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West Michigan Current Business Trends

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POSITIVE GROWTH RETURNS

Key Take-Aways from June 2023 Statistics:

- **A West Michigan Industrial Economy Remains Positive**
- **National Industrial Economy Continues to Soften**
- **Survey Comments Remain Cautious**

	June	May
NEW ORDERS Index (business improvement)	+ 9	+19
PRODUCTION Index (aka "output")	+ 6	+13
EMPLOYMENT Index	+14	+13
LEAD TIMES Index	-17	- 2

Key Participant Comments for June:

"Lead times are improving significantly for various items, making it much easier to acquire. Prices have stabilized but are still higher than in the last couple of years."

"Business is still strong and we struggle filling night shift direct labor positions."

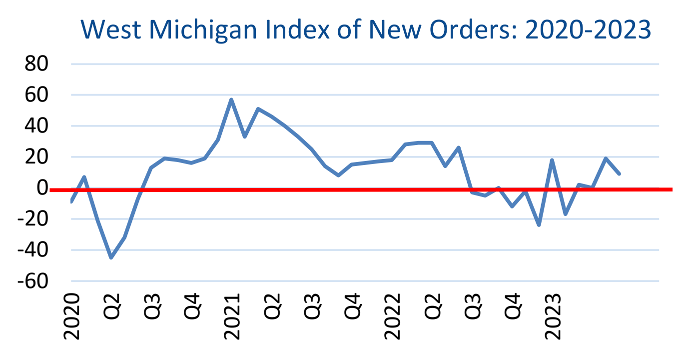
"Sales are down 20%, and the forecast for the next few months does not look any better."

"Electronics continue to be volatile on availability with allocation causing delays to our shipments."

"Business is excellent."

<u>The Local Economy</u>. The good news for West Michigan is that our June survey of business conditions continues to show no sign of a recession… at least yet. NEW ORDERS, our index of business improvement, remained positive but eased to +9 from May's +19. In a similar move, the June PRODUCTION Index, which some economists label as "output," eased to +6 from +13. However, the Index of PURCHASES, which measures activity in purchasing offices, fell significantly to -4 from May's +13. For West Michigan's cyclical industries, the automotive parts producers remain cautiously optimistic, although the pent-up demand for new vehicles may only last another year or so. Even though sales for the office furniture industry remain depressed by about 10-20%, the market has not collapsed. So far, the Grand Rapids office furniture manufacturers have not announced any major layoffs, and the layoffs that have been announced have related to out-of-state locations. Although the modest slowing of some sectors of our economy has allowed many firms to backfill job openings, a few firms continue to report problems filling open positions. With some firms slowing and others not seeing any obstacles going forward, June's comments from our survey panelists have become more widely mixed.

<u>The U.S. Economy</u>. At the national level, the July 1 press release from the Institute for Supply Management continues to depict the industrial economy as modestly contracting. ISM's June NEW ORDERS Index posted at -7, modestly better than May's -13, but still below the all-important break-even point of +0. The PRODUCTION (a.k.a., Output) Index for ISM dropped to -2 from +1. Another key ISM index, ORDER BACKLOG, modestly recovered to -23 from May's fifteen-year low of -27. June's NEW EXPORT ORDERS Index edged lower to -5 from +0. After statistical adjustments, ISM's Composite Manufacturing PMI posted at 46.0, down from May's 46.9.



