes food and energy, declined to 3.9 percent from 4.3 percent. It is worth repeating that inflation could be stuck at or near 3 to 4 percent for at least the next year or more. If the Federal Reserve continues to tighten interest rates until reaching the long-term goal of a 2.0 percent annual growth rate, higher rates may be coming.

GDP. According to the September 28th press release from the Bureau of Economic Analysis (BEA), the third and final estimate of year-over-year growth for the 2023 second quarter came in unchanged at 2.1. We are now waiting for October 26th when the BEA will announce the first official estimate of growth for the third quarter. The September report from the Atlanta Federal Reserve's GDPNow model forecasts a third quarter growth rate of 4.9 percent, down from 5.6 percent last month, but still very optimistic. The average for the Blue Chip GDP real-time model continues to edge higher, and now estimates a third quarter growth rate of 2.9 percent. In an apparent reversal from past reports, the Conference Board is now expecting the GDP for all of 2023 to end up at 2.9 percent, followed by a 2.5 percent rate for 2024. On the negative side, as of July 11th, J.P. Morgan continues to forecast a shallow recession starting "late in 2023." Looking at all forecasts, the consensus for 2023 third quarter growth still appears to be in the range of 2.1 to 2.4 percent, In other words, growth for the last two quarters of 2023 will be similar to the first two quarters of the year.

Looking Forward. For most of Michigan, all eyes are still on the Detroit Three auto firms and the UAW strike. Assuming that the auto firms do not suddenly capitulate, the strike could have many more days to go. Since neither the UAW nor the auto firms can endure a lengthy strike in today's economy, we should soon see a settlement, one way or another. Another wild card is to what degree Washington might decide to get involved. Fortunately, many of our local firms have wisely diversified their customer base to include Japanese and Korean non-union auto firms. A few have not. Therefore, even a prolonged strike will probably have only a dampening effect of the West Michigan economy.

Another concern for the overall economy comes from continued inflation and the response by the Federal Reserve to correct it. Without forcing a recession, the task of reaching the 2.0 percent target has now grown increasingly difficult. According to Bankrate, the current interest rate for a 30-year mortgage has risen to 7.83 percent, up from 7.51 percent last month. Needless to say, the interest rates for all other types of loans are rising at a similar rate, including the rates for financing the construction of new multifamily housing. The increase in rental rates, which had been running as high as 15 percent last year at this time, had briefly returned to normal in July. However, rising interest rates appear to have been the main factor causing the decline in rental rates to stall. The Fed had been delt a difficult hand. Overtightening could cause a recession, but undertightening could easily lead to another round of runaway inflation like we experienced in the 1970s. However, even with no action by the Fed, the cost of almost all loans of all types are continuing to rise. Hence, another rate increase seems unnecessary at this time.

September 2023 Survey Statistics

	UP	SAME	DOWN	N/A	Sept. Index	Aug. Index	July Index	25 Year Average
Sales (New Orders)	20%	51%	29%	0%	- 9	- 4	+ 0	+14
Production (Gross Output)	13%	65%	18%	4%	- 5	+14	- 3	+14
Employment	16%	66%	16%	2%	+ 0	+ 2	+ 7	+ 8
Purchases	9%	58%	31%	2%	-22	-17	- 5	+ 7
Prices Paid (major commodities)	13%	67%	18%	2%	- 5	+ 0	- 7	+15
Lead Times (from suppliers)	9%	67%	22%	2%	-13	-14	- 21	+11
Purchased Materials Inv. (Raw materials & supplies)	18%	56%	24%	2%	- 6	- 5	- 7	- 4
Finished Goods Inventory	7%	67%	24%	2%	-17	- 4	- 26	- 8
Short Term Business Outlook (Next 3-6 months)	9%	67%	24%	0%	-15	+ 2	+ 0	-
Long Term Business Outlook (Next 3-5 years)	31%	51%	16%	2%	+15	+19	+23	-

Items in short supply:

Import items, custom components, castings, some steel, some steel alloys, some aluminum, copper, brass, electronics, trained/qualified people.

