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West Michigan Current Business Trends

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West Michigan Economy Hits a Soft Spot

Key Take-Aways from January 2024 Statistics:

- **Local Industrial Economy Has Softened, But Not Collapsed**
- **National and International Economies Have Strengthened**
- **Local and National Business and Consumer Optimism Upticks**

	Jan.	Dec.
NEW ORDERS Index (business improvement)	-26	-14
PRODUCTION Index (aka "output")	- 20	- 11
EMPLOYMENT Index	- 7	- 5
LEAD TIMES Index	- 7	- 9

Key Participant Comments for January:

"January was noticeably slow."

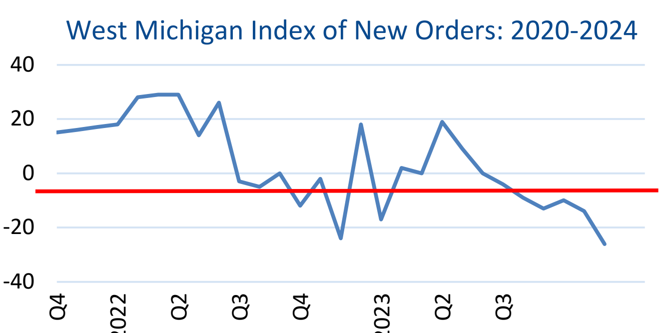
"We had a surprisingly strong December, and January is continuing that trend."

"Markets continue to be soft. However, we are riding the automotive wave by being on the proper platforms."

"The Red Sea situation has the potential to be disruptive (at least short term) and is being watched closely."

"Machine tool prices are dropping as finished goods inventories grow."

The Local Economy. Except for West Michigan, the January 2024 economic news is positive. Both January surveys of the U.S. economy from ISM and S&P are much more positive, and the mood of the American consumer has improved significantly. Despite two wars still far from resolved, the international economy has returned to break-even. Unfortunately, the West Michigan economy appears to have hit a soft spot. NEW ORDERS, our index of business improvement, fell to -26 from December's -14. The PRODUCTION Index, which some economists label as "output," slid to -20 from -11. The index of PURCHASES, which measures activity in purchasing offices, remained virtually unchanged at -14. The 2024



economy began the year with most of the bottlenecks in the supply chains cleared and most commodity prices back to normal. Many economic indicators are rising, and fears of a recession are now fading. Contrary to the aforementioned sagging numbers, both of our survey questions regarding short and long-term confidence rose for January. Hence, it does not appear that our West Michigan survey respondents are anticipating a recession anytime soon.

Although the West Michigan economy has obviously softened, our statistics appear more like a slowdown than a recession. Business conditions for our automotive part producers have slowed, especially for a few local firms that were supporting the new electric vehicles that are not selling as promised. In addition, auto sales are generally returning to normal, and the scarcity of most models has been reduced along with much of the pent-up demand. All of this has resulted in competition among the auto parts producers beginning to tighten. A similar slowing is also affecting the office furniture industry, which is gradually recovering as back-to-office mandates increase the demand for furniture upgrades. However, new office construction, a market segment which usually requires new office furniture, is being restrained by the unexpected surge in interest rates. The vacancy rates in existing office space remain high in many areas of the country, and some existing projects have been cancelled because of financial troubles in the commercial office industry brought on by higher interest rates.

The U.S. Economy. Although one month does not make a trend, the January report from the Institute for Supply Management posted a reversal from the previous months that depicted the U.S. economy drifting lower every month. Although still modestly negative, ISM's

NEW ORDERS Index came in at -3, up from December's -11. The PRODUCTION Index for January also edged up to -5 from -8. ISM's closely-watched ORDER BACKLOG Index remained virtually unchanged at -11, but still below the break-even point of +0. Unfortunately, the NEW EXPORT ORDERS Index fell from +0 to -10. After adding seasonal adjustments, ISM's composite index for January posted at 49.1, up significantly from December's 47.1. Again, one month is not a trend, but the numbers are at least heading in a positive direction.

