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West Michigan Current Business Trends

December 11, 2023

INDUSTRIAL MARKET STILL MODESTLY NEGATIVE

Key Take-Aways from November 2023 Statistics:

- **West Michigan Economy Remains Modestly Negative**
- **National Industrial Economy Also Modestly Negative**
- **The Impact of Higher Interest Rates Remains a 2024 Wild Card**

	Nov.	Oct.
NEW ORDERS Index (business improvement)	-10	-13
PRODUCTION Index (aka "output")	- 4	- 4
EMPLOYMENT Index	- 5	- 10
LEAD TIMES Index	- 8	-17

Key Participant Comments for November:

"The 'return to office' is still in transition but seems to be helping the office furniture industry."

"We expect to finish the year exactly flat with a strong outlook going into next year."

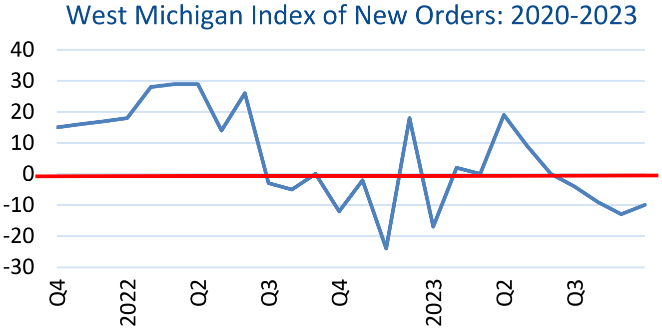
"Business looks very slow for the next several months."

"Glad the UAW strike is about over so we can get back to selling our products!"

"We're still having trouble finding qualified machine builders and manufacturing leaders."

The Local Economy. In the hope of reducing inflation without triggering a recession, the Federal Reserve has been raising interest rates for what will soon be two years. Just as last month, the West Michigan economy continues to slow in a fairly orderly fashion. Industrial inflation has now slowed to a normal rate, most of the major logistical bottlenecks have been cleared, and most employers are having less trouble filling open positions. Despite higher interest rates, there is still no immediate sign of a recession waiting for us in the next several months. For our West Michigan survey, NEW ORDERS, the all-important index of business improvement, posted

West Michigan Index of New Orders: 2020-2023



at -10, a modest improvement over October's -13, and in line with September's reading of -9. The PRODUCTION Index, which some economists label as "output," remained unchanged at -4. The index of PURCHASES, which measures activity in purchasing offices, recovered modestly to -12 from -17. As we head into 2024, the UAW strike is now history, and strong auto sales should continue to keep our local auto parts suppliers busy well into the summer. Although some members of the white-collar workforce will continue to work from home, the "return to office" mandate by many firms should keep our local office furniture firms from further distress. After hearing warnings of an impending recession for nearly two years and enduring numerous predictions of a 2023 recession from several reputable forecasters, we still find the December economy to be stable, even though significantly higher interest rates are beginning to pinch the interest rate sensitive segments of the economy. Although the "soft landing" that the Federal Reserve hopes to achieve is still a possibility, numerous uncertainties cloud the 2024 horizon. In short, we still cannot rule out a 2024 recession.

The U.S. Economy. The November report from the Institute for Supply Management continued to depict the U.S. economy as modestly negative. ISM's NEW ORDERS Index posted at -8, marginally better than October's -11, but still below the break-even point of +0. The PRODUCTION Index (a.k.a., Output) for ISM remained modestly negative at -1 up from -3. ISM's closely-watched ORDER BACKLOG Index edged lower to -21, down from -16. The NEW EXPORT ORDERS Index also eased to -8 from -1. After adding seasonal adjustments, ISM's composite index for November posted 46.7, unchanged from October.

