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Grand Rapids Economic Forecast 2007

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Grand Rapids Economic Forecast 2007

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- Business confidence has suffered a decline and is expected to rise modestly in 2007
- Employment growth is expected to be modest at 0.7% for 2007
- Overall sales are expected to grow at a lower rate of around 2.5% for 2007
- Exports continue to be a bright spot; expected growth is 6% for 2007
- The decline in regional confidence and sales reflects the ongoing restructuring and a slowdown of the national economy

Introduction

Our latest survey forecast for the greater Grand Rapids economy (Kent, Ottawa, Muskegon, and Allegan counties) was conducted in November 2006. A survey was mailed to the CEOs of 675 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, 166 organizations responded. The results of the survey need to be interpreted with caution because of the small sample size.

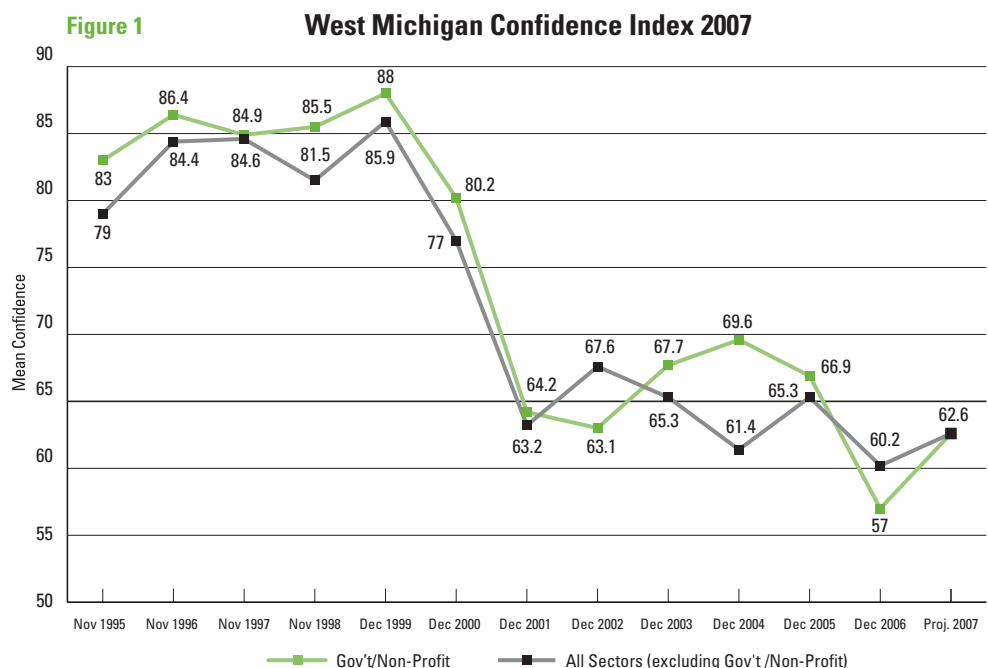
A brief methodological note is in order. Although we discuss the survey results in terms of averages, the data are also presented in a histogram format to show the entire distribution of responses. The employment, sales, and export numbers are more volatile as *raw averages* (when calculated without adjusting for outliers—responses beyond one standard deviation). Since the average of a small sample is overly influenced by extreme numbers, it is advisable to examine both the raw averages and the mean values generated without the outliers. The histograms, however, depict all the observations. Since individual responses vary significantly, the outliers in the data should be interpreted with caution. The averages without the outliers tend to be more reliable.

Confidence Index

A primary goal of our survey is to historically track the overall business confidence of the Grand Rapids metropolitan area by a Confidence Index. The Confidence Index respondents use a scale from zero percent (no confidence at all) to one hundred percent (complete confidence). The current results need to be interpreted in a larger historical context. We have been conducting surveys of the region for the last eleven years. When the economy has

been growing steadily at a robust rate, the confidence index has depicted a high level of confidence, generally above 80% for the private sector.

In the previous survey, the Confidence Index was marginally lower at 65.3% at the end of 2005, amid economic evidence that the economy was growing slowly. The results this year indicate that business confidence of the private sector has sunk to a relatively low level at 60.2%. Respondents are expecting a marginal improvement in confidence to 62.6 for 2007. We continue to base our analysis on the forecasts made by the private sector. The government and nonprofit sector are slightly lower reflecting the loss in government revenue. Factors influencing the depressed expectations for 2007 include the following: higher interest rates, continued high energy prices, the uncertainty due to the war on terrorism, and weak job growth prospects due to restructuring.



¹ Hari Singh is Chair of the Economics Department. Nancy Boese is the Regional Director of the Michigan Small Business & Technology Development Center (MI-SBTDC). We were aided by invaluable research support from Elvira Yaparova and graduate research assistants at MI-SBTDC.