An even more optimistic view of the U.S. economy comes from the British-based economic consulting firm now called S&P Global. S&P's Composite PMI posted positive at 50.7, up significantly from December's report of 47.9, and above the break-even threshold of 50.0. The pace of S&P's index of New Orders was the best since May 2022. Chris Williamson, Chief Business Economist at S&P Global Market Intelligence, further commented:

> "U.S. manufacturers have started the year with a spring in their step. Business optimism about the year ahead has surged to its highest since early 2022 thanks to a jump in demand. New orders are rising at a pace not seen for over a year and a half, improving especially sharply for consumer goods as households benefit from signs of an easing in inflation and looser financial conditions. Factories are also showing signs of restocking, with some firms buying more inputs to support higher production in the coming months. Payroll numbers are also rising again as firms seek to build extra operating capacity, boding well for the upturn to gain further strength as we head through the first quarter. The brighter news is tempered by signs of factory costs rising on the back of supply delays, with costlier deliveries often linked to adverse weather and recent disruptions to global shipping. These higher costs are feeding through to increased prices charged for goods by factories, which rose in January at the fastest pace since last April. Some renewed upward pressure on consumer prices could therefore appear in the months ahead if these supply-linked inflationary trends persist."

The World Economy. For January, the J.P. Morgan Worldwide Manufacturing Index returned to the statistical break-even point of 50.0, up from December's 49.0. JPM's Output Index came in at 50.3, up from 49.4. The JPM New Orders index rose to 49.8, up from 48.8. The PMI for Canada, our largest trading partner, recovered significantly to 48.3 from the survey's eight month low of 45.5. The January PMI for Mexico, our second largest trading partner, remained marginally positive but eased to 50.2 from 52.0. The PMI for China, our third biggest trading partner, remained unchanged at 50.8. The Chinese survey has now been positive for three successive months, which is the best the index has been for the past 30 months. Bennett Parrish, Global Economist at J.P. Morgan, further commented:

> "The global manufacturing output PMI rose 0.9-pt to an eight-month high of 50.3 in January. After global manufacturing lost some steam into year-end, today's news provides a glimmer of hope that momentum is improving again. The PMI subcomponents tracking new orders, future activity and employment also made advances, further raising optimism that fuller recovery could be established during the coming months. The impact of disruptions to Red Sea shipping routes on delivery delays and prices seems minimal thus far, at least at the global level."

Turning to the Eurozone, the January composite PMI compiled by the Hamburg Commercial Bank registered at a ten month high of 46.8, up from 44.4. Of the major Eurozone economies, only the PMI for Greece came in positive at 54.7. The 45.5 PMI for Germany, the largest economy in composite calculation, remains negative but rose from 43.3. Dr. Cyrus de la Rubia, Chief Economist at Hamburg Commercial Bank, further noted: continues

> "Let's face it, there is a real chance that the manufacturing sector's year-long recession in the Eurozone could stretch into the first quarter of this year. Even though the PMI is higher than it was at the end of last year, it is still not hitting the expansion mark. However, ECB president Christine Lagarde is playing it cautiously optimistic. During the January 25th press conference, she said, 'If we try to look at PMI numbers in particular (...), we are seeing some encouraging numbers.' For those with a glass-half-full perspective, the set of manufacturing PMI indicators offers a dose of optimism. Firstly, the headline PMI has marked three consecutive months of increase, a trend mirrored in the forward-looking indicator for new orders. Secondly, there is a broad-based upward trend in sub-indicators, encompassing stock of purchases, backlogs of work, and output. Plus, more companies than during the last nine months are expecting higher output in the coming year. Despite these encouraging signs, a word of caution is in order, as both the headline index and the majority of sub-indices persist within the contraction zone. The Eurozone's road to recovery in the manufacturing sector may see its kickoff in the southern economies, potentially acting as a catalyst to lift the larger economies out of the recessionary quagmire. Meanwhile, in Germany, the order situation for investment goods and intermediate goods is trending upward, although it might still take a few months to witness growth."