Prices on the UP side:

Brass, brass forging, castings, copper, fuel, SSD, powder coat, products that contain electronics, products with high labor content, meat, dairy, most dry goods, capital equipment, freight.

Prices on the DOWN side:

Corrugated Packaging, steel*, aluminum, most shop supplies, steel scrap, stainless scrap, ocean containers, plastic resins (PP, ABS, PC, PPE), carbon steel, stainless steel, specialty lumber, produce and poultry.

**Item reported as both up AND down in price*

Latest Unemployment Reports:

(Except as noted, data are NOT seasonally adjusted)

	Aug. 2023	Aug. 2022	Aug. 2009	20-Year Low
State of Michigan (July)	3.7%	4.2%	14.6%	3.2%
State of Michigan (Unadj.)	4.2%	4.3%	14.1%	2.9%
Kent County	3.6%	3.8%	11.9%	2.1%
Kalamazoo County	4.2%	4.3%	11.1%	2.1%
Calhoun County	4.8%	5.2%	12.8%	2.7%
Ottawa County	3.5%	3.5%	13.3%	1.8%
Barry County	3.7%	4.0%	10.9%	2.2%
Kalamazoo City	5.2%	5.4%	15.2%	3.2%
Portage City	3.8%	4.0%	8.7%	1.3%
Grand Rapids City	4.7%	5.0%	16.1%	3.0%
Kentwood City	3.4%	3.5%	10.7%	1.4%
Plainfield Twp.	2.7%	2.8%	8.0%	1.4%
U.S. Official Rate (Aug.)	3.8%	3.7%	9.6%	3.5%
U.S. Rate (Unadjusted)	3.9%	3.8%	9.6%	3.4%
U.S. U-6 Rate (Aug)**	7.1%	7.2%	22.9%	6.7%

***U-6 for Michigan = 6.9% for 2022 and Q1 2023*

SEPTEMBER COMMENTS FROM SURVEY PARTICIPANTS

"Customer demand for the month remains strong while raw material costs sliding at an accelerated pace. Our labor market is still very tight, and retention bonuses are required to keep employees."

"We have cautious optimism to finish out the year as strong as the first three quarters. We're starting to see some items pulling back, possibly from UAW strike, but some increasing as well. The full impact from the strike is anyone's guess at this time."

"Our Q4 is going to be a belt tightening exercise!"

"The auto strike has the attention of the entire country. Hopefully it can get resolved before too much damage is done to the supply chain."

"Supply, pricing, and production are pretty much at the same as they were last month with construction slowing down over the next couple of weeks. We're trying to finish out the season strong."

"Our business remains slow through the 4th quarter."

"The UAW strike will have a large impact on our business. If the strike continues much longer, all of our manufacturing locations and employees will be negatively impacted."

"We're seeing a return to our pre-pandemic annual business seasonality trends."

"Sales in August rebounded to an acceptable level from a slow July, but office furniture still slow. Indicators suggest a slowdown in the Marine industry as well."

"Our government needs to stop spending money and just printing money. Our dollar is 40% less than it was two years ago.

"We're watching to see if the UAW strike has much of an impact (or longer-term impact) on our business."

"Production and employment are down as a reflection of the partial seasonal nature of the business."

"In our industry, the demand is exceeding the capacity resulting in backlogs in our production and delivery to the end customers. We have considerable hostage inventory waiting on one or two components that are needed to build many of our products."

"We will hit forecast this month, but incoming orders starting to slow down. We still need to reduce inventory so we are cutting back on purchases. Shop floor is using excess time to catch up on training and kaizen."

"The general demand for construction materials is down, so near term growth will only come from increased market share."

"We are seeing machinery manufacturers build inventory and offering discounts to move supply."

