THE PURCHASING ECONOMY SURVEY REPORT August 2012

"A monthly survey of supply chain managers"

Welcome to our August report covering July survey results. Regional and national surveys of supply managers indicate that economic growth is slowing and inflationary pressures are their lowest since the recession. Follow my comments at: www.twitter.com/erniegoss

Red, Blue and Purple States: Top Economic Performers 1999-2010

Blue States Underperformed Red States

Do Red states, which are viewed as more pro-business and tax friendly, experience superior economic performance when compared to Blue states that are seen as more pro-government and tax burdensome? That is for the last three presidential elections, have the states voting for the Democrat presidential candidate (Blue), or the states with electoral votes cast for the Republican (Red), experienced the best economic performance? Alternatively, have the Purple states, states that voted for the Democrat presidential candidate in at least one of the elections, and the Republican in at least one of the three presidential elections been the top performing group? U.S. Bureau of Economic Analysis data show that in terms of the growth of the overall state economy, or Gross Domestic Product (GDP) between 1999 and 2010, Red states grew by a median of 66.2% or significantly greater than Blue states at 52.2%, and Purple states at 60.5%. As for job additions over the same time period, Blue states again underperformed with a median growth of 0.2% compared to Red states' expansion of 3.2% and Purple states' of 3.3%. In terms of after- tax per capita income growth, the gap was substantial with Red states advancing by a median 52.3% compared to the much slower growth of Purple states at 46.1% and Blue states at 49.7%. Moreover in terms of overall growth (GDP), 8 of the top 10 performing states were Red states while only 4 of the 10 bottom performing states were Red. On the other hand, Blue states tended to have a somewhat more evenly distributed income with a median Gini coefficient of 0.450 compared to Red and Purple states' 0.455. Gini coefficients range between 0 and 1.00 with lower coefficients indicating more evenly distributed income. Details of the analysis can be accessed at: www.economictrends.blogspot.com Ernie Goss.

Link to video:
http://www.youtube.com/watch?v=lRawe2cNuQg

LAST MONTH'S SURVEY RESULTS

Mid-America Indicators Sink to Recession Lows:
Drought Weighs on Region

SURVEY RESULTS AT A GLANCE

- Leading economic indicator fell below growth neutral for the first time since 2009.
- New export orders drop to lowest level since August 2009.
- Business confidence takes biggest one-month plunge since 1994.
- Drought impacting ethanol and food processing plants.

Drought conditions across a nine-state region pushed the Mid-America monthly Business Conditions Index below growth neutral for the first time since 2009. The index, a leading economic indicator from a monthly survey of supply managers, declined for a third straight month indicating a rising likelihood of a recession.

Overall index: The index, which ranges between 0 and 100, fell to 48.7 from 57.2 in June. As a result of deteriorating global and national economic conditions as well as drought conditions, the index took its biggest decline since the recession in November 2008. Over the past several years, the region has benefited from very healthy exports and robust farm income. These two economic drivers are clearly moving in the negative direction. Recent gains in the dollar have made U.S. goods less competitively priced abroad. Combine that with drought conditions and we will see farm income take a hit and that will spill over into other industries in the region.

This month supply managers were asked the how the drought was impacting the costs of inputs purchased and the sales of output sold by their companies. Only 14 percent reported negative impacts on sales while 19 percent reported increasing costs due to the drought. Over the next six months, supply managers expect the costs of inputs that they purchase to rise by 2.1 percent. This is slightly higher than expected price increases from April of this year when we asked the same question.

Drought conditions are already negatively affecting ethanol and food processors in the region. In an earlier survey conducted in rural areas of the region, almost two-thirds of ethanol producers either temporarily closed or cut back operations due to lower oil prices and to a lack of corn and/or higher corn prices resulting from the drought.

Employment: The economic slowdown took its toll on the employment index. While the index remained above growth neutral for the seventh month in a row, it declined sharply to 51.1 from June's much stronger 61.8. While government data on state job growth for July will be positive but tepid, I expect the numbers to move negative in the months ahead. Very weak new orders and production for July will mean job losses for firms in August.

