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Current Business Trends

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STILL ON SOLID FOOTING

So far, so good. According to the data collected in the last two weeks of June, NEW ORDERS, our closely-watched index of business improvement, edged up to +33 from +30. in a similar move, the West Michigan PRODUCTION index rose to +39 from +37. Activity in the purchasing offices, the index of PURCHASES, came in at +27, up nicely from +19. The comments from our survey participants remain positive, but many are justifiably concerned about an impending tariff war. With the economy now approaching full capacity, shortages are starting to appear in many places. Trucking and other logistics services are in short supply, and freight surcharges are adding unexpected new costs, which is hampering profitability. Many firms continue to be constrained by personnel shortages, and one firm has resorted to hiring untrained workers who "seem capable of learning." Michigan still has 80,000 jobs that can't be filled because of the scarcity of trained workers.

Individual industries. Initially, 2018 was expected to be another year of slow growth for the West Michigan economy. However, business conditions for our local auto parts suppliers have remained strong, and the local firms producing capital equipment are still benefitting from the recently-passed tax advantages for new capital investments. The office furniture industry, which arguably plateaued in 2017, is now receiving a new wave of sales because of the new tax incentives. It is the summer repair season, so many of our industrial distributors reported positive business conditions for June.

The U.S. Economy. The June survey report from the Institute for Supply Management, our parent organization, came in stronger than expected. NEW ORDERS, ISM's index of business expansion, rose modestly to +33 from +31. In a similar move, the PRODUCTION index nudged up to +28 from +27. The EMPLOYMENT index came in positive for the twenty-first successive month and edged higher to +18 from +16. ISM's overall index for June rose to 60.2 from May's 58.7, only six ticks from the recent short-term high of 60.8.

A contrasting view of the U.S. economy comes from the British consulting firm of IHS Markit.com. The firm's overall PMI for June registerd 55.4, down from 56.4 in May. The May report was fairly optimistic, but the tone of the June commentary was much more reserved:

> "The PMI for June rounds off the best quarter for manufacturing for almost four years, but also fires some warning shots about what lies ahead. As such, the second quarter could represent a peak in the production cycle. On the downside, new orders inflows were the weakest for seven months, with rising domestic demand countered by a drop in export sales for the first time since July of last year. Business optimism about the year ahead also fell to the lowest level since January, with survey respondents worried in particular about the potential impact of trade wars and tariffs."

The World Economy. The J. P. Morgan Monthly Global Manufacturing Report for May noted that the survey of 32 nations remains positive, although the overall index eased to 53.0 from 53.1, an 11-month low. JPM's NEW ORDERS index also eased slightly to 52.9 from 53.4. Six of the countries in the survey reported deteriorations in overall operating performance for June, namely Brazil, Denmark, Malaysia, Russia, South Korea, and Turkey. The Chinese PMI remains modestly positive, and the European countries as well as the U.S. are still moderately positive. The survey author further commented:

> "The upturn in the global manufacturing sector lost further momentum in June, as output and new order growth slowed and the rate of increase in new export business slipped closer to stagnation. Concerns about international trade were also a factor underlying a drop-off in business optimism to a 19-month low."

The IHS Markit's press release for the eurozone's manufacturing sector reported growth to be reasonably positive, despite hitting an 18-month low. Markit's overall index for June came in at 54.9, significantly below the record high of 61.1 reported last December. Given that the index is still well above the 50.0 break-even point, there is no immediate cause for concern. The Netherlands and Austria are currently the strongest eurozone performers, and even troubled Greece, Spain, and France remain modestly positive. Chris Williamson, Chief Business Economist at London-based IHS Markit, further noted:

> "Eurozone manufacturing reported its weakest expansion for 18 months in June, with risks clearly tilted towards output growth waning further in coming months. Production growth has weakened markedly since the end of last year, and new order inflows have slowed even more. Manufacturers may therefore need to rein in their production further to adjust to the recent downturn in order book growth unless demand revives. The survey reveals mounting worries from companies relating to the impact of tariffs and trade wars, suggesting firms are bracing themselves for the potential for further export losses. Not surprisingly, business expectations for future production deteriorated in June to the lowest since November 2015. At the same time there are signs that political uncertainty is also dampening business spirits, most evidently in Italy, which was consequently the second-worst performer of all countries surveyed in June ahead of France."