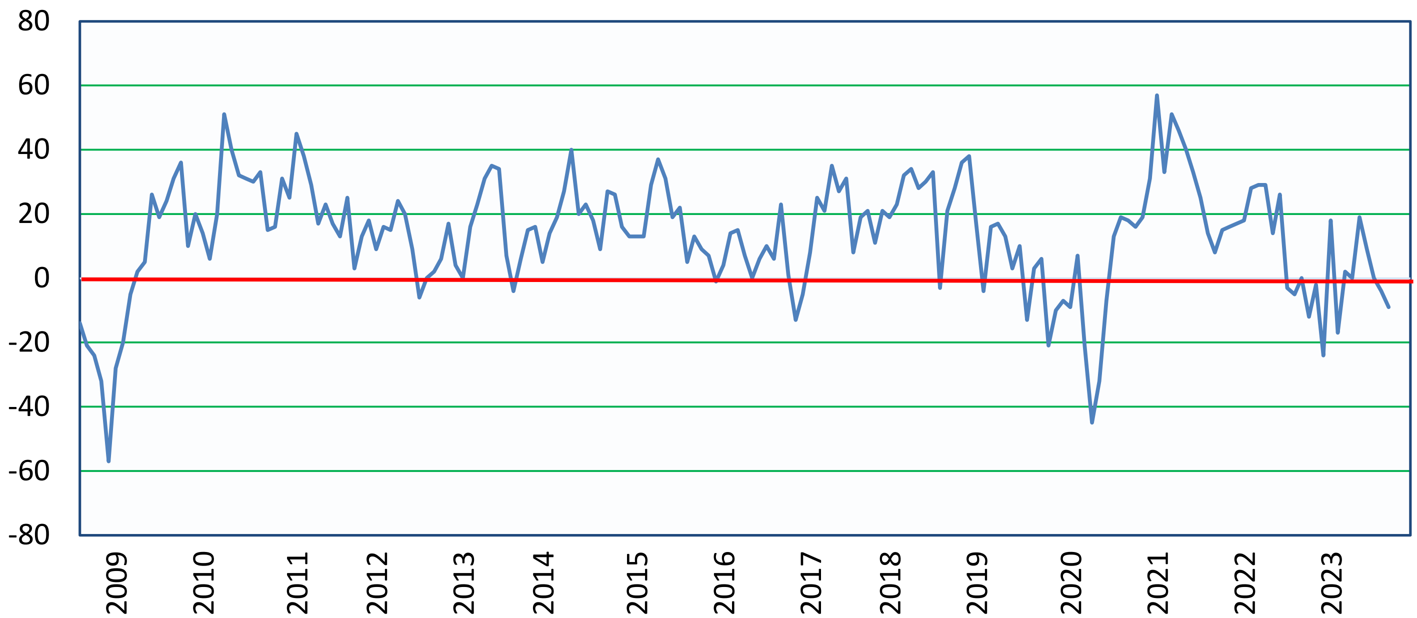
"We still have long lead times on most imported goods. Suppliers are cutting in-house inventories and turning more products to a pre-order or special order status."

"Electronics and some steel materials continue to be allocated resulting in uncertain lead times to receive our orders."

"Holding steady."