Wholesale Prices: The prices-paid index, which tracks the cost of raw materials and supplies, was unchanged from June's 51.1. These low readings for our inflation gauge are consistent with weakening economic conditions. However, I do expect drought conditions in the region to push the index higher in the months ahead even as the economy continues to slow.

Confidence: Looking ahead six months, economic optimism, as captured by the July business confidence index, fell to its lowest level since the recession at 38.0, down from June's 56.7. This is the largest one month decline that we have recorded since we initiated the survey in 1994. European economic turmoil, the impending fiscal cliff, the national economic slowdown and the drought all combined to push the confidence index to recession levels.

Inventories: The July inventory index sank to 45.7 from 53.9 in June. This is another signal of economic pessimism as supply managers cut the inventory levels for July in anticipation of slower production in the months ahead.

Trade: July's export reading for the Mid-America region declined to 45.2, its lowest level since August 2009, and down from June's weak 48.4. At the same time, July imports decreased to 46.5 from 51.5 in June. Weaker global growth and the rising value of the dollar making U.S. goods less competitive abroad pushed the export reading lower. At the same time, slower regional growth restrained the demand for imported supplies and materials. I expect trade numbers to weaken even more in the months ahead for the nine-state region.

Other components: Other components of the July Business Conditions Index were new orders at 44.0, down from 57.3 in June; production or sales at 46.7, down from 56.7; and delivery lead time at 55.9, down from June's 56.2.

MID-AMERICA STATES

ARKANSAS

The overall index, or leading economic indicator, for Arkansas slumped to 52.4 from June's healthy 59.7. Components of the index from the monthly survey of supply managers for July were new orders at 30.6, production or sales at 61.8, delivery lead time at 47.0, inventories at 52.0, and employment at 66.0. The drought

will push growth in the state lower in the months ahead, especially for firms with close ties to the state's large poultry industry. Except for Nebraska, no other state in the region depends more heavily on food processing to support growth than Arkansas. As a result, higher farm commodity prices in the months ahead will be a significant economic headwind for the state economy, but growth should remain positive but weaker.

IOWA

Iowa's July Business Conditions Index declined to 62.1 from June's 68.0. The overall index for the state has remained above growth neutral for the last 31 months. Components of the index for July were new orders at 65.0, production or sales at 62.4, delivery lead time at 50.4, employment at 72.8, and inventories at 60.1. I was very surprised to see the positive July readings for the state. I expect them to weaken significantly in the months ahead as the negative impacts from the drought winds through the economy. Food processing represents approximately one fourth of Iowa's manufacturing sector. It will be suffer from the higher farm commodity prices in the months ahead," said Goss. One supply manager said, "The drought is having minimal impacts on the biological vaccines at this time. If it continues it will (negatively) impact our business."

KANSAS

The Kansas Business Conditions Index for July slipped to 47.8 from June's 51.7. Components of the index from July's survey of supply managers in the state were new orders at 51.8, production or sales at 43.5, delivery lead time at 47.0, employment at 42.9, and inventories at 54.0. The USDA has declared almost 80 percent of the counties in Kansas as federal disaster areas as a result of the drought. Thus, not surprisingly, our July survey indicates that the drought is negatively affecting businesses with links to agriculture and food production in the state. I expect overall state growth to be flat to negative in the next three to six months.

MINNESOTA

The July Minnesota Business Conditions Index sank below growth neutral for the first time in almost three years. The index, based on a survey of supply managers in the state, declined to 45.6 from June's much stronger 58.6. Components of the index from the July survey were new orders at 34.7, production or sales at 42.3, delivery lead time at 65.4, inventories at 35.7, and employment at 50.1. The downturn in export orders weighed more heavily on the Minnesota economy for July than the drought. The global economic slowdown combined with the rising value of the dollar pulled the overall index below growth neutral for the month. I expect state growth to be flat to slightly negative in the next three to six months.

MISSOURI

The July Missouri Business Conditions Index was slightly above growth neutral for the month even though it plunged to a tepid 50.2 from June's 59.1. Components of July's Business Conditions Index were new orders at 45.4, production or sales at 47.0, delivery lead time at 60.6, inventories at 45.4, and employment at 52.9. One supply manager reported the shutdown of auto plants for July vacations pushed growth lower. The purchaser expects to see production increases for August and September. On the other hand, the drought is having a very significant and negative impact on businesses that we survey with links to agriculture. Food processors in the state which account for more than one of six manufacturing jobs will be negatively affected as higher input prices force cutbacks later in the year.