Local Unemployment. Michigan's May unemployment rate came in at 4.6 percent, according to the latest report from Michigan's Department of Technology, Management and Budget. Just like last month, the higher unemployment numbers in some localities as well as the U.S. are primarily the result of idle workers reentering the workforce. The local index of EMPLOYMENT for June remained strong at +30, well ahead of our 25-year average of +8. Of the 83 counties in Michigan, unemployment in Ottawa County is still the lowest at 2.7 percent. Unemployment for Kent County is not far behind at 2.9 percent.

National Unemployment. Despite the speed of modern technology, the U.S. unemployment report is always posted weeks ahead of the state and local reports, even though the same database is utilized. The June unemployment rate for the entire U.S. now stands at 4.0 percent, up from May's 3.8 percent. Just between May and June, about 100,000 more people found work. However, about 600,000 more people decided to return to the workforce, resulting in the overall unemployment percentage to rise. Comparing June 2017 to June 2018, total employment in the U.S. grew by 2,326,000 workers. This is clearly good news for the economy.

Automotive. Auto sales for June again grew at a moderate rate, telling our numerous local auto parts suppliers not to worry. The seasonally adjusted sales rate (SAAR) for June came in at 17.47 million, up sharply from June 2017's sale pace of 16.72 million and last month's 16.91 million rate. For the Detroit Three, Fiat-Chrysler gained 8.0 percent, primarily based on strong sales from Ram and Jeep. GM sales grew by an estimated 5.7 percent, fueled by a batch of incentives averaging a whopping $5,200 per vehicle. Ford's June increase was limited to 1.0 percent, primarily because of a 2.3 percent drop in fleet sales. Of the other major brands, Toyota added 3.6 percent, Honda gained 4.8 percent, Nissan grew 1.2 percent, and the troubled VW group netted a gain of 3.8 percent. According to Jeremy Acevedo, manager of industry analysis at Edmunds.com:

> "The U.S. market is virtually saturated. Add to that record-high vehicle prices, rising interest rates and historically high numbers of people who owe more than their cars are worth, and the stage is set for a market contraction."

Tariff Wars. An old adage notes that everyone loses in a war, so to be successful, it is necessary to make sure that the other party is losing faster than you. At some point, you hope the other party will call for a truce and negotiate a surrender to keep from losing more. Obviously, this "trade war" is just beginning, and so far, no one has lost very much of anything. As noted in past reports, commodities like steel are rising in price, but many steel prices are still below the lofty levels of just six years ago. The current economy is strong, so this may be the best time to try to negotiate more favorable treatment for American sellers. Unfortunately, it is the industrial BUYERS who must bear the rising prices and decreased availability. After months of threats, the actual tariffs are now being levied, and everyone is worried about what the impact will be. According to the rhetoric, both sides are digging in for a fight. Although we are frequently reminded that the trade war growing out of the Smoot-Hawley tariffs in the late 1920's was one of the causes of the Great Depression, many other economic factors were in play at that time as well. Hence, the Smoot-Hawley tariffs did not "cause" the Great Depression, but they did make it worse. Needless to say, there is no apparent end in sight to the current dispute(s), and economic analysts around the world are wondering if this trade war will usher in the end the current economic prosperity.