A contrasting view of the U.S. industrial economy comes from S&P Global, the British-based international consulting firm that conducts a monthly survey of purchasing managers similar to ISM. The June S&P Composite PMI recorded a second noticeable drop to

46.3, down from May's 48.4, and considerably below April's 50.2. Key factors causing the recent weakness in the PMI are the survey's indices of Order Backlogs and Output. In addition, the S&P index of New Orders recorded the fastest decline since the onset of the pandemic. Although many of the S&P panelists had remained cautiously optimistic, the level of optimism appears to be fading. Chris Williamson, Chief Business Economist at S&P Global Market Intelligence, further commented:

"The health of the U.S. manufacturing sector took a sharp turn for the worse in June, adding to concerns over the economy potentially slipping into recession in the second half of the year. Leading the darkening picture was a severe drop in demand for goods, with new orders slumping at a rate among the steepest since the global financial crisis of 2009. Companies report that customers have become increasingly reticent to spend amid the rising cost of living, higher interest rates, growing concerns about the economic outlook and a switch in spending to services. Exacerbating the downturn has been a continued focus on inventory reduction as manufacturers, their suppliers and their customers all seek to cut warehouse stocks in the face of weakening demand. In this environment, pricing power is fading rapidly. Prices charged for inputs by suppliers are now falling at a rate not seen since 2009 barring only the early pandemic lockdown months. The big question is how long this service sector spending can be sustained in the face of headwinds from the cost of living and higher interest rates."

The World Economy. At 48.8, the J.P. Morgan Worldwide Manufacturing Index for June continues to drift further below the break-even point of 50.0. JPM's New Orders Index dropped to 48.0, and Output fell to 49.2. The PMI for Canada, our largest trading partner, fell from 49.0 in May to 48.8. The PMI for Mexico, our second biggest trading partner, remained modestly positive and rose from 50.5 in May to 50.9. The China Caixin PMI posted at 50.5, slightly below May's 50.9. However, the sharp recovery that China had expected from the pandemic reopening has yet to materialize. Bennett Parrish, Global Economist at J.P. Morgan, further commented:

"International trade flows remained especially weak, as new export business contracted for the sixteenth successive month. The rate of decline accelerated to the strongest in six months, with reductions signalled in the U.S., euro area, Japan, South Korea and Brazil (among others), while mainland China saw only a negligible increase. The current sustained weakness of the demand environment led to an increasingly cautious approach from manufacturers. Staffing levels were broadly unchanged during June, purchasing activity was cut back to the greatest extent since January and stocks were depleted as companies freed up funds. The dearth of demand also led to backlogs of work being reduced for the twelfth month in a row. Business optimism was less upbeat in June. Although manufacturers (on average) still forecast output to rise over the coming year, the overall degree of positivity dipped to its lowest since last November. Confidence was at a six-month low in the US, an eight-month low in mainland China and a seven-month low in the euro area (with France and Germany forecasting output to fall over the coming 12 months). Japan was one of the rare exceptions that saw sentiment strengthen."

Unfortunately, the European economy continues sink further into a recession. According to the report from the Hamburg Commercial Bank, the June PMI for the Eurozone posted at 43.4, down from 44.8. Significant declines in New Orders and Output were among the major negative pressures for June. Although beleaguered Greece managed to post a modestly positive PMI, the PMIs for all of the other major European countries were negative with many reaching 38-month lows. Commenting on the June data, Dr. Cyrus de la Rubia, Chief Economist at Hamburg Commercial Bank, further noted:

"Eurozone manufacturing production contracted for the third month in a row in June, according to the PMI output index, with the rate of decline accelerating and pointing to a worsening of factory conditions. New orders also fell at a faster rate, which further increases the likelihood that industrial production, which contracted by 0.9% month-on-month in the first quarter, according to Eurostat, will drop again in the second quarter. There is growing evidence that the capital-intensive industrial sector is reacting negatively to the ECB's (European Central Bank) interest rate hikes. Companies surveyed reduced their headcounts for the first time since January 2021, and purchasing activity declined at one of the worst rates on record. Cuts to sales prices for the second month in a row come as no surprise given the weakness in demand and rapid rate of cost deflation. The downturn is visible across the board geographically as all four of the biggest eurozone countries remained in contraction in June. In terms of new orders, the weakness in demand is most pronounced in Germany, followed by Italy and France. Delivery times are continuing to normalize, with the corresponding index signalling that since February, companies in the currency union are receiving their goods more quickly than in the previous month. While is seems as if companies do not complain so much anymore about delivery times, shortages of materials are still a lingering issue. According to DG ECFIN, for example, around 28% of companies in the eurozone complained of a shortage of materials in the second quarter – by 2019, this figure had averaged just under 7%."