Automotive. Partially because of inclement weather in many parts of the country, the year-over-year SAAR (Seasonally Adjusted Annualized Rate) for January 2024 posted at 14.8 million units, well below the 15.2 to 15.8 forecasts and down from December's 15.3 million level. For some of the nameplates that still report on a monthly basis, Honda gained 10.3 percent, Ford, 4.7 percent, and Toyota, 23.3 percent. One of the January losers was Hyundai-Kia, down 7.3 percent. Adding together all of the firms that reported January sales, the industry gained a respectable 9.4 percent. Jeff Schuster, vice president of automotive research and analysis at GlobalData, commented:

> "We continue to expect 2024 to be a return to more normalized patterns of sales and pricing to stabilize, albeit at a higher-than-normal level. Growth in incentives and the eventual cut in interest rates should prove to be a catalyst for continued growth in 2024. There is no question the transition to EVs will be slower than many in the industry expected, but don't write off EVs in 2024, there will be 47 new BEVs on the market in 2024, accounting for 10% of the total volume."

West Michigan Unemployment. According to the January 25 monthly report from the Michigan Department of Technology, Management & Budget (DTMB), Michigan's December (latest month available) seasonally adjusted year-over-year unemployment rate remained unchanged at 4.3 percent. For West Michigan, Ottawa County posted a December unemployment rate of 2.7 percent, followed closely by Kent County at 2.8, and both Allegan and Barry Counties at 3.2 percent. For our West Michigan monthly survey, the West Michigan Index of EMPLOYMENT edged lower to -7 from -5. Even though the unemployment rates reported for most West Michigan counties by the DTMB continue to fall, staff reductions were reported by 20 percent of the survey respondents. For the first month in almost three years, none of our survey respondents mentioned problems with filling open positions. Of course, 13 percent of our January respondents did add staff, so there are still job openings, but not as many as there were. However, we can expect our local employment statistics from DTMB to modestly soften in coming months.

Business and Consumer Confidence. As reported by numerous news organizations, the Conference Board's Consumer Confidence Index for January rose to 114.8 (1985=100), up from 108.0 in December. The reading was the highest in over three years. In a similar move, the January University of Michigan Index of Consumer Sentiment rose sharply to 79.0 from 69.7, the highest the index has posted since July 2021. For our West Michigan survey, the SHORT-TERM BUSINESS OUTLOOK Index for January, which asks local firms about their business perceptions for the next three to six months, posted at +7, up from a flat reading of +0. In a similar move, the LONG-TERM BUSINESS OUTLOOK Index, which queries the perceptions for the next three to five years, upticked to +47 from +42, the highest the index has been since 2018. From past experience, we know that neither business nor consumer confidence are 100 percent (or even 80 percent) reliable indicators of the future economy. The so-call "black swan" events tend to creep up on us. However, they DO indicate that neither consumers nor the business community expect a recession in the near future.

Industrial Inflation. After falling for the past eight months, the West Michigan January index of PRICES posted at +9, up sharply from +0. In confirmation of the trend, the January ISM index of PRICES bounced to +6, up sharply from -10. JPM's index of world prices edged modestly higher to 52.9 from 52.4. Although S&P's Global Price Pressure Index for January posted at a rather modest +0.1, it is the first the index has signaled rising prices in nine months. If the current trend continues for another month or two, there will be ample evidence that industrial inflation may be returning. The good news, of course, is that a pattern of rising prices tends to rule out an impending recession. Commenting on the latest price trends, Usamah Bhatti, Economist at S&P Global Market Intelligence, added:

> "The latest indicators signalled that commodity price and supply pressures remained subdued at the start of the year. Despite seeing upwards pressure for the first time since last April, the increase in commodity prices was only fractional. Of the ten commodities to see strengthening price pressures, electrical items and transport led the way, with the latter seeing the most reports of price rises since October 2022. This lines up with the latest Global Manufacturing PMI data pointing to higher global input prices that have been partially driven by shipping disruption in the Red Sea and Panama Canal. Supply chain pressures were also muted in January, with the latest reading picking up to a three-month high but remaining well below the levels seen in 2021 and 2022. Only three of the 20 monitored commodities saw reported shortfalls above the long-run trend, led by electrical items which rose to a four-month high."

