IAR'S INLAND EMPIRE REPORT ON BUSINESS
Prepared by: The Institute of Applied Research

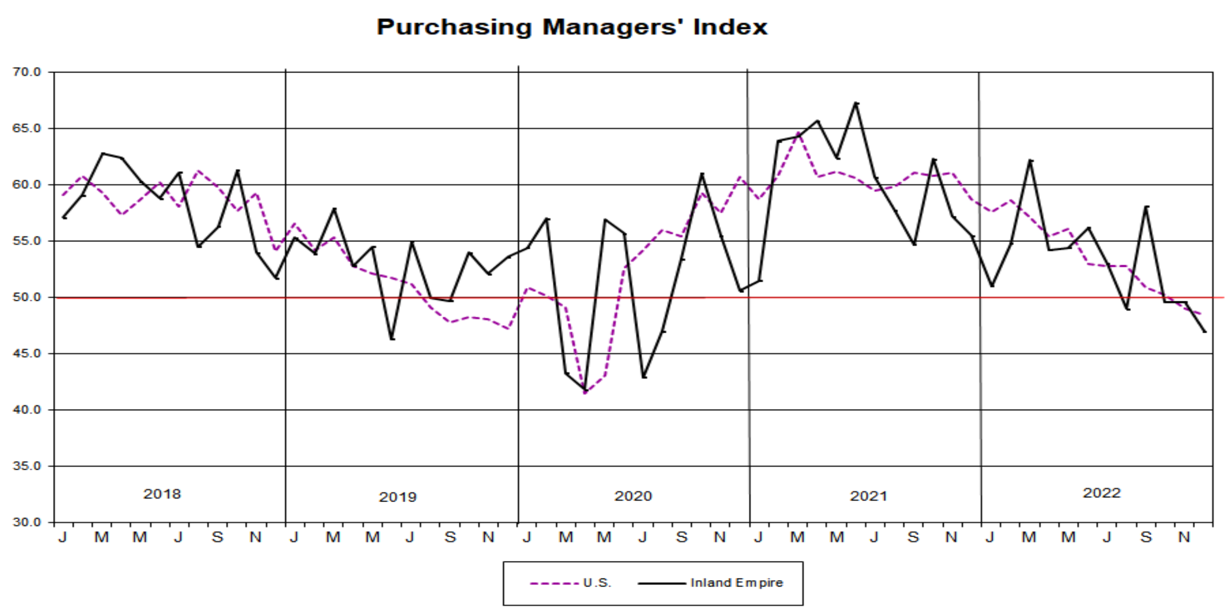
Housed in CSUSB's Jack H. Brown College of Business and Public Administration

Report for December 2022

Sponsors: ***San Bernardino County Economic Development Agency***
Riverside County Office of Economic Development