Automotive. According to the July 9 edition of Automotive News, U.S. sales of cars and light trucks rose 13.3 percent in the first six months of 2023. The June SAAR (Seasonally Adjusted Annualized Rate) posted at 15.2 million units, up considerably from the June 2022 reading of 13.1 million units. Among the sales winners for the first half of 2023 were General Motors, up 18.5 percent, Ford, up 9.9 percent, Honda, up 24.8 percent, Hahyundi-Kia, up 18.3 percent, Subaru, up 15.3 percent, and VW, up 1.1 percent. Losers included Stellantis (Chrysler), down 1.3 percent, and Toyota, down a scant 0.7 percent. Ivan Drury, director of insights at Edmunds, further commented:

"This road to recovery for the industry has been a winding one. With many automakers committing to better aligning production and demand, we might be on the cusp of seeing what a new normal sales pace looks like compared to the pre-pandemic years, when bloated inventories and deep discounts shaped the industry."

Industrial Inflation. In our June survey, the West Michigan Index of PRICES fell from -2 to -17, the lowest the index has been since 2009. At the national level, the June ISM index of PRICES fell to -17 from -12. S&P's Commodity Price report noted that June industrial prices fell at the fastest pace since 2015. Of the 26 commodities tracked by S&P, 21 registered a reduction in price.

According to Usamah Bhatti at S&P Global Market Intelligence:

"Manufacturing supply chains showed sustained evidence of normalisation during June, albeit on the backdrop of depressed output and demand in the global manufacturing sector. Latest data indicated that reported commodity shortfalls were unchanged from June's recent low and broadly in line with the long-run average. Over half of the 20 monitored commodities signalled either a drop or the same extent of shortages as in June, including semiconductors, electricals and transport. Notably, firms saw transport shortfalls fall to the joint-lowest level since October 2020. At the same time, manufacturers reported a quicker decline in commodity prices in the latest survey period. The Price Pressures Index was at its lowest for seven-and-a-half years and signalled one of the sharpest reductions in commodity prices in the survey history. Within this, there were reportedly steep drops in the price of energy and chemical goods, particularly polyethylene. In fact, reports of energy price reductions were the second-highest in the survey history. Oil prices reportedly fell for eighth months running, with manufacturers signalling the strongest decrease since February."

West Michigan Unemployment. For the West Michigan industrial economy, the index of EMPLOYMENT continues to log in at double-digit positive. The June index edged up to +14 from +13, although 9% of the survey respondents did report staff reductions. It seems like an old story, but a few firms continue to report problems of finding enough qualified workers to fill their job openings. At the state level, the Michigan Department of Technology, Management & Budget (DTMB) reported that the May (latest month available) seasonally adjusted year-over-year unemployment rate for Michigan edged lower to 3.7 percent. For West Michigan, the unemployment rate for Kalamazoo County has now fallen to 3.0 percent, followed by Ottawa County at 3.3 percent, and Kent County, 3.4 percent. Just as last month, it is obvious that West Michigan unemployment continues to be lower than the rest of the state.

Business and Consumer Confidence. The Conference Board Consumer Confidence Index, revised on June 27, increased in June to 109.7 (1985=100), up nicely from 102.5 in May. In a similar move, the June University of Michigan Index of Consumer Sentiment upticked sharply to 64.4 from last month's reading of 59.2. Joanne Hsu, Surveys of Consumers Director, further commented, "Overall, this striking upswing reflects a recovery in attitudes generated by the early-month resolution of the debt ceiling crisis, along with more positive feelings over softening inflation. Views of their own personal financial situation were unchanged, however, as persistent high prices and expenses continued to weigh on consumers." For our local survey, the SHORT-TERM BUSINESS OUTLOOK Index for June, which asks local firms about their business perceptions for the next three to six months, retreated modestly to -4 from May's +7. The LONG-TERM BUSINESS OUTLOOK Index, which queries the perceptions for the next three to five years, posted at +27, down slightly from +33.