A slightly less pessimistic view of the U.S. economy comes from the British-based economic consulting firm now called S&P Global. S&P's Composite PMI for November posted at 49.4, down marginally from the break-even point of 50.0 reported in October. However, the S&P's index of New Orders was lower for the sixth successive month, partially because of continued economic uncertainty and inventory liquidation. Chris Williamson, Chief Business Economist at S&P Global Market Intelligence, further commented:

> "U.S. manufacturers reported yet another tough month in November. Output barely rose as inflows of new work showed a renewed decline, hinting at little – if any – contribution to fourth quarter GDP from the goods-producing sector. Orders have in fact risen in only three of the past 18 months, reflecting a prolonged period of subdued post-pandemic demand, in turn linked to consumers switching their spending to services such as travel and recreation, and business customers reducing excess inventories which had been accumulated during the supply concerns of the pandemic. Encouragingly, there are some signs of the inventory cycle starting to turn, with producers of intermediate goods (inputs supplied to other firms) now reporting modest order book growth. U.S. producers nevertheless continue to focus on cost cutting by trimming headcounts, and have now taken the knife to payroll numbers for two consecutive months. Barring the early months of the pandemic, the survey has not seen such a back-to-back monthly fall in factory employment since 2009. The decline in employment could feed through to weaker consumer spending, but will also reduce wage bargaining power. Lower wage pressures, combined with a marked cooling of raw material input cost inflation, have already fed through to a lowering of average factory selling price inflation for goods to a rate below the average seen in the decade prior to the pandemic, the rate of increase dipping again in November to help further lower consumer price inflation in the months ahead."

<u>The World Economy</u>. Despite two wars disrupting the world economy, the J.P. Morgan Worldwide Manufacturing Index posted at 49.3 in November, up from 48.8 in our previous report but modestly below the neutral point of 50.0. It seems clear that the world economy is more resilient than might be expected. JPM's New Orders Index edged higher to 48.9 from 48.5. In a similar move, JPM's Output Index improved to 49.9 from 48.9. The PMI for Canada, our largest trading partner, eased to 47.7 from 48.6. The November PMI for Mexico, our second largest trading partner, improved slightly to 52.5 from 52.1. The PMI for China, our third largest trading partner, rose to 50.7, up from 49.5. Bennett Parrish, Global Economist at J.P. Morgan, further commented:

> "The November PMIs offer a glimmer of hope that global industry may have found a bottom at the start of 4Q23. The manufacturing output index rose 1-point to 49.9, more than reversing the October drop and tempering concerns that activity was sliding back into contraction. At this level, the output PMI is consistent with very soft growth in global manufacturing. A sizable increase in the European PMIs is encouraging given that the outlook in the region has been particularly weak. Asia – a bellwether for global industry – also saw a notable rise."

Turning to the Eurozone economy, the Hamburg Commercial Bank composite PMI posted at 44.2, up from October's 43.1. After seventeen months below the 50.0 break-even point, the Eurozone economy may finally be showing signs of bottoming out and recovering. Of course, the Ukrainian war has become a new paradigm in what some are calling "Cold War, Part Two." Germany, the largest economy in the group, posted a PMI of 42.6, the highest the index has been in six months. The PMIs for Greece and Ireland remain marginally positive, but all of the others PMIs remain significantly negative. Dr. Cyrus de la Rubia, Chief Economist at Hamburg Commercial Bank, further noted:

> "November has not been the prettiest, and this does not refer only to the weather but also to the situation in the manufacturing sector of the Eurozone. Output is still on the decline, and firms have trimmed their staff for a sixth straight month. Sure, almost all the sub-indices have perked up a bit. However, the improvements are mostly timid, lacking the dynamism needed to declare an upward trend. Could we take a glimmer of hope from new orders? The corresponding index, stagnant at more or less 39 points for a four-month stint, has finally made a move, reaching a six-month high. As one-month shifts demand caution, it is prudent to hold off on declaring this to be a trend until we see another month or two of upward movement. While the downturn is broadly based across the eurozone, dynamics differ among the top four economies of the currency union. Germany stands out as the single country where the fall in output is softening, while the others are experiencing a deepening of the crisis. In terms of new orders, Germany, France, Italy and Spain witnessed slowdowns in new order declines, but to varying degrees. These heterogeneous movements show that the recovery, which will kick in eventually next year in our view, might encounter some resistance in gaining momentum. A crucial barometer for the recovery's onset will likely be a more synchronized upward movement in the economies PMI indexes, leading to a self-reinforcing reciprocal push among countries."