Industrial Inflation. The current inflation spiral still shows no sign of slowing. The prices for some key commodities like steel, aluminum, all grade of plastics, and corrugated containers have been rising in price for several months. In this month's "price Increase" report, metallic chemical and industrial textile appeared for the first time. Locally, our June index of PRICES remained steady at +49, well ahead of our 25-year average of +15. The West Michigan index of LEAD TIMES edged higher to +49 from +43, causing shortages, production delays, higher prices, and ulcers for some of our survey respondents. At the national level, ISM's index of PRICES eased modestly to +54 from +59. However, JPM's worldwide index of "Input Prices" index posted a sharp jump to 62.2, up from May's 60.7.

GDP. The third (and hopefully final) estimate of economic growth for the first quarter of 2018 came in at 2.0 percent, down two ticks from the second estimate. However, the current projections for the second quarter of 2018, which ended on June 30, continue grow more and more optimistic. In addition to the strong reports coming from the industrial sector, increased consumer spending because of the tax cuts are expected to give the GDP numbers a significant boost. Projections for the next two quarters are also strong, partially because the expansion of the industrial markets will continue to spill over into the consumer sector as time goes along. The panel of economists from the *Wall Street Journal* are still saying that the economy will continue to expand through 2019, leaving sometime in 2020 to be the most probable beginning of the next recession. It is worth repeating that all recessions have triggers, and some economist are now suggesting that it could be a trade war that ushers in a recession in late 2019 or early 2020.

Business Confidence. Although fear of a trade war continues to weigh heavily on the minds of our survey respondents, it is fortunate that last month's negative trend did not continue. The West Michigan index for the SHORT-TERM BUSINESS OUTLOOK for June, which asks local firms about the perception for the next three to six months, edged up nicely to +41 from +33. But the LONG-TERM BUSINESS OUTLOOK, which queries the perception for the next three to five years, recovered modestly to +31 from +27.

Summary. For the short term, the economy still has plenty of positive momentum. Barring a geo-political catastrophe, the positive impact of the recent tax cuts will keep the economy growing. Constraining factors include material and logistical shortages, rising prices, and the inability to hire more workers. Until our next report, watch (1) the GDP second quarter report from the Commerce Department, (2) the trade war rhetoric, (3) reports of the ACTUAL impact of higher tariffs, and (4) other economic statistics like unemployment, retail sales, and home sales which all tell us where the economy is going. Hopefully, wiser minds will prevail and we will begin to see signs of at least some trade issues being resolved.

JUNE COMMENTS FROM SURVEY PARTICIPANTS

"We have a slow period on the horizon (6-12mo) that will result in a workforce reduction. This will include the loss of some highly trained and skilled individuals that will be extremely difficult to replace when demand increases in about 12 months."

May was down from a VERY strong April. And now June is down from May. Overall, it will be a good quarter, but activity is down from where it started."

"Sales in automotive parts remain strong. We see no direct impacts from the 232 tariffs imposed on the EU, but the tariffs will have a impact on stainless steel pricing in the order of 18 to 25% over the next 2 quarters. There are still plenty of unknowns in the trade situation, however it has yet to change much of our strategy at this time."

"Our inventories are declining due to implementing lean initiatives."

"We are very busy and should continue to be very busy for the next few months."

"Our annual shutdown is over and we are back in operation producing cement."

"This month was similar to last month. Employment is up due to bringing in temporary student summer help."

"We're starting prep work for tariff increases and how to handle them."

"We need to have more sales intake to stem the low shipments we are experiencing."

"Tariffs on steel from Canada are impacting the pricing of cold headed product made in the U.S."

"Overall business volume remains very solid across all industrial segments we are involved in."

"We are seeing steadily rising prices for raw materials."

"It seems like the price for almost everything is on the rise. Also, it seems like we are taking a back seat to the auto Industry when it comes to lead times and part delivery."

"We're thriving in out neck of the woods. Business is as robust as I've ever seen it, and I wasn't born yesterday."

"Freight surcharges are very real and starting to really impact logistics costs, availability, and delivery timing."

"If you didn't set a strategy in 2016 for securing electronic components, it's going to be tough until 2020."