GDP. Like most statistics that are subject to revisions, it is the final revision that really counts. According to the June 29 press release from the Bureau of Economic Analysis (BEA), the final estimate of 2023 First Quarter GDP growth rose to 2.0 percent from last month's "revised" estimate of 1.3 percent. Looking ahead to the second quarter, we have our usual wide mix of forecasts. The July 6 press release from the Atlanta Federal Reserve's GDPNow model forecasts a growth rate of 2.1 percent, up from last month's estimate of 2.0 percent. Wolters Kluwer N.V.'s Blue Chip model for the second quarter has risen to 0.9, and the forecast model has continued to rise for the past four months. The Conference Board's second quarter forecast also continues to improve and now stands at 0.6, up from last month's -0.6. The Philadelphia Fed's survey of 38 economists remains unchanged at 1.0 percent for the second quarter.

Looking Forward. The pessimists continue to rant that it is only a matter of time before the next recession begins. From the industrial economy, they see sharply falling prices, declining inventories, weakening sales, and growing pessimism among many industrial firms. However, the optimists note that the unemployment rate remains remarkably low and that even the industries with slower sales are so far not collapsing. Hence, the possibility for the so-called soft landing is still very much in play. On the consumer side of the economy, the escalation of interest rates has put a severe crip in the affordability of housing, especially for the first-time home buyers. For home buyers who wish to move, trading a 3 percent mortgage for a 6 percent mortgage results in an average monthly payment increase of about $1,000 per month for houses of equal value. While prices in the industrial market are falling or stabilizing, many prices in the consumer market remain high. The money that many consumers saved during the pandemic is starting to run out, and the federal government has taken away the punch bowl that held trillions of dollars in stimulus money. From the recent business news, we know that there is at least some concern about the stability of some of our regional banks.

Bottom line: With all of these vectors going in different directions, it becomes increasingly difficult for ANYONE to accurately predict where the economy is going. A few reputable economists have predicted that the recession should have begun a few months ago, and they are now trying to figure out how they misjudged. Others say that the recession will begin later in the year. Another growing chorus of economists declares that we will experience a soft landing, wherein interest rate sensitive sectors of the economy will soften but the rest of the economy will remain strong enough to keep us from sliding into a recession.

June 2023 Survey Statistics

	UP	SAME	DOWN	N/A	June Index	May Index	Apr. Index	25 Year Average
Sales (New Orders)	30%	49%	21%	0%	+ 9	+19	+ 0	+14
Production (Gross Output)	21%	60%	15%	4%	+ 6	+13	+ 5	+14
Employment	23%	68%	9%	0%	+14	+13	+ 3	+ 8
Purchases	11%	74%	15%	0%	- 4	+13	+ 5	+ 7
Prices Paid (major commodities)	6%	67%	23%	4%	-17	- 2	+11	+15
Lead Times (from suppliers)	6%	71%	23%	0%	-17	- 2	+ 3	+11
Purchased Materials Inv. (Raw materials & supplies)	15%	55%	21%	9%	- 6	- 3	-19	- 4
Finished Goods Inventory	6%	55%	30%	9%	-24	-23	- 8	- 8
Short Term Business Outlook (Next 3-6 months)	15%	66%	19%	0%	- 4	+ 7	- 3	-
Long Term Business Outlook (Next 3-5 years)	36%	53%	9%	2%	+27	+33	+16	-

Items in short supply:

Phosphates, grades of sweeteners and/or derivatives, domestic aluminum, domestic castings, hydraulic components, computer chips, some electronic components, some electronic controls, garment materials, certain steel products, casters, safety relays, safety contactors, some PLCs, rotary sensors, older computer and electronic parts, some coil aluminum supply issues, anything from Ukraine.