<u>Automotive</u>. The UAW strike is now past, and the production bottlenecks that have plagued the industry for most of the past three years have moderated. All of this is good news for our West Michigan automotive parts suppliers. The November sales reported by *Automotive News* estimates that the year-over-year SAAR (Seasonally Adjusted Annualized Rate) posted at 15.4 million units, up nicely from 14.4 million units in 2022. For the firms that still report monthly, year-over-year sales for November are up a significant 14.1 percent. Looking at November sales for the major brands, Honda, hardest hit by the chip shortage, gained 33.2 percent, Mazda, 21.0 percent, Subaru, 14.9 percent, Hyundai-Kia, 13.1 percent, Ford, 7.0 percent, and Toyota, 3.8 percent. Randy Parker, CEO of Hyundai Motor America commented:

> "Pent-up retail demand remains strong, even in the face of affordability challenges. Targeted incentives, such as 0 percent financing for 60 months on the Santa Fe and Tucson crossovers, are delivering results. Crossovers and utility vehicles represented a record 82 percent of sales at Hyundai last month."

<u>West Michigan Unemployment</u>. Unemployment is always a "laggard" statistic, so it is no surprise that the employment situation in West Michigan appears to be remains relatively stable. However, at -5, the West Michigan EMPLOYMENT Index has turned negative for the second successive month since the end of the pandemic. For November, 20 percent of this month's survey respondents reported staff reductions, about the same as the 21 percent reported last month. In about three months, because of the economic "laggard" effect, we can expect our local unemployment numbers to begin to edge higher. For now, the Michigan Department of Technology, Management & Budget (DTMB) reported that the October (latest month available) seasonally adjusted year-over-year unemployment rate for Michigan edged up to 4.1 percent from 3.9 percent. For West Michigan, the October unemployment rate (unadjusted) for Kalamazoo County posted at 4.2 percent, Kent County, 3.2 percent, and Calhoun County, 4.2 percent. At 3.1 percent, Ottawa County reported the lowest county unemployment rate for West Michigan.

Business and Consumer Confidence. After three straight losses, the November Conference Board Consumer Confidence Index increased to 102.0 (1985=100), up from 99.1 in October. However, the November University of Michigan Index of Consumer Sentiment backtracked to 61.3 from 63.8. The survey author noted that more-favorable current assessments and expectations of personal finances were offset by a notable deterioration in expected business conditions. For our local survey, the SHORT-TERM BUSINESS OUTLOOK Index for November, which asks local firms about their business perceptions for the next three to six months, edged back to positive at +3, up from -4. The LONG-TERM BUSINESS OUTLOOK Index, which queries the perceptions for the next three to five years, upticked nicely to +36 from +28.

Industrial Inflation. Our West Michigan index of PRICES for November came in at -2, modestly below the break-even point of +0. At the national level, the November ISM index of PRICES posted at +0, up considerably from the October reading of -9. Despite ample supply for some products, the rising cost of doing business throughout the world appears to have halted further price reductions. Although the supply situation for higher-end semiconductors and other miscellaneous electronics remains tight, prices for most big-ticket commodity prices continue to fall or stabilize. At 0.7, the S&P's Global Supply Shortage Index has fallen to its lowest level in 46 months. Commenting on the latest price trends, Annabel Fiddes, Economic Indices Associate Director at S&P Global Market Intelligence added:

> "Pressure on global manufacturing supply chains continued to ease in November, with reports of supplier shortages running at the lowest since just before the onset of the pandemic in January 2020. Transport has been one key area where shortages have lessened notably over the course of 2023. The improvement in the availability of commodities and weaker demand has helped to keep a lid on cost pressures, with global commodity prices broadly stable for the second straight month. A number of metals, along with chemicals and oil, were all reported as having fallen in price, but reports of price increases for semiconductors and electrical items picked up in the latest survey period."