"This year's schedule is full, and we are now working on 2019."

"If Tier I's don't allow price increases to pass through we will have to quit shipping. We cannot absorb these increases in raw material."

"Machine tools consumption is up. Our lead times are up from the manufactures of machines."

"Late shipments are because of the increased orders, requested shorter lead time from customers, and difficulties finding and keeping quality production workers."

"We are still very busy but continue to have problems securing employees."

"Thank you for the detail in your unemployment information. It has impacted our business this year because new hires are NOT staying or able to perform the task they hired in to perform."

"Supplier lead-times continue to grow presenting material availability 'risk'."

"Tariffs will hit us in July. There are still no skilled candidates for open positions. We are still hiring inexperienced people that seem capable of learning."

JUNE 2018 Survey Statistics

	UP	SAME	DOWN	N/A	June Index	May Index	Apr. Index	25 Year Average
Sales (New Orders)	42%	48%	9%	1%	+33	+30	+28	+14
Production	44%	46%	5%	5%	+39	+37	+28	+14
Employment	35%	60%	5%		+30	+32	+23	+ 8
Purchases	36%	55%	9%		+27	+19	+34	+ 7
Prices Paid (major commod.)	49%	51%	0%		+49	+49	+59	+15
Lead Times (from suppliers)	51%	47%	2%		+49	+43	+39	+11
Purchased Materials Inv. (Raw materials & supplies)	35%	53%	7%	5%	+28	+28	+26	- 4
Finished Goods Inventory	13%	67%	13%	7%	- 1	- 1	+ 0	- 8
Short Term Business Outlook (Next 3-6 months)	46%	49%	5%		+41	+33	+35	-
Long Term Business Outlook (Next 3-5 years)	38%	56%	4%	5%	+31	+27	+40	-

Items in short supply: Semi-skilled and skilled labor, trucks, contractors, trucking, aluminum, solid carbide, electronic components, quality labor, CS steel, linear bearings, electronic components, logistic services, manpower, electrical board components.

Prices on the UP side: Steel, carbon steel, stainless steel (due to 232 tariffs on EU), transportation, salt, carbide drills, SEBS resin, polypropylene, plasticizers, paraffinic oil, aluminum, electronic components, fasteners, stampings, packaging (corrugated), bags, foams, and film, nylon resin, China imports, metal-based chemicals, industrial textiles.

Prices on the DOWN side: Brass, aluminum*, oil, resin*.

*Item reported as both up AND down in price.

Latest Unemployment Reports

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

	May 2018	May 2017	Aug. 2009	20 Year Low
State of Michigan (Adj.)	4.6%	4.4%	14.6%	3.2%
State of Michigan (Unadj.)	3.8%	3.8%	14.1%	2.9%
Kent County	2.9%	3.1%	11.9%	2.1%
Kalamazoo County	3.4%	3.7%	11.1%	2.1%
Calhoun County	4.1%	4.5%	12.8%	2.7%
Ottawa County	2.7%	2.9%	13.3%	1.8%
Barry County	3.3%	3.5%	10.9%	2.2%
Kalamazoo City	4.2%	4.7%	15.2%	3.2%
Portage City	3.1%	3.4%	8.7%	1.3%
Grand Rapids City	3.8%	4.2%	16.1%	3.0%
Kentwood City	2.7%	3.0%	10.7%	1.4%
Plainfield Twp.	2.2%	2.4%	8.0%	1.4%
U.S. Official Rate (June)	4.0%	4.3%	9.6%	3.8%
U.S. Rate (Unadjusted)	4.2%	4.5%	9.6%	3.6%
U.S. U-6 Rate (June)**	7.8%	8.4%	16.7%	8.0%