Consumer Inflation. According to the January 11 press release from the Burean of Labor Statistics, the year-over-year "headline" Consumer Price Index for December posted at 3.4 percent, up from November's 3.1 percent. Excluding food and energy, the "core" CPI came in at 3.9 percent, down from November's 4.0 percent. Although the CPI is the most widely publicized index of consumer inflation, the Federal Reserve notes that they put more decision-making weight on the Personal Consumption Index, which is published by the Bureau of Economic Analysis. According to the BEA's January 26 report, the "headline" PCI index for December came in at 2.6 percent, unchanged from November. However, the core PCI, which excludes food and energy, fell to 2.9 percent from 3.2 percent. Various members of the Federal Reserve board have commented that recent interest rate hikes are working as they should, and that the Fed's target inflation rate of 2.0 percent is now getting closer. However, the text of both the BEA and BLS reports clearly note that the cost of housing or "shelter" contributed over half of the increase for <u>both</u> indices in January. Hence, the cost of housing, which includes the cost of rent or rent equivalent <u>must</u> come down in order to reach the Fed's 2.0 percent target. The December Rent Index from Zillow posted an increase of 3.33 percent, down considerably from the 15.64 percent report two years ago, and closer to the current rate of inflation. Better news comes from the monthly Rent Report Index from Rent Group, which notes that rents actually declined 2.09 percent in January. The rent index from Realtor.com posted a modest drop as well. Unfortunately, rental contracts tend to be a year or two in length, so it will take time for the stabilization of rents (and rent equivalates) to be reflected in the monthly CPI and PCI surveys.

GDP. According to the January 25 press release from the Bureau of Economic Analysis (BEA), the gross domestic product (GDP) increased at an annual rate of 3.3 percent in the fourth quarter of 2023. Although the BEA labels 3.3 percent as an "advance" estimate which may be subject to further revision, the report came in much stronger than nearly all of the major forecasts. Assuming that the Q4 advance estimate is nearly correct, the GDP for the entire year was up 3.10, fairly close to the long-term average. Almost none of the forecasts were correct, resulting in a bit of a black mark on the economics profession given that so many highly trained economists with huge support staffs could be so wrong. Hoping to be more accurate in 2024, analysts are now turning their attention to the estimates for growth in the 2024 first quarter. As of February 7, the Atlanta Federal Reserve's GDPNow model forecasts a 2024 first quarter growth rate of 4.2 percent. It is noteworthy that the Atlanta Fed's computer model has been the most accurate for many quarters. By contrast, the average growth rate for the Blue Chip GDP Realtime model forecasts a growth rate of only 1.2 percent. The Conference Board, having predicted recessions in numerous recent forecasts, now says that they are no longer forecasting a recession. However, "..., we do expect the consumer spending growth to cool and for overall GDP growth to slow to under 1% in Q2 and Q3 2024." The Paris-based Organization for Economic Growth and Development (OECD) forecasts a slow first quarter, but then expect the U.S. GDP to slide into a recession in the second quarter of 2024. In short, we still have no firm consensus of what lies ahead for the 2024 economy from presumably reliable economics forecasters.

Looking Forward. For the past two years, we have lived with the prediction of an impending recession. As we enter 2024, most of the forecasts are trending in the direction of a slower economy but no official recession. However, increasing turmoil in the geopolitical situation still leaves the door open for an unexpected event that could upset any forecast. The GDP model for the economy computed by the Atlanta Fed is in part more accurate because it includes the ISM survey in its computation. Much more variation in the economy relates to the health of the industrial economy than most economists give credit. With both of the major surveys of the U.S. industrial economy now returning to normal, the probability of a recession anytime soon is unlikely. Higher interest rates will continue to pinch the interest rate sensitive firms and markets for most of 2024, but the Federal Reserve now believes that this "pinch" has been sufficient to bring inflation under control. With 40 percent of the CPI driven by the cost of housing, inflation will drift lower very slowly throughout the year. If the Fed sticks to its goal of bringing inflation down to 2 percent, we cannot expect any kind of a rate cut for most of 2024. Furthermore, cutting rates too soon leaves the Fed with little "dry powder" when a recession finally occurs. In the post-war years, there have now been 11 recessions, which averages to one every six years. In short, we are kidding ourselves if we don't think there will never be another recession.