Consumer Inflation. On November 14, the U.S. Burean of Labor Statistics reported that the Consumer Price Index for October came in at 3.2 percent, unchanged from September. Excluding the more volatile components of food and energy, the "core" October CPI posted at 4.0 percent. In confirmation. the November 30 Bureau of Economic Analysis press release of the October Personal Consumption Index posted at 3.0 percent, down from 3.5 in September. Excluding food and energy, the index came in at 3.5 percent, down from 3.7. Hence, both measures of inflation depict inflation continuing to slow. However, the press releases for both indices continued to stress that the "shelter" component of the index, also known as rent or rent equivalent, continues to be the main component keeping the indices from easily declining to the 2.0 percent target of the Federal Reserve. Barring a recession, the current inflation rate of 3.0 percent or so may be with us for at least the next 12 months or so.

GDP. On November 29, the Bureau of Economic Analysis (BEA) surprised the economic community with an announcement that the third quarter GDP grew at a rate of 5.2 percent, up from last month's preliminary estimate of 4.9 percent. Given last month's unexpectedly high "first estimate," many analysts had expected a downward revision. However, another similar economic measure, GDI (gross domestic income), posted at 1.5 percent. Both indices should come out the close to the same, but because of data collection methods, there is always at least some variation. Several reputable economists have raised concert that the gap between the two indices hasn't been this large since the eve of the Great Recession in 2007.

Other economists are now turning their attention to the estimates for growth in the fourth quarter of 2024. The December 1 report from the Atlanta Federal Reserve's GDPNow model forecasts a fourth quarter growth rate of only 1.2 percent, which is identical to the estimate posted a month earlier. The average for the Blue Chip GDP Realtime model currently stands at 1.1 percent. The Conference Board also expects a GDP of 1.1-1.3 percent for the fourth quarter but forecasts a shallow recession to shroud the first two quarters of 2024. J.P. Morgan erroneously forecast at recession for "late in 2023," but has now decided that the recession will not begin until "late in 2024." Just as previous months, reputable economic institutions are posting an unusually wide range of forecasts for the remainder of 2023 and all of 2024.

Looking Forward. Yes, the economy will continue to decelerate going into 2024. It remains obvious that the higher interest rates imposed by the Federal Reserve will continue to impact the cost of borrowing at all levels of the economy. Many commercial construction projects have already been shelved, and higher corporate bond rates have limited expansion for many firms in the S&P 500. The interest rate that commercial banks charge their most creditworthy corporate customers, generally called the "prime rate," now stands at 8.5 percent. As of December 5, the current average interest rate for a 30-year mortgage computed by Bankrate stands at 7.53 percent. According to Lendingtree, the average interest rate for all new credit cards has risen to 24.56 percent, with some cards now charging as high at 32-35 percent. According to Edmonds, the APR for new cars and trucks has now risen to 7.4 percent, up from numerous zero percent offers from the past ten years or so. All of these higher rates for all types of loans HAVE YET to take a significant bite out of the economy. As we move into the 2024 spring and summer months, the impact will become much more obvious.

Will these higher rates, along with the ongoing geopolitical uncertainties, lead to a recession in 2024? The top forecasters are widely dispersed. Bank of America, UCLA economists, Comerica Bank, Atlanta Federal Reserve all say that there will be no 2024 recession, although the economy will slow. Many other financial institutions are posting a recession probability, the highest of which is the Conference Board at 80 percent, followed by Bloomberg at 70 percent, Bankrate at 46 percent, Moody's at, 33 percent, and Goldman Sachs at 15 percent. All of these forecasts are from highly trained economists, all of which are having a difficult time balancing the numerous uncertainties that 2024 will bestow.