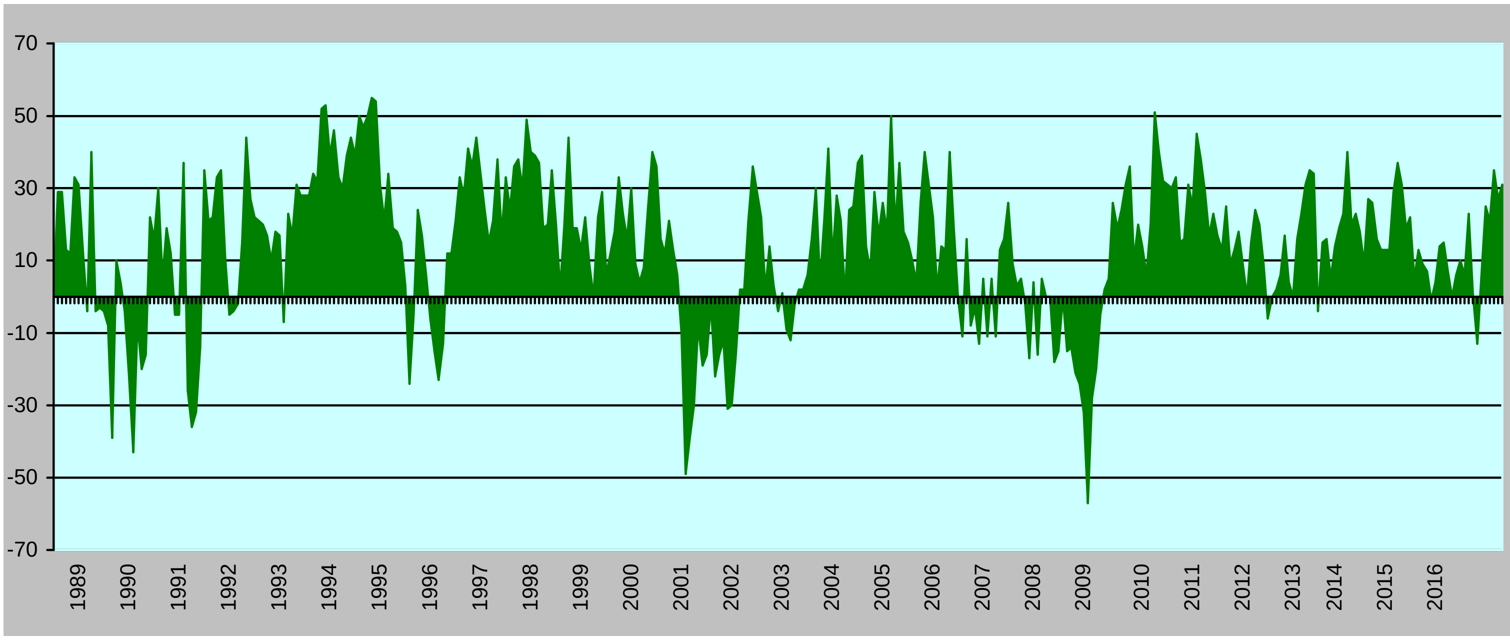
**U-6 for Michigan = 9.0% for April 2017 to March 2018