January 2024 Survey Statistics

	UP	SAME	DOWN	N/A	Jan. Index	Dec. Index	Nov. Index	25 Year Average
Sales (New Orders)	18%	38%	44%	0%	- 26	-14	- 10	+14
Production (Gross Output)	9%	55%	29%	7%	-20	-11	- 4	+14
Employment	13%	65%	20%	2%	- 7	- 5	- 5	+ 8
Purchases	13%	60%	27%	0%	-14	-15	-12	+ 7
Prices Paid (major commodities)	16%	77%	7%	0%	+ 9	+ 0	- 2	+15
Lead Times (from suppliers)	9%	75%	16%	2%	- 7	- 9	- 8	+11
Purchased Materials Inv. (Raw materials & supplies)	22%	55%	16%	7%	- 6	- 22	-10	- 4
Finished Goods Inventory	9%	67%	20%	4%	-11	-18	- 7	- 8
Short Term Business Outlook (Next 3-6 months)	27%	53%	20%	0%	+ 7	+ 0	+ 3	-
Long Term Business Outlook (Next 3-5 years)	51%	43%	4%	2%	+47	+42	+36	-

Items in short supply:

Some specialty chemicals, control engineers, hemp.

Prices on the UP side:

Steel, packaging paper, ocean freight, electronics, hydraulics, pneumatics, plastics, aluminum, some finishing services, polycarbonate, ABS, polyoils, hemp, packaging, polypropylene, some meats, some produce, domestic fuel.

Prices on the DOWN side:

Dairy, eggs, soft seating/cushions, PA6, ABS, PC, machine tool, domestic fuel, packaging paper, steel*.

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

Latest Unemployment Reports:

(Except as noted, data are NOT seasonally adjusted)

	Dec. 2023	Dec. 2022	Aug. 2009	20-Year Low
State of Michigan (Dec.)	4.3%	4.3%	14.6%	3.2%
State of Michigan (Unadj.)	3.5%	3.8%	14.1%	2.9%
Kent County	2.8%	3.0%	11.9%	2.1%
Kalamazoo County	3.2%	3.5%	11.1%	2.1%
Calhoun County	4.0%	4.3%	12.8%	2.7%
Ottawa County	2.7%	2.9%	13.3%	1.8%
Barry County	3.2%	3.7%	10.9%	2.2%
Kalamazoo City	4.0%	4.4%	15.2%	3.2%
Portage City	2.9%	3.2%	8.7%	1.3%
Grand Rapids City	3.7%	4.1%	16.1%	3.0%
Kentwood City	2.6%	2.9%	10.7%	1.4%
Plainfield Twp.	2.1%	2.3%	8.0%	1.4%
U.S. Official Rate (Dec.)	3.7%	3.7%	9.6%	3.5%
U.S. Rate (Unadjusted)	3.5%	3.3%	9.6%	3.4%
U.S. U-6 Rate (Jan.)**	7.2%	6.7%	22.9%	6.7%

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

JANUARY COMMENTS FROM SURVEY PARTICIPANTS

"January was noticeably slow."

"Markets continue to be soft. However, we are riding the automotive wave by being on the proper platforms."

"December sales proved to be strong, though short of budget. January is looking to be the same way. Container prices are spiking and appear to be a combination of seasonal/Lunar New Year activity plus disruption in the Red Sea. We are also watching the aftermath of the Taiwan elections and "noise" that might come from China as the results were not the preferred outcome of President Xi and Chinese government."

"We are hopeful for a great end of the first quarter!"

"We've had a slower start to the year than anticipated but still stronger than November/December."

"We had a surprisingly strong December, and January is continuing that trend."

"The Red Sea situation has the potential to be disruptive (at least short term) and is being watched closely."

"Our business outlook is still holding strong."

"We just had our first big weekend for snow, so we are at full force with fuel, salt, and sand purchases."