Prices on the UP side:

Packaging materials, MRO items, some services, labor rates, brass forgings, ash lumber, chemical and petroleum based products, HDPE, electronics, gelatin, sweeteners, food driven raw material, anything sourced out of Europe.

Prices on the DOWN side:

Stainless steel, carbon steel, scrap steel, aluminum, aluminum coil, corrugated packaging, lubricants, tree pulp, surcharges, polypropylene, raw chemicals, some freight pricing, PA6, PP, PC, ABS.

Latest Unemployment Reports:

(Except as noted, data are NOT seasonally adjusted)

	May 2023	May 2022	Aug. 2009	20-Year Low
State of Michigan (May)	3.7%	4.0%	14.6%	3.2%
State of Michigan (Unadj.)	3.8%	4.1%	14.1%	2.9%
Kent County	3.4%	3.5%	11.9%	2.1%
Kalamazoo County	3.0%	3.0%	11.1%	2.1%
Calhoun County	4.6%	4.7%	12.8%	2.7%
Ottawa County	3.3%	3.4%	13.3%	1.8%
Barry County	3.6%	3.7%	10.9%	2.2%
Kalamazoo City	4.9%	5.0%	15.2%	3.2%
Portage City	3.6%	3.7%	8.7%	1.3%
Grand Rapids City	4.5%	4.7%	16.1%	3.0%
Kentwood City	3.2%	3.3%	10.7%	1.4%
Plainfield Twp.	2.6%	2.6%	8.0%	1.4%
U.S. Official Rate (May)	3.7%	3.6%	9.6%	3.5%
U.S. Rate (Unadjusted)	3.4%	3.4%	9.6%	3.4%
U.S. U-6 Rate (June.)**	6.9%	6.7%	22.9%	6.7%

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

JUNE COMMENTS FROM SURVEY PARTICIPANTS

"Electronics continue to be volatile on availability with allocation causing delays to our shipments."

"Price increases have mostly tapered."

"Freight prices are still up, not as high as they were but still higher than what we would consider normal."

"We are getting hit with 3 to 4% price increase on most things."

"Steel prices have come down slightly, but are still at a premium rate."

"Our terminal markets are currently much healthier than expected. Demand is very high compared to forecasts, and replacement orders continue to come in at regular intervals. So far, our supply chain has been able to keep up without too much disruption, however we have seen lead times from key material suppliers slip in June and expect them to move out another 20%+ in July. Our own lead times are beginning to move out. However, this appears to be happening with all our competitors as well, so we anticipate the next 3 to 5 months to be very strong."

"Q2 will bring us even further into a new norm as organizations start to dive deep into the numbers to re-establish foundations and reset to changing market demands. Reductions in pricing and inventory levels remain priority as well as emphasis of sales attainment against fiscal plans."

"We have continued concerns over future housing demand vs. housing costs and slower volume creating capacity in the market."

"Business is excellent."

"With the federal government keep talking recession, I believe it's starting to make people believe that it is happening more than it is and there are some businesses that are cutting back and spending less to try to preserve cash."

"It's going to be a strong month for us: the best of the year. It feels like it may be stable to slightly slower from here for the short/medium term. There's lots of uncertainty and lack of good forecasting."

"Sales are down 20%, and the forecast for the next few months does not look any better."

"Lead times are improving significantly for various items, making it much easier to acquire. Prices have stabilized but are still higher than in the last couple of years."

"Most supply chain related items are stabilizing (cost-wise). Lead times, generally, are coming down. Lead times related to services (fabricating / welding) are still a bit higher."

"Business is still strong and we struggle filling night shift direct labor positions."

