

CURRENT BUSINESS TRENDS

by

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Still modestly down. That's the latest word on the Southwestern Michigan economy, according to the data collected in the last two weeks of May. NEW ORDERS, our index of business improvement, came in at -7, just slightly below the -4 we reported last month. The PRODUCTION index remained negative, but moderated to -4, up from -12. The EMPLOYMENT index came back to -21 from -39. Activity in the purchasing offices, our index of PURCHASES, backtracked to -26 from -22. Hence, last month's declaration that it is still too soon to declare the beginning of a recovery has come to pass. Whereas the signs of a recovery may be at hand for the nation as a whole, the bankruptcy of General Motors may have caused some of our local firms to step back and see where all of the chips fall before moving forward. As many pundits have already noted, we are in uncharted territory, and some thing we will have to reevaluate on a month-to-month basis until we see what the future holds for Southwestern Michigan as a whole.

Turning as we always do to individual industries, it is no surprise to find that some of our auto parts suppliers are struggling. Even those firms supplying the transplant firms have had some difficulties, although tide may now be turning. Business conditions for the industrial distributors turned a little weaker this month, although there were exceptions. Capital equipment firms continue to be down.

At the national level, the June 1, 2009 press release from the Institute for Supply Management, our parent organization, shows that the national economy is now outperforming the local economy. ISM's index of NEW ORDERS came in at +8, up from +2. The PRODUCTION index stayed modestly negative at -2, but recovered from the -13 we reported last month. The EMPLOYMENT index remained unchanged at -28. All of this resulted in ISM's Index of Manufacturing rising to 42.8, up from 40.1. This is up considerably from December's low of 32.9, and constitutes the best report we have seen in eight months. Any index below 50.0 generally depicts a contracting economy, so we are still not in a state of recovery. However, since the index has now improved steadily for the past five reports, there is now considerably evidence that the national economy has bottomed out.

At the international level, the news is also more positive than our local statistics. The composite index for J.P. Morgan's Global Manufacturing Report dated June 1, 2009 rose to 45.3 from 41.8, highest level the index has been since August. China and India reported increases in NEW ORDERS for the second consecutive month, which helped raise the international index of NEW ORDERS to 48.6. Also, the pace of job reductions eased in the Eurozone, Japan, and the UK. However, the author still characterizes the current report as "...well below a level consistent with outright recovery."

Last month's big news was the Chrysler bankruptcy. It now appears that the sale of assets to Fiat will provide enough cash to keep the company afloat, although the post-bankruptcy Chrysler will be 68% owned by the UAW pension fund. Having Chrysler come out of bankruptcy is certainly good news, but it is wise to remember that this only means that the *current* financial crisis has been mitigated. The firm still needs to deal with the thousand of unsold units still sitting on dealer lots, and with the problem of what cars the public will buy in the future. In this sense, whether Chrysler survives over the long term will be determined by the marketplace.

This month, it's GM's turn to make headlines. As a result of the current bankruptcy plan, the governments of the US and Canada will acquire a 72% stake in the company, which will really be divided between the "new" and "old" GM. The taxpayer ante will be another \$30 billion, which makes the \$1.5 billion that Lee Iacocca requested for Chrysler in 1979 look like chicken feed. There is already speculation that the company will be back for more money when the \$30 billion runs out. Again, there is still no guarantee that the firm will be able to sell cars that the public will buy.

Focusing back on some good news, the problem of inventory liquidation that we have noted in the past three reports continues to improve. ISM's April index of INVENTORIES came in at -34, which indicates that many firms are still trying to work those inventories down. However, the JP Morgan International report noted that worldwide inventories are starting to come back into line. Similarly, the Greater Grand Rapids index of PURCHASED MATERIAL INVENTORY came in at -17, an improvement over the -25 reported last month. For Southwestern Michigan, the index improved to -4 from -26. As inventories come back into line, the worldwide prices for commodities such as copper and corn continue to stabilize. Commodity price stabilization is essential to economic recovery.

A bigger problem for the economy as a whole remains the massive amount of debt that the government will need to float between now and October. Two trillion dollars is an almost inconceivable amount of money by any standard, and the reaction of the markets to this amount of new debt is difficult to assess. Most financial observers doubt that this amount of money can be raised without offering the new debt at a higher rate than the current 10-year rate of 3.72%. Indeed, despite the efforts of the Federal Reserve to keep rates as low as possible, the markets are already diving rates higher in apparent anticipation of the requirements for the massive amount of government financing about to hit the market. Since mortgage rates are once again starting to edge up, any potential recovery in the housing sector could be stalled.

Finally, it seems obvious that Michigan will continue to be under a cloud until the GM bankruptcy is over. The current plan calls for the bankruptcy to be over in 60-90 days, and this may be possible. However, a huge marketing gap still exists, and the fact remains that people must start buying a lot more cars before we can declare an end to the crisis. If this does not happen, GM will simply slide back into bankruptcy.

COMMENTS FROM SURVEY PARTICIPANTS

"We're playing the reduced inventory game with our customers. Business is weak, but some orders are starting to surface to cover ongoing production."

"Outlook for the next three months looks worse than we anticipated."

"We have gone to a four day week. Not good, but it keeps everyone employed."

"Some forging suppliers are pushing for cost increases. We have issues with delivery from suppliers due to plant shutdowns. We're seeing more delivery 'pull in' requests than 'push out.'"

"Some customers are starting to re-build inventories."

"There are many requests for quotes, but not many new orders as a result."

"There is more activity, but quantities are way down."

"April was a good month, the best in some time. But the early indications show May is off to a terrible start."

"Toyota Camry and Corolla schedules are increasing, but there is still a long way to go back to normal."

"Suppliers are very hungry for business, worried about losing accounts, and are being aggressive. As a purchasing person, I don't forget the suppliers who were on the bandwagon to jump the gun on raising prices. I reward the faithful and punish the others."

"Sales are still soft. Our California plant shut down as of 5/15/09. I expect some more lay offs in the Kalamazoo plant. We are not having much fun right now."

	UP	SAME	DOWN	N/A	May Index	Apr. Index	Mar. Index	22 Year Average
Sales (new orders)	33%	25%	42%		- 7	- 4	-20	+11
Production	25%	29%	29%	17%	- 4	-12	-24	+10
Employment	4%	71%	25%		-21	-39	-26	+ 2
Purchases	12%	50%	38%		-26	-22	-40	+ 7
Prices Paid (major commod.)	0%	79%	21%		-21	-31	-20	+ 2
Lead Times (from suppliers)	12%	67%	21%		- 9	- 0	-28	+27
Purchases Material Inventory (Raw materials & supplies)	17%	41%	21%	21%	- 4	-26	-20	- 6
Finished Goods Inventory	17%	33%	38%	12%	-11	-30	-24	- 4

Items in short supply: Bearings

Prices on the UP side: Printed materials, fuel, some electronics, plastic resins, complex assemblies.

Prices on the DOWN side: Corrugated products, copper, steel, wire, most metals, CO2, dry ice.