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Grand Rapids Economic Forecast 2012

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- Business confidence index is poised to approach 60% for the first time in 5 years
- Employment is expected to grow by 1.5% to 2% in 2012
- Overall nominal sales are expected to increase by 2.5% for 2012
- Exports continue to be a bright spot; expected growth is 7% during 2012
- All indicators signal a continuous but slow improvement in 2012

Introduction

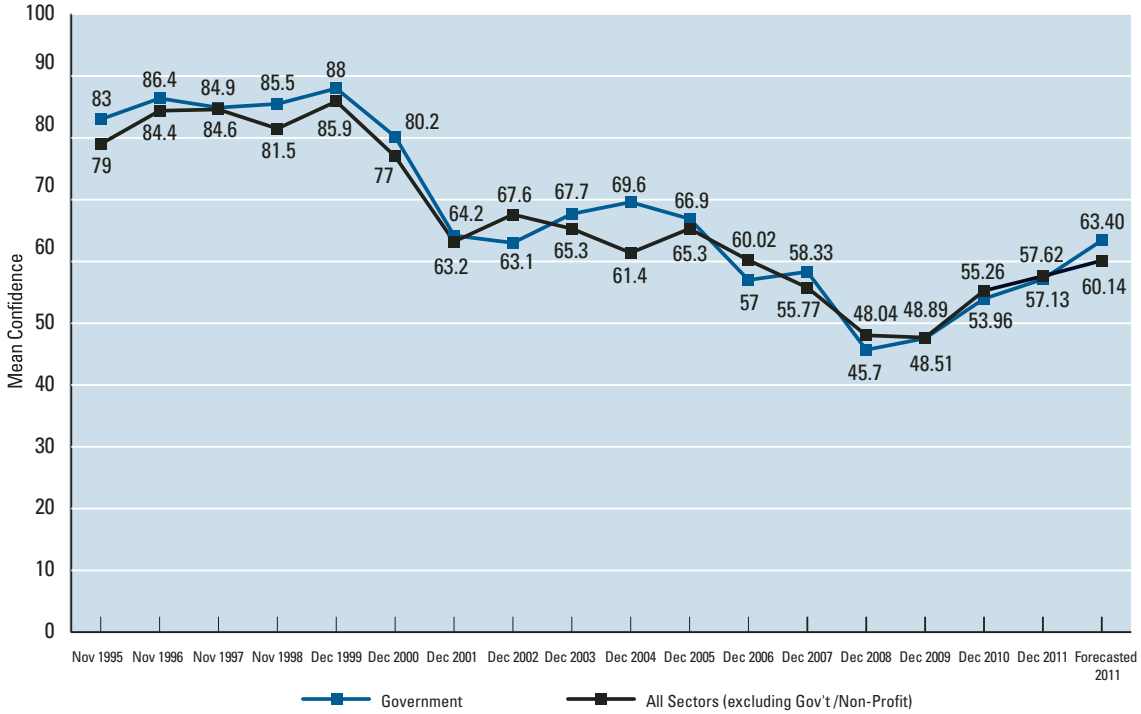
The survey for the greater Grand Rapids economy (Kent, Ottawa, Muskegon, and Allegan counties) was conducted in November 2011. A survey was mailed to the CEOs of 1000 organizations based on a representative sample. We tried to ensure that the sample represented different sectors of the regional economy and the geographical diversity of the area. Eventually, 259 organizations responded, resulting in a response rate of 26%. Due to the small sample size, the survey should be interpreted with caution.

A few methodological considerations are in order. Although we discuss the survey results in terms of averages, the data are represented in a histogram format to show the entire distribution of responses. The employment, sales, and export numbers are more volatile as *raw averages* (when calculated without adjusting for outliers—responses beyond one standard deviation). Since the average of a small sample is significantly influenced by extreme numbers, we use the averages without the outliers to provide more reliable results. The histograms, however, depict all the available observations to show the broad picture. Note that the total numbers in the histogram figures do not add up to exactly 259 because a few respondents did not provide their employment or sales data.