November 2023 Survey Statistics

	UP	SAME	DOWN	N/A	Nov. Index	Oct. Index	Sept. Index	25 Year Average
Sales (New Orders)	24%	42%	34%	0%	- 10	-13	- 9	+14
Production (Gross Output)	20%	46%	24%	10%	- 4	- 4	- 5	+14
Employment	15%	63%	20%	2%	- 5	-10	+ 0	+ 8
Purchases	22%	44%	34%	0%	-12	-17	-22	+ 7
Prices Paid (major commodities)	15%	66%	17%	2%	- 2	-14	- 5	+15
Lead Times (from suppliers)	7%	76%	15%	2%	- 8	-17	- 13	+11
Purchased Materials Inv. (Raw materials & supplies)	17%	49%	27%	7%	-10	- 6	- 6	- 4
Finished Goods Inventory	15%	48%	32%	5%	- 7	+ 2	-17	- 8
Short Term Business Outlook (Next 3-6 months)	27%	49%	24%	0%	+ 3	- 4	-15	-
Long Term Business Outlook (Next 3-5 years)	41%	52%	5%	2%	+36	+28	+15	-

Items in short supply:

PoQuarry tile, domestic castings, steel castings, some steel, construction related items, replacement parts, specialty garments, nitronic stainless steel, sprockets, controls and hoppers, some aluminum.

Prices on the UP side:

Fuel, natural gas, benzene, certain chemicals, raw paper stock, nitronic stainless steel, steel, repair parts, beef, pork, dairy products.

Prices on the DOWN side:

Aluminum*, steel*, PA6, ABS, and HDPE plastics, poultry, seasonal produce, fuel, transportation, international shipping containers, machine tools, copper.

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

Latest Unemployment Reports:

(Except as noted, data are NOT seasonally adjusted)

	Oct. 2023	Oct. 2022	Aug. 2009	20-Year Low
State of Michigan (Sept.)	4.1%	4.4%	14.6%	3.2%
State of Michigan (Unadj.)	4.2%	3.7%	14.1%	2.9%
Kent County	3.2%	3.2%	11.9%	2.1%
Kalamazoo County	3.7%	3.7%	11.1%	2.1%
Calhoun County	4.2%	4.3%	12.8%	2.7%
Ottawa County	3.1%	3.1%	13.3%	1.8%
Barry County	3.2%	3.4%	10.9%	2.2%
Kalamazoo City	4.2%	4.2%	15.2%	3.2%
Portage City	3.4%	3.4%	8.7%	1.3%
Grand Rapids City	4.3%	4.3%	16.1%	3.0%
Kentwood City	3.0%	3.0%	10.7%	1.4%
Plainfield Twp.	2.4%	2.4%	8.0%	1.4%
U.S. Official Rate (Oct.)	3.9%	3.7%	9.6%	3.5%
U.S. Rate (Unadjusted)	3.6%	3.4%	9.6%	3.4%
U.S. U-6 Rate (Oct.)**	7.2%	6.7%	22.9%	6.7%

***U-6 for Michigan = 7.1% for Q4 2022 thru Q3 2023*

NOVEMBER COMMENTS FROM SURVEY PARTICIPANTS

"Holiday seasons are slow for most people involved in the remodeling world."

"We expect to finish the year exactly flat with a strong outlook going into next year."

"Business looks very slow for the next several months."

"This is our slow season, and this month is trending at or slightly below expectations."

"Business is steady."

"Glad the UAW strike is about over so we can get back to selling our products!"

"We're still having trouble finding qualified machine builders and manufacturing leaders."

"We've had very sluggish sales through mid-November. Office Furniture and Marine are soft, but that's nothing new. Is it a blip or the start of a trend? Too soon to tell."

"Sales have ticked up a little bit. Inventory still too high, so we're cutting back on purchases. Lead times for bar stock from mills running over 1 year for a lot of materials."

"Pricing for 2024 remains on hold at the moment, although there are indicators that pricing should decrease for 2024. Forecasts are low across the board. Lead times continue to fall."

"Avoiding a long-term auto strike saved our organization a lot of pain."