NEBRASKA

For the first time since October 2010 the Business Conditions Index for Nebraska declined below growth neutral 50.0. The index from a survey of supply manager in the state slumped to 48.3 from 54.5 in June. Components of the index were new orders at 46.0, production or sales at 47.9, delivery lead time at 51.9, inventories at 48.0, and employment at 47.9. As stated by one supply manager, I believe the drought will have a significant impact on Nebraska and surrounding states. I pray that 2013 returns to normal rainfall." As a share of the state economy, no other state in the region depends more heavily on livestock production and food processing. "Both of these will be negatively impacted by drought. We are already detecting significant and negative impacts in our monthly surveys from the drought. I expect those negative impacts to grow in the months ahead with consequent pullbacks in the Nebraska economy, at least in the short run.

NORTH DAKOTA

The leading economic indicator for North Dakota declined to a still healthy reading for July. The Business Conditions Index dipped to 56.5 from 63.0 in June. Components of the overall index for July were new orders at 58.7, production or sales at 57.3, delivery lead time at 56.8, employment at 59.3, and inventories at 50.3. While the impacts from the drought are not as severe in North Dakota, they are nonetheless affecting the state economy. In addition to businesses tied to agriculture and food production, shortages of water are negatively affecting energy production in the state. While I do expect positive growth for the state in the months ahead, it will clearly be slower.

OKLAHOMA

The Business Conditions Index for Oklahoma slumped to 52.7 from 56.8 in June. Components of the leading economic indicator for the July survey of supply managers in the state were new orders at 56.6, production or sales at 51.5, delivery lead time at 53.2, inventories at 50.1, and employment at 52.3. With drought conditions in all of the state's 77 counties, it was not surprising to measure a decline in Oklahoma's leading economic indicator. With feed costs rising, livestock producers in the state are selling off their herds. Thus, businesses linked to agriculture, especially livestock where there is not crop insurance, will experience slower to no growth in the months ahead. I do expect Oklahoma's growth to remain positive but much slower in the months ahead.

SOUTH DAKOTA

The leading economic indicator for South Dakota declined below growth neutral for July. The Business Conditions Index from a survey of supply managers in the state declined to 46.0 from June's 52.1 and May's much stronger 62.4. Components of the index for July were new orders at 41.6, production or sales at 44.4, delivery lead time at 49.7, inventories at 48.1, and employment at 46.3. The drought is having a substantial and negative impact on the state's economy. Based on our survey, the impact will pull growth into negative territory in the months ahead. While crop insurance will soften the impacts on crop farming, livestock producers and businesses tied to this important state sector will suffer in the months ahead. For example, food processing accounts for almost one out of every six manufacturing jobs in the state. This industry will experience negative impacts from higher input costs resulting from the drought.

THE BULLISH NEWS

- The U.S. economy added 163,000 jobs in July. Not enough to keep unemployment from rising to 8.3% but better than expected.
- The Case-Shiller home price index rose 2.2% from April. This was the largest one-month increase in 12 years of the 20-city index.

- Energy price growth continues to moderate.

THE BEARISH NEWS

- U.S. Gross Domestic Product growth for the second quarter of 2012 (annualized and seasonally adjust) was 1.5%. Growth should be more than triple this in the so-called recovery.

- National and Creighton's regional PMIs (leading economic indicators) dropped below growth neutral. Both are indicating slow to NO growth for the next 3-6 months.

- U.S. retail sales growth has been virtually flat for the last two months.

WHAT TO WATCH

- PMI's: On Sept. 4, Creighton's releases its regional leading economic indicators (PMIs) and the national Institute for Supply Management releases its national PMI. I cannot overemphasize the importance of this data. They are the first economic releases for September. Further declines in the overall PMI will be very bearish for the U.S. economy.

- Jobs: On Friday September 7, the U.S. Bureau of Labor Statistics (BLS) will release the employment report for August. Another semi-strong employment reading (above 150,000 jobs added) will be bullish for equity markets and the U.S. economy.