Employment

Due to the ongoing restructuring in the manufacturing sector, the regional labor market in West Michigan has been repairing at a slow pace. Figure 2 indicates projected employment growth for 2007. Overall, the growth in employment for 2007 is projected at .69% with outliers and at 0.73% without outliers.

Consider this expectation in the context of what we know at this time. Traditionally, the regional and national economies have followed similar trends in terms of the business cycle. However, recently the actual economic situation in Michigan has been relatively worse compared to the national economy. West Michigan has traditionally relied more on the manufacturing sector. Employment in the manufacturing sector continues to decline as more consolidation in the workforce takes place, particularly in auto and auto-related industries. American auto manufacturers are losing market share and are saddled with high legacy costs. The full economic impact of their consolidation and buy-outs has yet to take place. Ongoing consolidation will have relatively less negative impact in the west compared to the east side. However, job losses in manufacturing will continue in West Michigan. New jobs will be created in the services sector particularly in health, education, and financial services.

The labor market in West Michigan has been showing very modest growth in 2006 and is not likely to improve significantly in 2007. Our survey indicates that 53% of respondents are likely to hire new workers in 2007. Most respondents who intend to hire expect to employ permanent workers (76%) as opposed to temporary workers (24%). However, given that new job applicants will enter the labor market, net job opportunities will be scarce.

Figure 2 Respondents' Anticipated Change in Employment for 2007
(All Sectors)

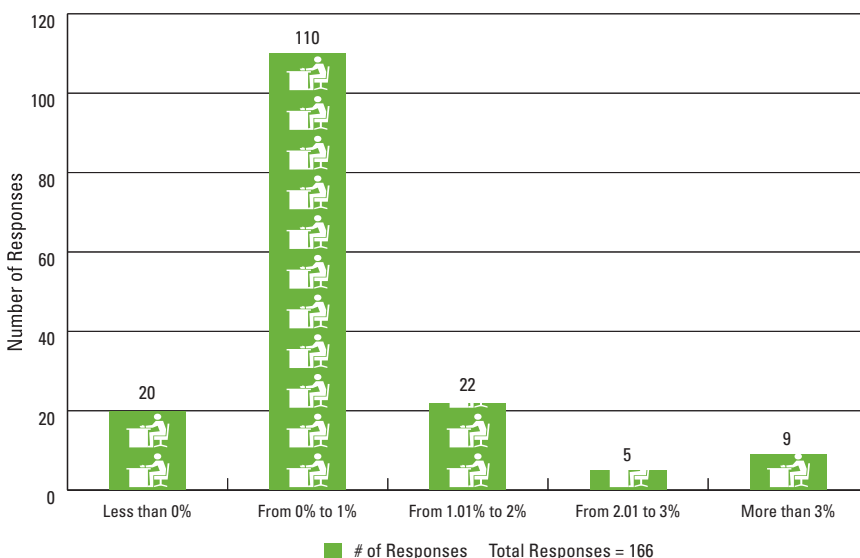
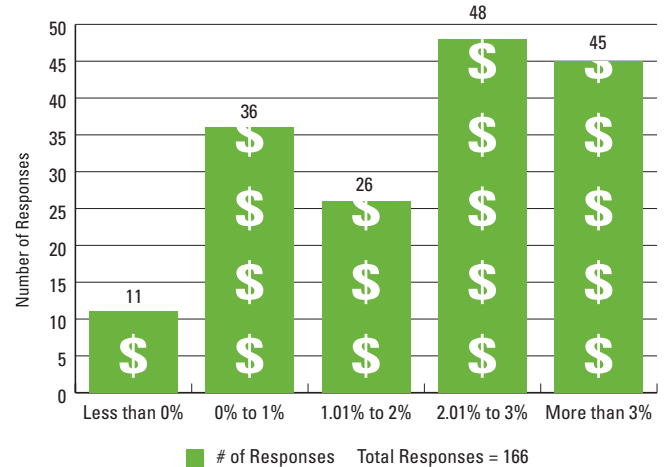


Figure 3 Respondents' Anticipated Change in Sales for 2007
(All Sectors)



Sales

Sales projections made by respondents for last year were 3.3%. The projected average sales growth for 2006 is 2.58% without outliers and 2.53% with outliers (Figure 3). In times of robust economic growth, sales have grown at an annual rate of 5%. The expectations of our respondents indicate that it may take some time before this higher trend growth rate is achieved. Note that our sales numbers are for the nominal sales of all goods/services produced in the West Michigan economy.