Confidence Index

A major goal of our survey is to historically track the overall business confidence of the Grand Rapids area with a confidence index. The confidence index respondents use a scale from zero percent (no confidence at all) to one hundred percent (complete confidence). In response to the question: *How confident are you in the regional economy?* The average responses for the private sector and the government/non-profit sector over the last 17 years are shown in Figure 1.

Figure 1 West Michigan Confidence Index 2012



Let us consider the private sector confidence index. The current results need to be interpreted in a larger historical context. For the last seventeen years that we have surveyed the region, when the economy has been growing steadily at a robust rate, the confidence index has depicted a high level of confidence, generally around 80% for the private sector. Since the 2001 recession, the confidence index has been in the vicinity of the sixties and the high fifties. The confidence index in 2008 and 2009 was below the 50% benchmark. In December 2010, the confidence index had

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increased to 55.3%. In November 2011, it increased to 57.6% and is projected to increase to 60.1%. The government and nonprofit sector has similar numbers: 54% for 2010 and 57.1% for 2011, and 63.4% projected for 2012.

For the first time in the last five years, the projected confidence is approaching the 60% benchmark. There is a palpable increase in the regional confidence for the next year. The regional economy is expected to improve slowly in 2012 after a long consolidation process.

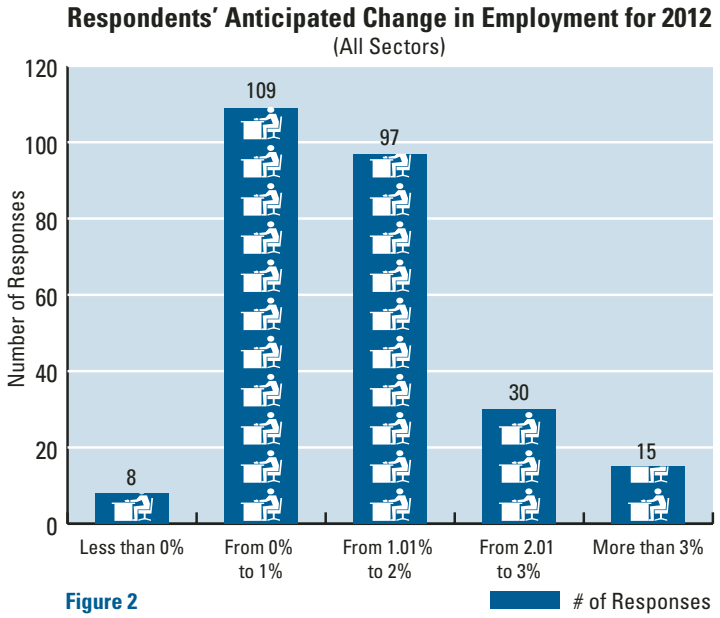

Figure 2

Employment

Due to the restructuring in the manufacturing sector, the regional labor market in West Michigan had been repairing at a very slow pace since the recent recession. For 2011, employment was projected to grow at an average of 2%. Actual employment growth has been slower. The numbers from the Local Area Unemployment Statistics (LUAS) survey indicate that employment in KOMA has grown by approximately one percent. The Current Employment Statistics (CES) establishment survey for the three metropolitan areas (Grand Rapids-Wyoming, Holland-Grand Haven, and Muskegon-Norton Shores) indicates employment growth of approximately 1.8%. It appears that our projection last year was more optimistic than what actually happened in 2011.

Factors that continue to depress expectations for 2012 are the same ones that slowed the recovery in 2011. They include the still-tight credit market for small business, the persistently high unemployment rate, fiscal uncertainty and higher debt at the federal level, and ongoing concerns about the Eurozone. Consumer and business confidence will consolidate slowly as the national economy improves. The structural problems in Michigan will continue to depress expectations compared to the national profile. However, the new resurgence in the manufacturing sector is encouraging.

The respondents answer the following question: *What percent change do you expect in employment for the four counties in 2012?*

For 2012 we can see that the distribution is clustered in the 0 to 2% range, but there are 142 respondents who expect to hire more than 1%. Only 8 respondents expect to reduce their work force. Average employment is expected to grow at 1.4% (without outliers) and 2.1% (with outliers). Given these expectations, regional employment will grow in the 1.5% to 2% range.