- Retail Sales: On August 14, the U.S. Census Bureau releases its retail sales data for July. The last two months have been awful. Growth from June that is flat or negative will be the first solid indicator of a significantly higher risk of a recession.

THE OUTLOOK

FROM GOSS:

- The risk of a 2013 recession has risen from 20% to 35% over the past three months.

- There will be another European economic eruption in the next 30 days pushing the European Central Bank to open the "money" spigot. What they need is substantial economic restructuring, not more Euros.

- Third quarter GDP growth will be less than 1% as economic uncertainty rises as we approach the "fiscal cliff."

OTHER FORCASTS:

- The National Association of Business Economics (NABE) (July 2012): "The July survey results suggest that the increase in sales experienced earlier in the year may have been short-lived. Fewer panelists in the July survey (39%) reported rising sales than in the April survey, in which 60% of panelists reported rising sales. The survey suggests fewer capital spending increases and panelists continue to forecast stability in capital spending over the next 12 months. NABE panelists express significant concerns about the impact on their sales if Bush-era tax cuts expire in late December and the automatic government spending cuts take place in early January. Indeed, 65% of the panelists expect sales to fall under this scenario, while 30% of the panelists expect that sales would stay the same.

- "Collaborating with the Competition," Mary Siegfried, Inside Supply Management," March 2012, P. 20. Horizontal collaboration allows companies in the same industry to share resources for cost savings and improved customer service. With ever-changing business challenges such as transportation costs, volatile demand and an evolving customer base, supply management organizations are exploring new and unique ways to use collaboration in their supply chains. One such effort is turning traditional vertical collaboration strategies on their side and may change the way organizations view their supply chain — and their competitors. http://www.ism.ws/pubs/ISMMag/ismarticle.cfm?ItemNumber=22235

Goss Eggs (Recent Dumb Economic Moves)

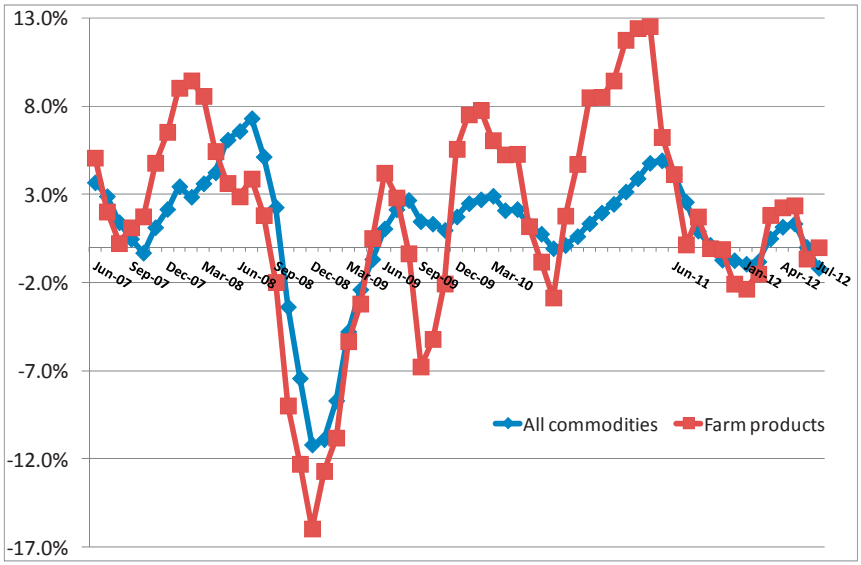
- Both the Republican House and the Democrat Senate wasted ink, time and money by passing different versions of the extension of the "Bush" tax cuts. Nothing is going to happen regarding the "fiscal cliff" until after the elections in November. The fiscal cliff slated for January 2013 will usher in a record increase in taxes for all and $110 billion in spending cuts.

Survey results for August will be released September 4.
Follow Goss on twitter at http://twitter.com/erniegoss
For historical data and forecasts visit our website at:
http://www2.creighton.edu/business/economicoutlook/

PRICE DATA

ALL COMMODITIES/FARM PRODUCTS 2007-2012
FUELS & RELATED/METALS & METAL PRODUCTS

Price changes, 3 month moving average, 2007-2012



Price changes, 3 month moving average, 2007-2012