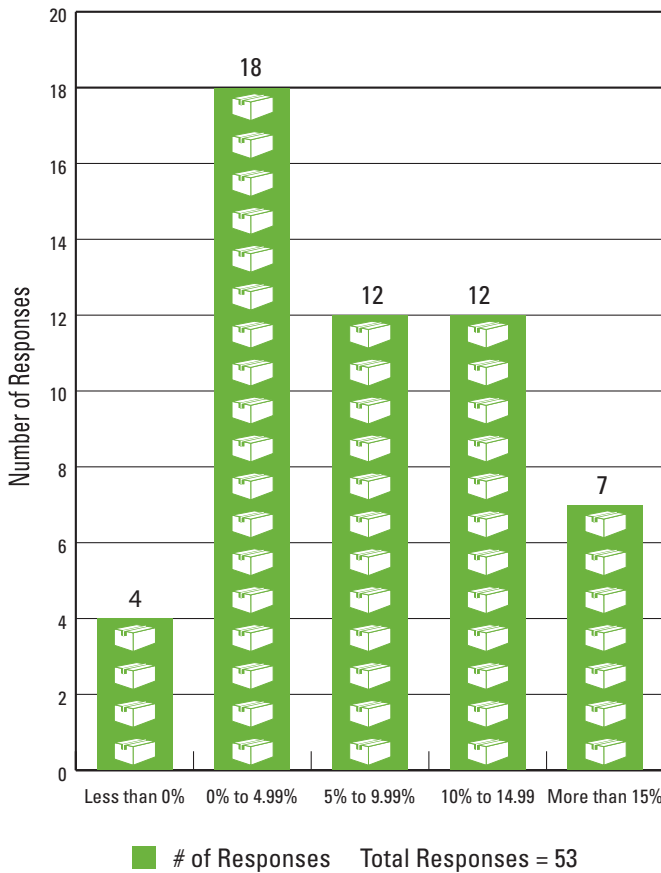
Export growth

About one-third of all respondents export their output. The expected growth in exports has generally averaged higher than 5% in the late 1990s. Last year, exports were projected to grow at 4.7% without outliers and at 6.9% with outliers. In 2007, exports are projected by respondents to grow 5.8% without outliers and 6.7% with outliers (Figure 4). Given the volatility in exchange rates and uncertain prospects for worldwide growth, it is not surprising that expectations for growth in exports are volatile. The adjusted average growth is probably more reliable. The falling dollar relative to the Euro has helped the exports sector recently. Overall, export growth projections are marginally higher relative to last year's expectations. Compared to domestic sales, export growth is still a bright spot for the regional economy. Since the expected growth of exports is based on a much smaller sample, it should be viewed with caution.

The expectations about achieving a robust regional growth rate of 5% appear to have become more pessimistic. The results indicate that compared to last year, respondents have significantly more pessimistic expectations about the return of good economic times. A majority of the respondents (53%) expect a significant economic rebound (a robust 5% annual growth) only after 2008. This finding corresponds to the reduction in business confidence for 2007 compared to previous years.

Exporting Respondents' Anticipated Change in Exports for 2007

Figure 4



The survey results demonstrate that some industries are able to capitalize on an expanding export market. More firms need to aggressively seek export opportunities. In spite of the recent problems in the manufacturing sector, eventually this sector will be more lean and competitive. However, new job opportunities in manufacturing are likely to be limited. At the same time, opportunities are emerging in new sectors: healthcare, bio-tech, education, and specialized services. State resources need to be leveraged to position ourselves strategically in these growth sectors of the future. Whether we are seeking to re-vitalize the manufacturing sector or expand into the industries of the future, both strategies require a highly skilled work force. Expanding education and training opportunities by improving schooling and extending scholarships for college are a good long term strategy for Michigan.

Acknowledgments

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

What is the final word on the national and regional economy? At the national level, there is considerable fiscal stimulus. The Federal Reserve Bank may still raise interest rates in a preemptive manner to reduce the risk of future inflation, although the general presumption is that the Fed will be neutral for a while. The declining housing market continues to be a drag on economic growth. The real growth in output for 2007 is expected to slow down due to the impact of higher interest rates, continued high energy prices, and the consolidation in the housing market. The growth in real output at the national level will be approximately 2.5%. As we have seen in 2006, there will be considerable variation in GDP growth in the quarterly estimates.

At the regional level, since the consolidation in the manufacturing sector is likely to continue, the outlook is less optimistic. Employment growth will be modest (0.7%) and sales will grow at a slower pace (2.5%) for 2007. For those who seek external markets, export growth continues to be a good opportunity to buffer domestic markets (6% annual growth).

Respondents' Anticipated Date of Economic Rebound (All Sectors)

Figure 5