Index of New Orders: West Michigan

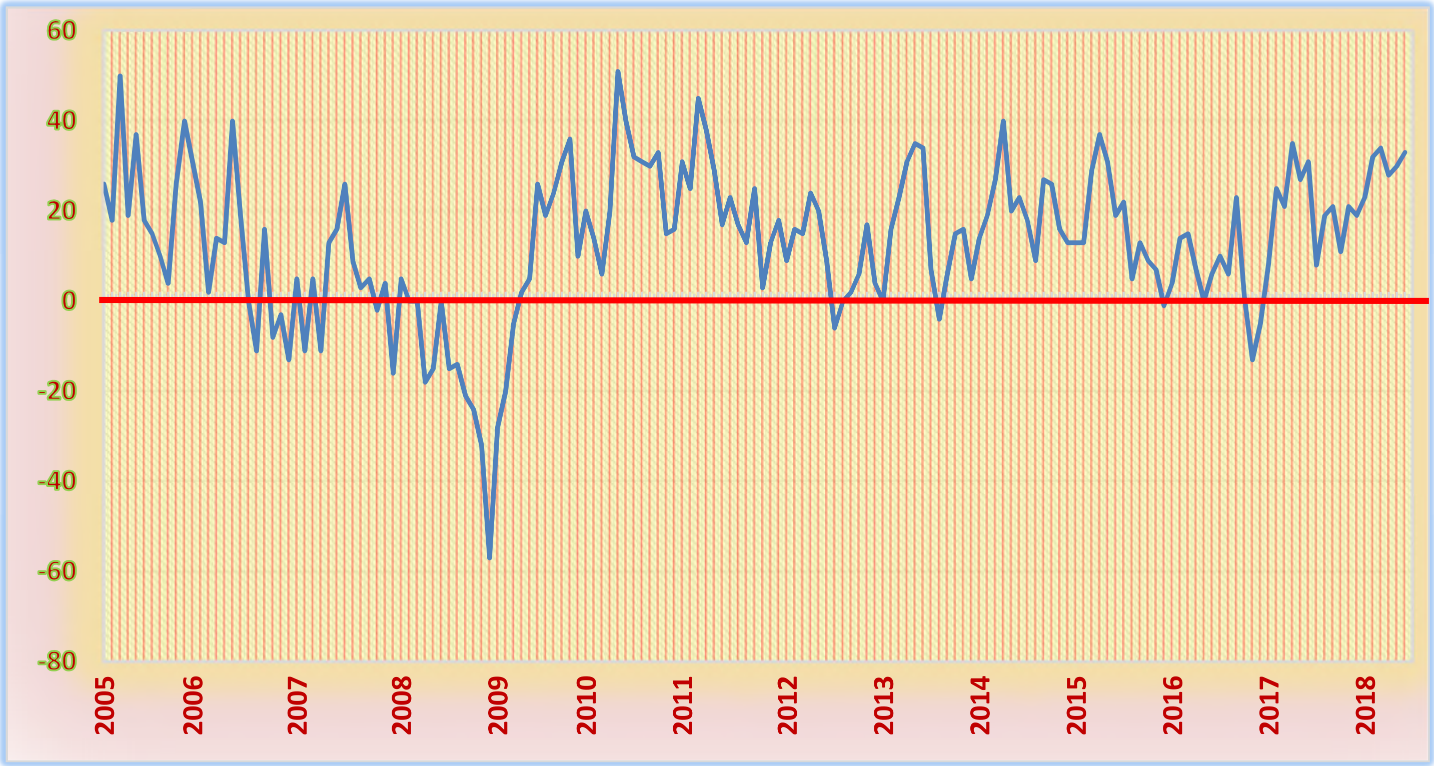
As the name implies, this index measures new business coming into the firm, and signifies business improvement or business decline. When this index is positive for an extended period of time, it implies that the firm or organization will soon need to purchase more raw materials and services, hire more people, or possibly expand facilities. Since new orders are often received weeks or even months before any money is actually paid, this index is our best view of the future.

Latest Report	+33 for the month of June 2018
Previous Month	+30 for the month of May 2018
One Year Ago	+31 for the month of June 2017
Record Low	- 57 for the month of December, 2008
Record High	+ 55 for the month of September, 1994
First Recovery	+ 3 in April of 2009 and forward