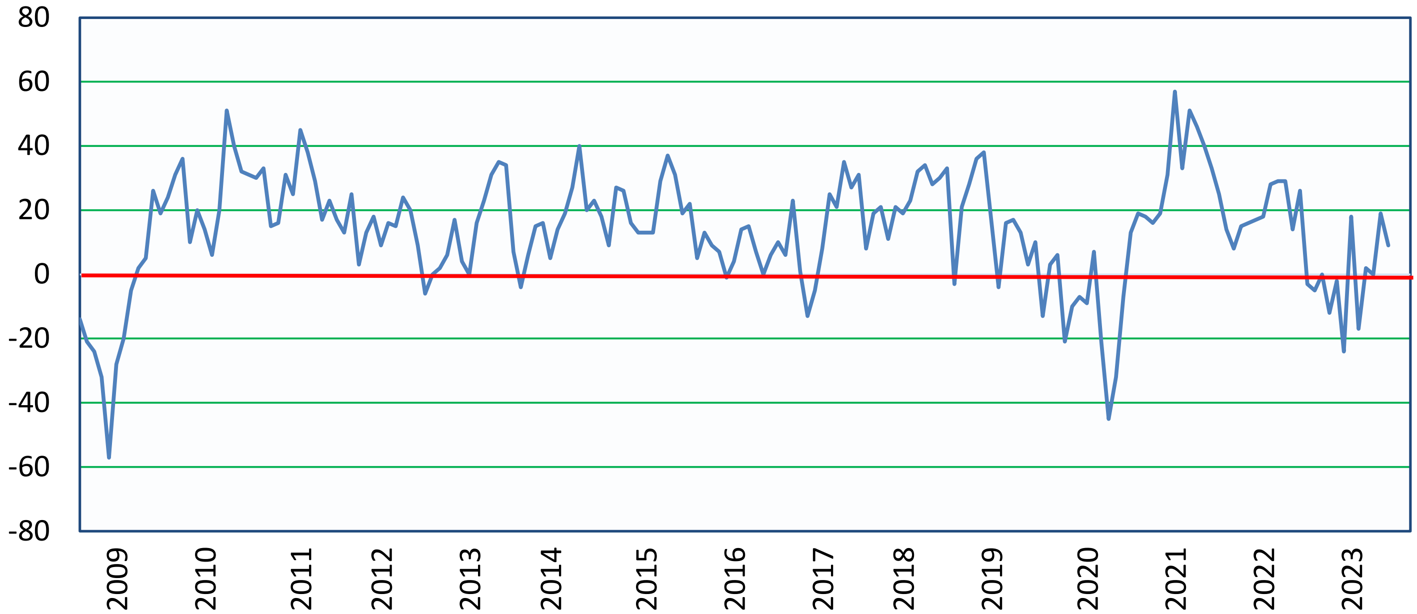
"Markets continue to be softer than planned, but we are hopeful that business starts to pick up again on the back half of the year."

"Sales are softer than last month. Capacity on shop floor now exceeds incoming orders. Inventory will start to rise if orders don't pick back up. We are going to dedicate as much of the open capacity to training as possible."

"Business is slow and expected to remain so for the foreseeable future."

