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Grand Rapids Economic Forecast 2011

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- Business confidence index is poised to rise significantly above 50% for the first time in 2 years
- A significant rebound in employment, expected growth is 2% in 2011
- Overall nominal sales are expected to grow by 2.5% for 2011
- Exports continue to be a bright spot; expected growth is 9% during 2011
- All indicators signal a significant turnaround in 2011

Introduction

The survey for the greater Grand Rapids economy (Kent, Ottawa, Muskegon, and Allegan counties) was conducted in November 2010. A survey was mailed to the CEOs of 937 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. Of the 937, 211 organizations responded, resulting in a response rate of 22.5%. 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 histograms figures do not add up to exactly 211 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 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). Here are the average responses for the private sector and the government/non-profit sector over the last 16 years (Figure 1). In response to the question: How confident are you in the regional economy?

Let us consider the private sector confidence index. The current results need to be interpreted in a larger historical context. During our surveys of the region for the last sixteen years, 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. However, the confidence index during the last two years (December 2008 and 2009) was below the 50% benchmark (approximately

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In November 2010, the confidence index increased to 55.26%. It is projected to be higher at 59% for 2011. The government and nonprofit sector has similar numbers 53.96% for 2010 and 59.18% projected for 2011).

Although we are beginning to come out of the Great Recession, expectations are still depressed but the overall outlook is beginning to take a positive turn. For the first time in the last two years the projected confidence is rising significantly above the 50% benchmark. There is a palpable increase in the regional confidence for the next year. The regional economy has picked up its pace for the long consolidation process.

Factors that continue to depress expectations for 2011 include the continued tightening of credit to small business and the high unemployment rates. Consumer and business confidence will consolidate slowly as the national economy improves. The structural problems in Michigan and the ongoing consolidation in manufacturing will continue to depress expectations significantly compared to the national profile.

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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.

The respondents answer the following question: What percent change do you expect in employment for the four counties in 2010?

The projected change in employment for 2009 for the private sector was a decline of almost one percent (-0.94%). The actual decline in employment in West Michigan for 2009 was quite close to the projection.

Similarly for 2010, we projected private employment to be one half of one percent. The actual numbers for October 2010 compared to one year earlier show an increase of about 0.3 of one percent. It appears that the forecasts have been quite accurate for the last two years.

For 2011 employment is projected to grow at an average of 2.3% in the private sector (without outliers). This is a significant increase compared to last year. All the responses are depicted in Figure 2. We can see that the distribution is clustered in the 0 to 2% range, but there are 40 respondents who expect to increase their workforce by more than 3%. Only 11 respondents expect to reduce their workforce.

Last year 36% of the respondents indicated that they will hire workers in 2010. This year approximately 60% have indicated that they will hire in 2011. Of the persons who responded, about two thirds (66%) indicated that they would hire permanent workers. These numbers corroborate the significant pickup in hiring that is expected to take place in 2011.

Sales
For sales, the respondents answer the following question: What percent change in sales do you project for the four counties in 2010? 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 0.77%. For 2011, sales are expected to grow at 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
During good times the expected growth in exports has generally averaged higher than 5% in the late 1990s. Last year, exports
were expected to grow an average of 8%. Compared to the domestic outlook, export growth has been a bright spot for the regional economy. 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 9%. However, since the expected growth of exports is based on a much smaller sample of only 52 respondents, it should be viewed with caution.

The more optimistic numbers in employment, sales, and export have also influenced the expectations about achieving a robust regional growth rate of 5% in the near future. Last year, 36% of the respondents expected a robust growth in two years. This year the number has gone up to 42% (by December 2012). Last year the number for after two years was 45%, but this year that percentage has shrunk to 37% (after December 2012).

These results are consistent with Dr. Brian Long's West Michigan Supply Management survey of purchasing managers (N.A.P.M.) that shows a turnaround in production and employment in 2011.

What is the final word on the national and regional economy? At the national level, the economy will continue to pick up growth. The Federal Reserve Bank is attempting to keep long-term interest rates low by embarking on quantitative easing for the second time (QE 2). The compromise tax package that extends the tax cuts enacted by President Bush and has a variety of other tax incentives is likely to provide more stimulus, at least in the short run.

Nationwide employment will continue to improve in 2011. Right now it is reflected in more hiring of temporary workers and lengthening of the average work week hours. Full time hiring will increase significantly as businesses become progressively more confident about the future. However, it is likely that the employment situation will have a “new normal” compared to the “good old days” of the late 1990s when the nationwide unemployment had dropped to 4.5%. Since a significant part of the unemployed are older and have been without work for a long time, the new normal in the labor market, even in good times, might be in the 6% to 7% range.

The economy will expand faster in 2011 compared to last year, but the growth in real Gross Domestic Product will not be back at full capacity. There will be considerable variation in GDP growth rates each quarter. Overall, GDP may grow 3% to 4% for the entire twelve months of 2011.

One note of caution is in order. The impact of accommodative fiscal and monetary policies, within the context of historically high budget deficits, has already started exerting upward pressure on long-term interest rates. Unless we put our long-term fiscal house in order by reducing long-term entitlements and raising taxes, there is a significant 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 the key issues confronting the nation.

At the regional level, there is significant improvement across the board. Overall confidence is projected to increase significantly above the 50% benchmark. Employment will grow by approximately 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 rebound even more next year to 9%.

West Michigan will continue to find a foothold by diversifying away from manufacturing into specialized services such as health care, professional services, and education. The state needs to ensure that it will create a highly-qualified work force for the future by investing more resources in education. State resources need to be leveraged to position ourselves strategically in growth sectors of the future. Besides health care and homeland security, 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.