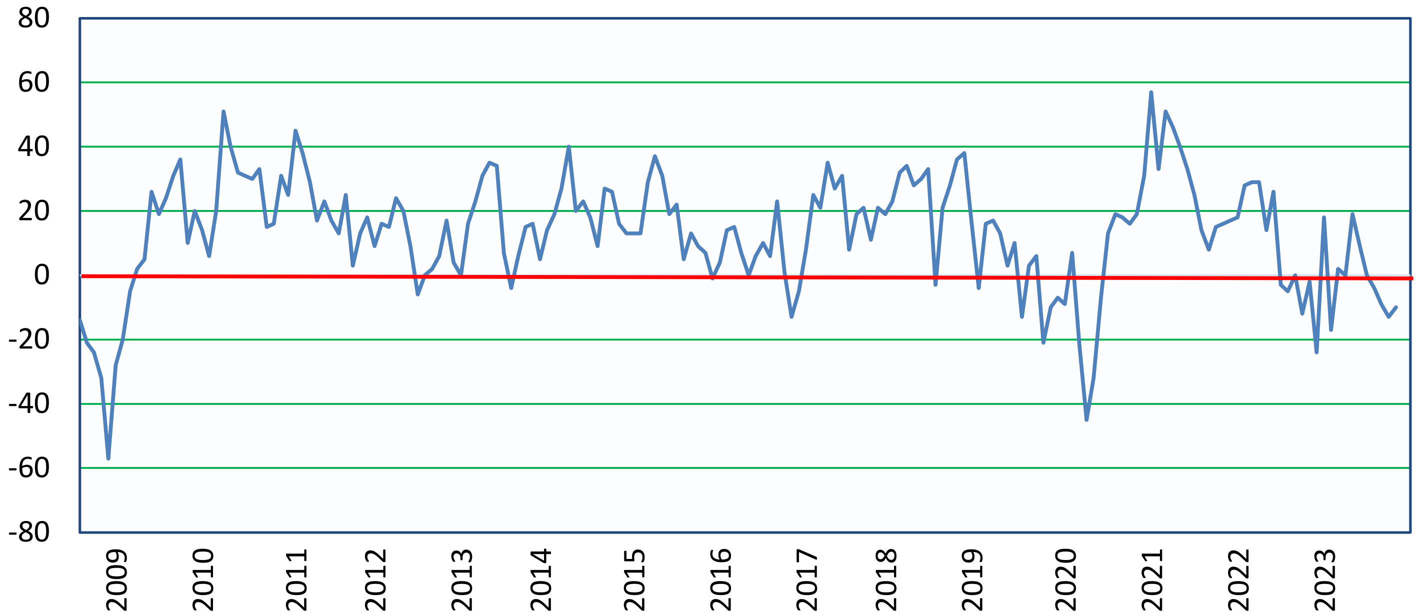
"We're holding steady and hitting targets, but not much more than this which is still a win. The "return to office" is still in transition but seems to be helping the office furniture industry."

"Our market is softening."

"Prices are leveling in machine tools. The rise in Interest rates has slowed purchases."