ISM-West Michigan Index of New Orders 1988 - 2018

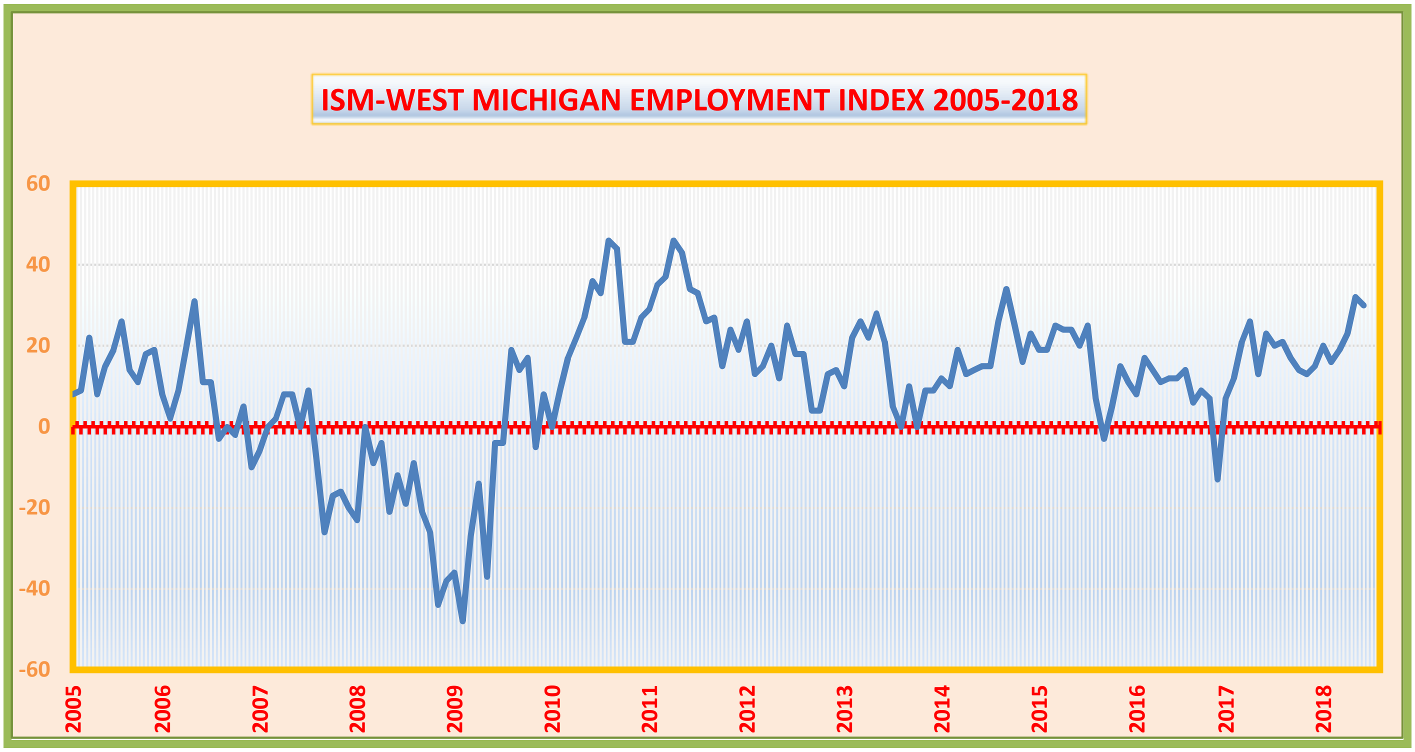


ISM-West Michigan Index of New Orders: 2005-2018 Only



ISM-West Michigan Index of Employment

The index of EMPLOYMENT measures the firm's increases and decreases in staffing, including permanent workers and temps. After economic downturns, it measures new hires as well as previous workers called back to work. When this index is positive for an extended period of time, it almost always signals a reduction in industrial unemployment for West Michigan. Normally, there is about a month or two in lag time between this report and the payroll numbers being reflected by the government statistics. However, almost all employment indexes are laggards, meaning that firms often wait until upticks in orders are confirmed before adding staff, and conversely laying off staff only after a downturn in orders appears to be certain for the foreseeable future.



ISM-West Michigan Future Business Outlook

The indexes of LONG TERM BUSINESS OUTLOOK and SHORT TERM BUSIESS 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.