"Sales are sluggish, and we will struggle to make forecast this month. We continue to focus on inventory reduction."

"Sales are softer than plan. Backorder still good, but next few months will be a little light."

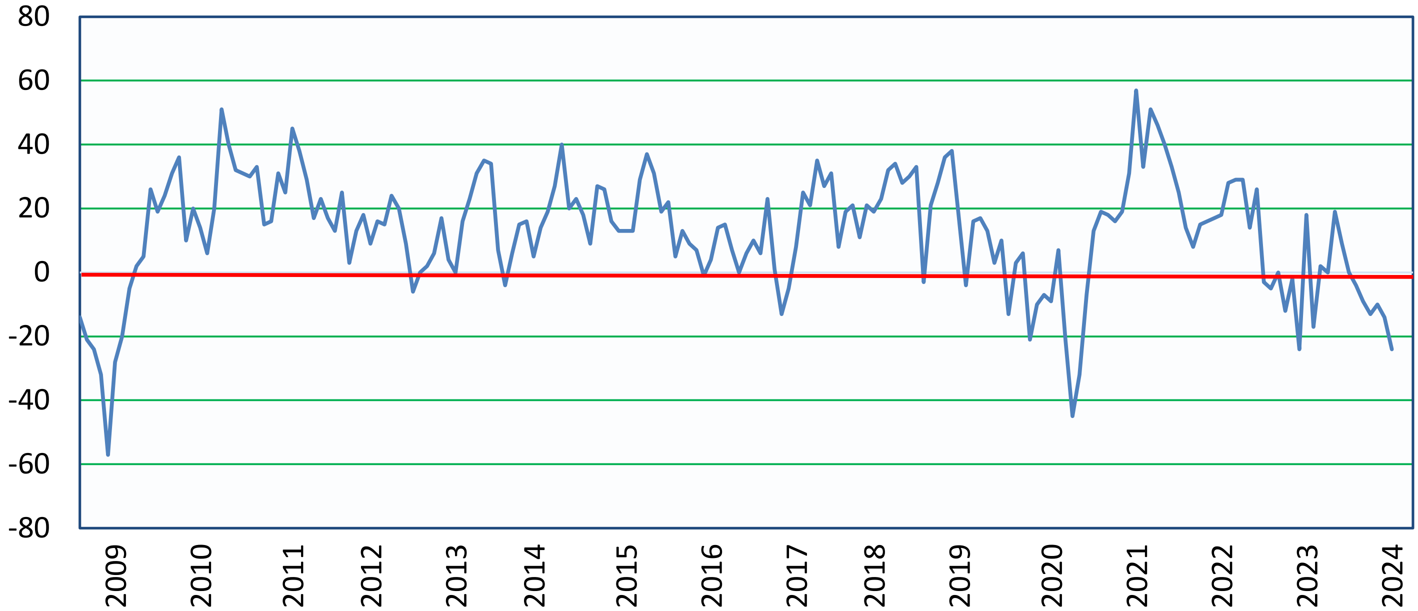
"Business is picking back up. It usually it gets a little slow around the Holiday Season."

"We're currently not experiencing any extreme part shortages. International freight (imports from Europe, China, Indonesia, Australia) is on the radar and could cause longer lead-times/delays."

"Machine tool prices are dropping as finished goods inventories grow."