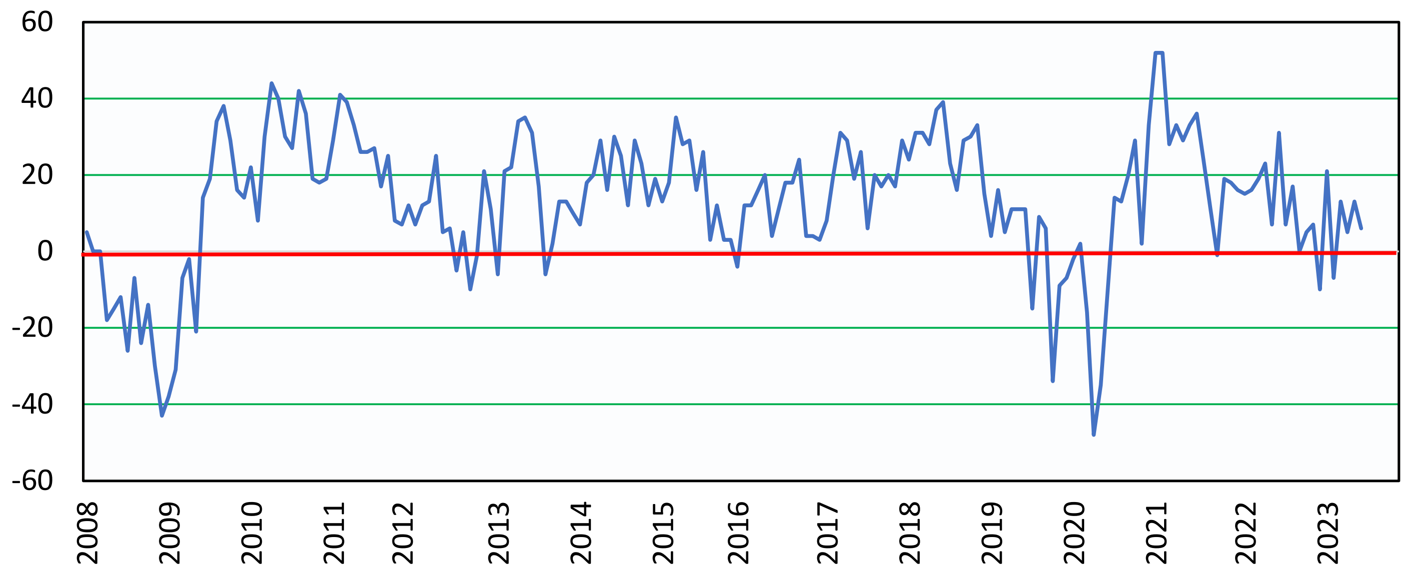
West Michigan Index of New Orders: 2008-2023

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.



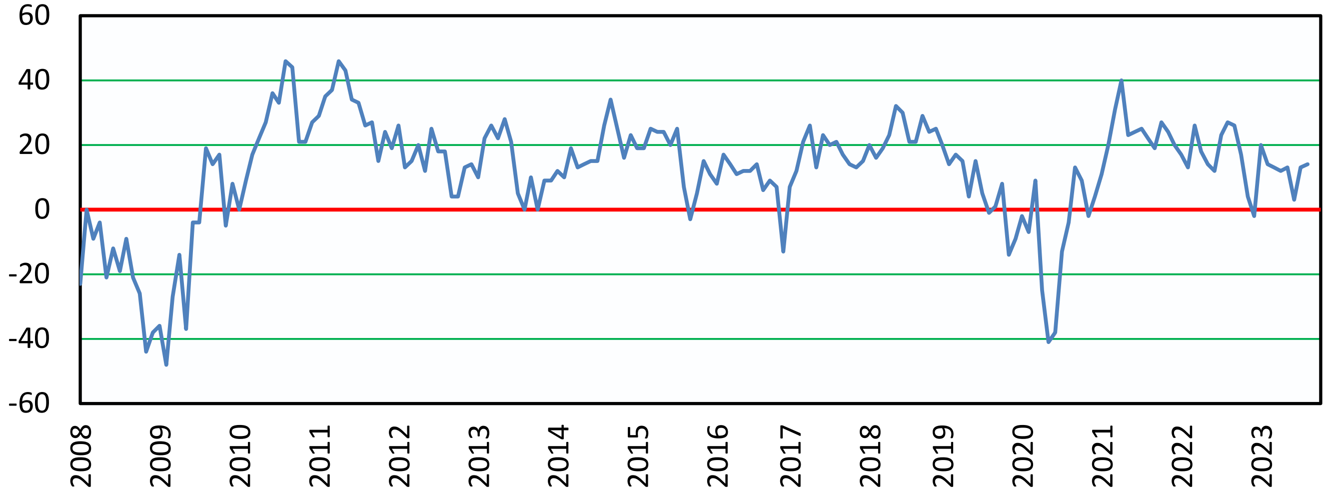
West Michigan Index of Production (Output): 2008-2023

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.