More than half of the respondents (51%) expect to hire next year. Of those persons being hired, about 70% are expected to be permanent workers. These numbers corroborate the slow improvement in the labor market in 2012.

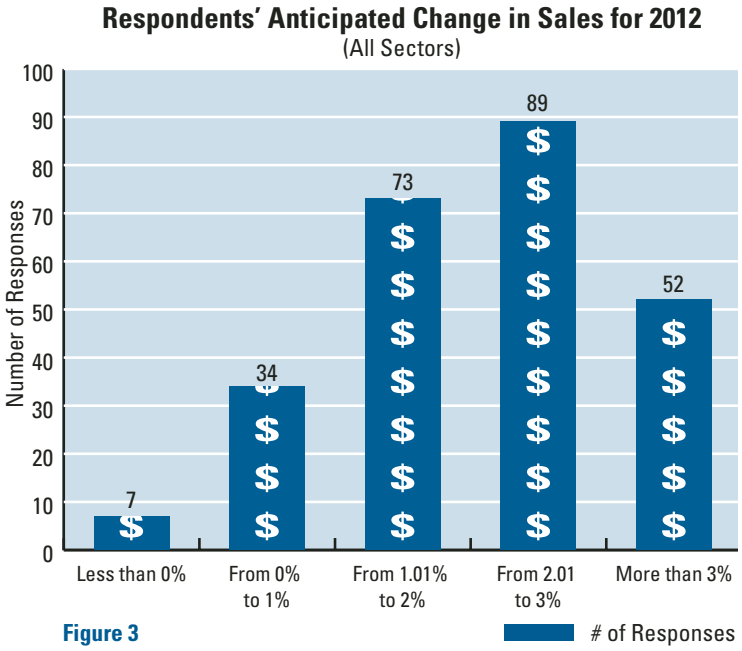

Figure 3

Sales

For sales, the respondents answer the following question: *What percent change in sales do you project for the four counties in 2012?* In times of robust economic growth, sales have grown at an annual rate of 5%. The sales projection made by respondents for last year was 2.5% for the private sector (without outliers). We can see in Figure 3 that respondents are clustered around the 1% to 3% range. The holiday season shopping numbers indicate that retail sales are showing a significant rebound. In this context an overall sales growth of 2.5% seems reasonable.

Note that our sales numbers are for the nominal sales of all goods/services produced in the West Michigan economy. Consequently, the increase could be in prices and/or quantities.

Export Growth

In spite of the recessionary times, exports have been growing above 6% for the last few years. Part of the export growth is propelled by the low value of the dollar and the resumed high growth rates in Asia, particularly China and India. This year exports are expected to grow at approximately 6.5% (without

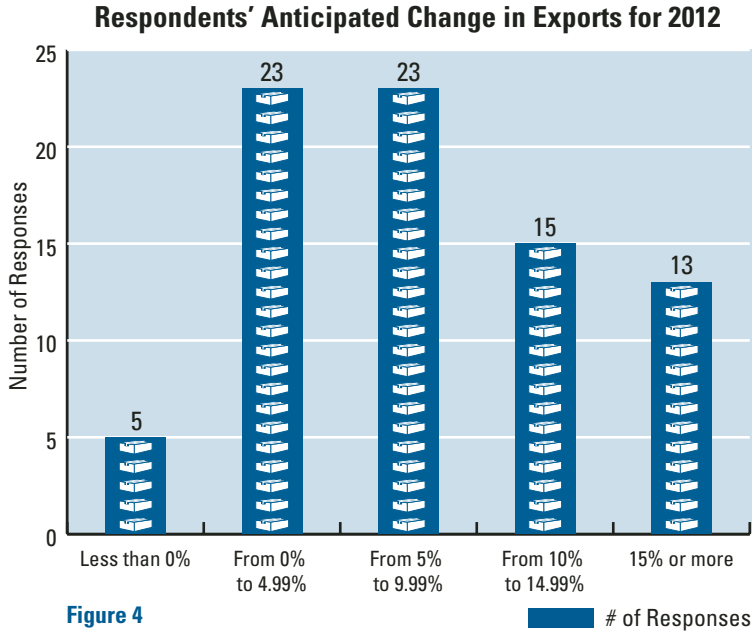

Figure 4

outliers) and 8.2 (with outliers). Actual growth will be in the 6% to 8% range for 2012. However, since the expected growth of exports is based on a much smaller sample of only 79 respondents, it should be viewed with caution.