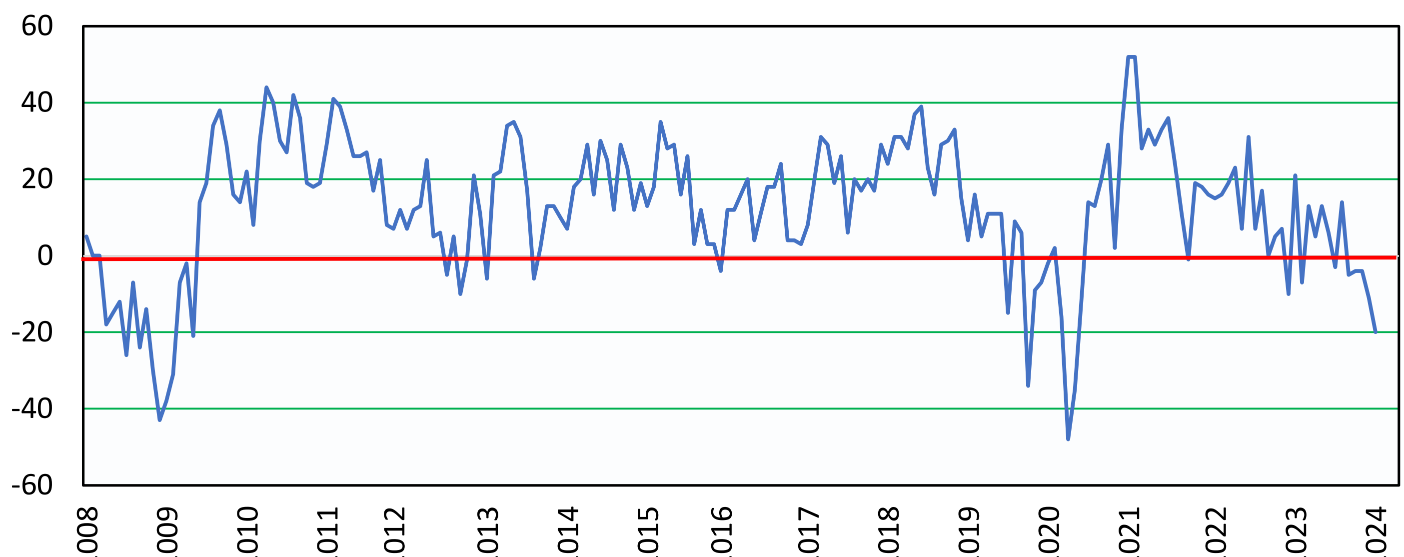
West Michigan Index of New Orders: 2008-2024

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.



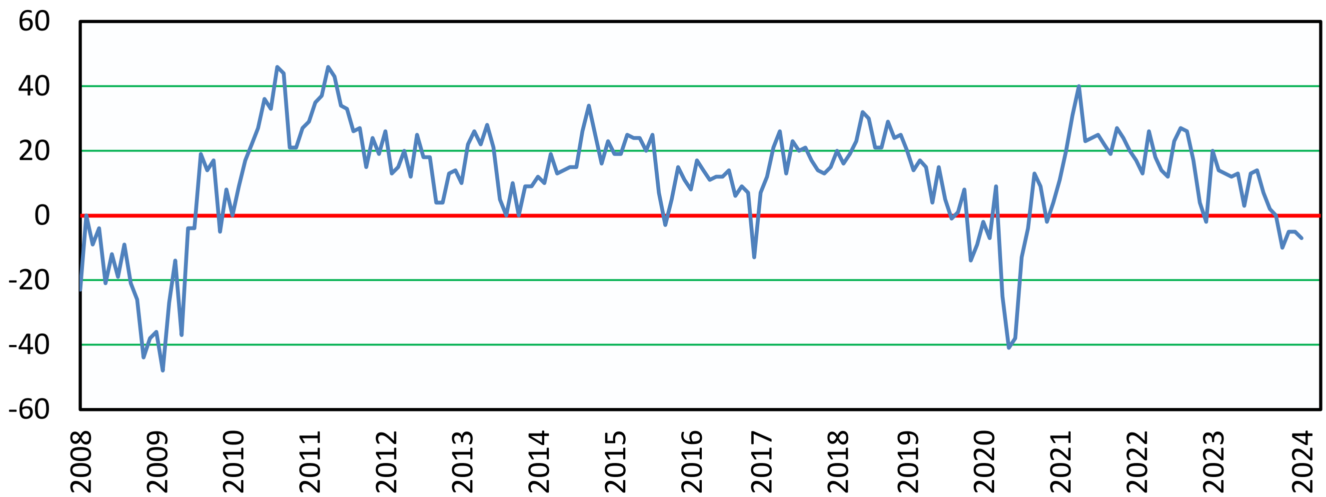
West Michigan Index of Production (Output): 2008-2024

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: 2008-2024

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: 2013-2024

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.