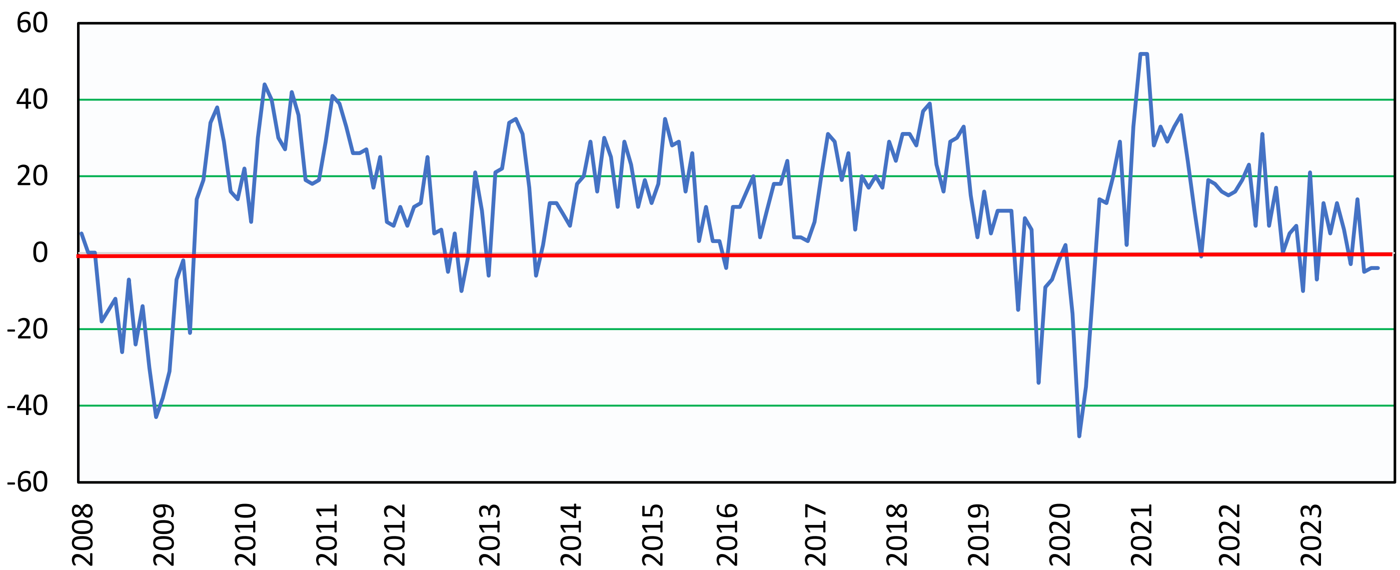
West Michigan Index of New Orders: 2008-2023

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.



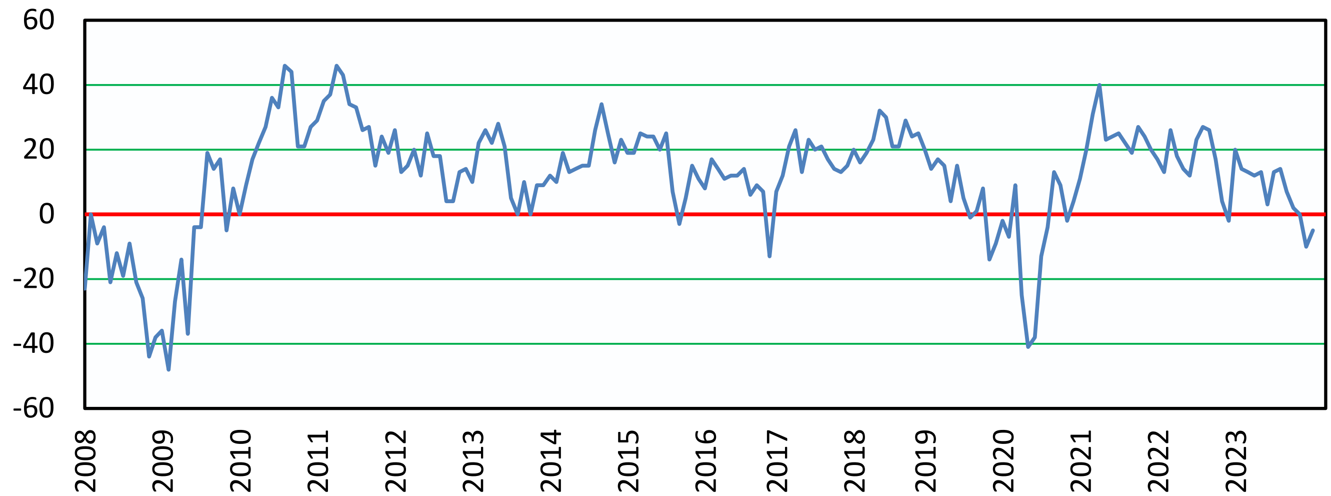
West Michigan Index of Production (Output): 2008-2023

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.