General Expectations

The slow improvement in employment, sales, and exports has also influenced the expectations about achieving a robust regional growth rate of 5% in the near future. (Figure 5) Approximately 43% expect a robust growth by December 2013. A significant majority (57%) expected a robust growth only after December 2013. These numbers are more pessimistic than last year. Anecdotal evidence suggests that most respondents have a notion that even in "good times" we will return to a "new normal" although most are not clear about what this would look like. Given the continued national and global uncertainty and the continuous bickering at the Federal level, this pessimism is understandable.

General Outlook

What is the final word on the national and regional economies? At the national level, expected growth will average between 2% and 3% for 2012 with significant volatility. The economy will continue to grow slowly. Nationwide employment will continue to improve in 2012. The Household Survey job report from the Bureau of Labor Statistics (BLS) for December, 2011 indicating the creation of 200,000 new jobs is encouraging. Full-time hiring will increase significantly as businesses become progressively more confident about the future. However, it is not likely that the employment situation will improve dramatically. By the end of 2012, the unemployment rate will be in the 7.8% to 8.3% range.

One note of caution is in order. Problems similar to the Eurozone could visit our shores soon. Unless we put our long-term fiscal house in order by reducing long-term entitlements and reforming the tax code to raise more revenue, there is a distinct possibility that the long-term solvency of the government resources will be tested by the market. The important thing is to get the timing right in pivoting towards a more constrained fiscal policy for the long term, once we have consolidated a strong growth path. The right time to have a more restrictive fiscal policy and whether the federal government will develop a *credible binding policy for controlling entitlements* are two key issues confronting the nation.

At the regional level, the economy continues to improve slowly. Overall confidence is projected to approach the 60% benchmark. Employment will grow by approximately 1.5% to 2%. Nominal sales will increase by 2.5%. In spite of its volatility, exports have always been a bright spot during the Great Recession and are projected to grow next year by 7%.

There are several wild cards that may disrupt the forecasts. These include a significant meltdown in the Eurozone, further downgrading of U.S. debt, and/or some other external shock.

West Michigan will continue to find a foothold by diversifying into specialized services such as health care, professionals services, education and high tech\precision manufacturing. The state needs to ensure that it will create a highly qualified work force for the future by investing more resources in education and training. State resources need to be leveraged to position ourselves strategically in growth sectors of the future. Besides health care and high tech manufacturing, state policies need to promote more renewable/alternative energy options within the state.

Acknowledgments

We are very grateful to all the organizations that participated in the survey. ■

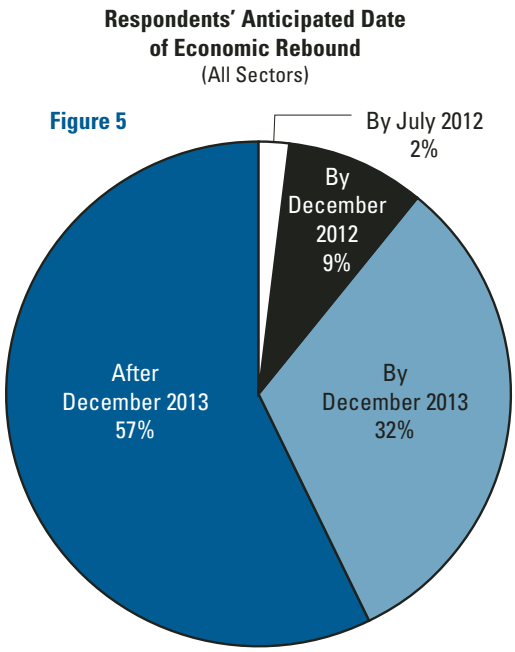

Figure 5