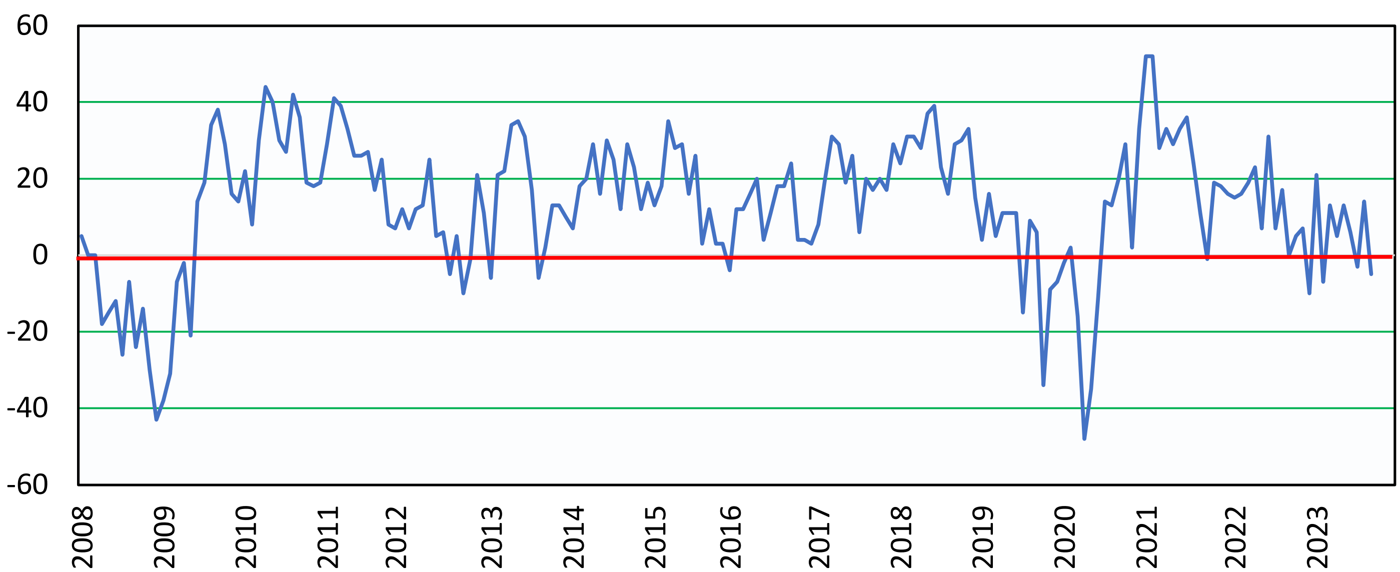
West Michigan Index of New Orders: 2008-2023

As the name implies, the NEW ORDERS 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.



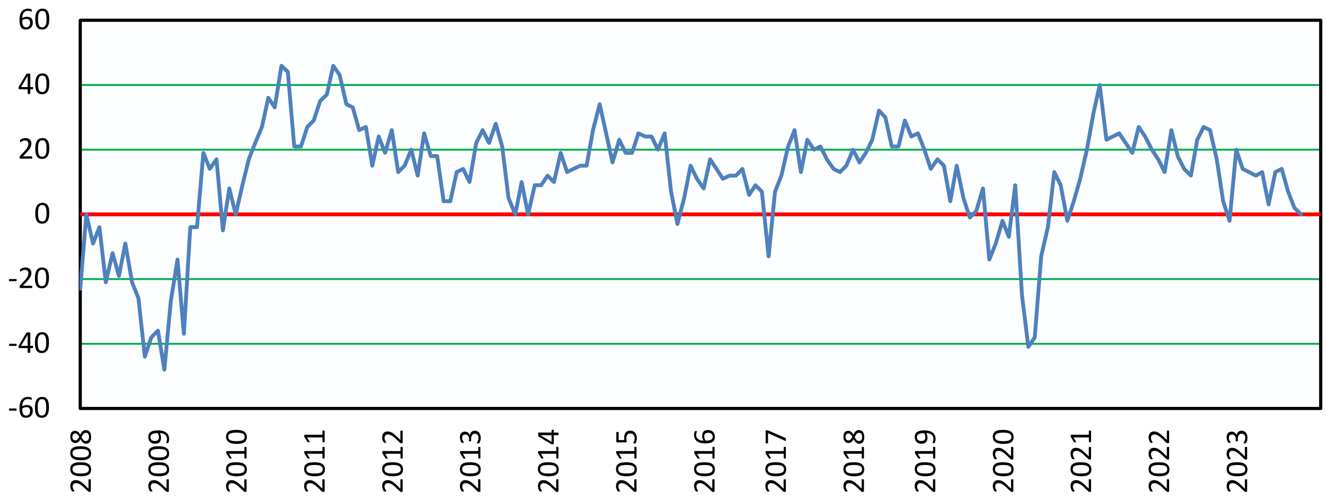
West Michigan Index of Production (Output): 2008-2023

As new orders come in and materials arrive at the loading dock, production schedules are posted to meet the customer's needs. Although production schedules respond to demand, they also respond to seasonal factors such as holidays as well as bad weather, materials shortages, or other external influences.



West Michigan Index of Employment: 2008-2023

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.



Michigan Future Business Outlook: 2013-2023

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.