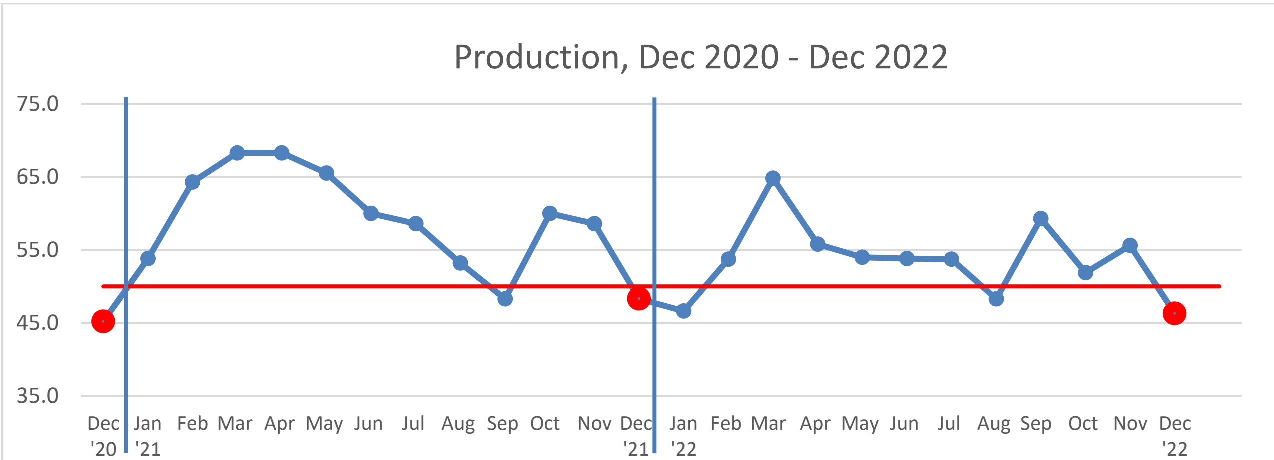
INLAND EMPIRE PMI REGISTERED BELOW 50 FOR THE THIRD MONTH

According to Dr. Barbara Sirotnik (Director, Institute of Applied Research) and Lori Aldana (Project Specialist, Institute of Applied Research), "This month's Inland Empire **Purchasing Managers' Index (PMI)** registered **47.0,** a drop from last month's 49.6. It takes three consecutive months of figures below 50 to establish a new trend. Since this is the third month in a row below the baseline of 50, December's number reflects a new trend of decline in the Inland Empire's manufacturing sector. We note that the National report prepared by the Institute for Supply Management also showed a drop in its PMI, changing from 49.0 in November to 48.4 in December. But since the national data have only been below 50 for two consecutive months, a new trend of decline has not yet been established for the U.S. manufacturing sector.



Source of U.S. PMI®: Institute for Supply Management®, Source of IE PMI®: Institute of Applied Research

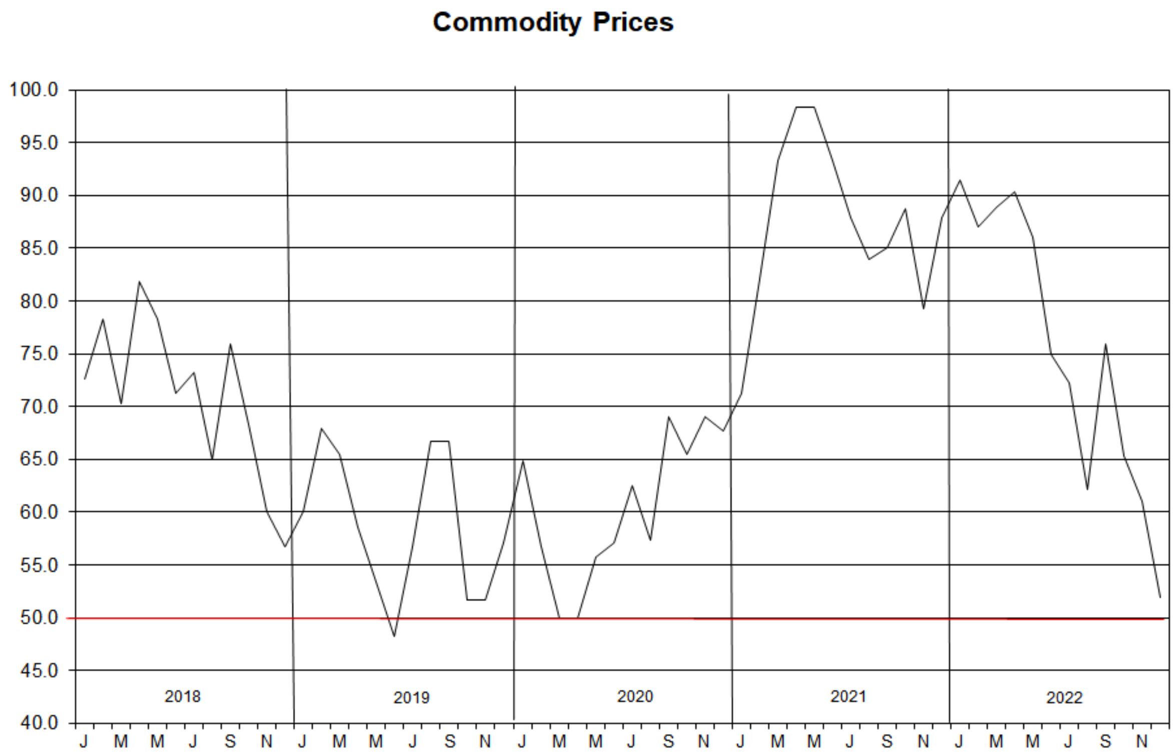
The **Production Index** (one of the two key components of the PMI) registered a big drop from last month's 55.6 to **46.3** this month. This is not necessarily a cause for concern. As seen in the graph below, December production figures (the red dots) tend to drop below the 50.0 benchmark as production decreases during the holiday season.



The **New Orders Index** (the other key component of the PMI) also registered **46.3** this month. The "bad news" is that it means new orders have slowed, but the "good news" is that the index showed a significant increase from last month's 37.0. As noted by one of our panelists: "Sales orders have slowed since mid-November, but I do believe orders will bounce back in January."

The **Employment Index** remained unchanged from last month's **48.1**, indicating that employment is continuing to decrease somewhat, at the same rate as last month. Some panelists were positive about the employment picture, making comments such as: "Keeping good employee and revenue counts." Other panelists made negative comments such as the following: "We are still having to send employees home when there is no work which is affecting morale especially at holiday time," and "Finding new employees is still an issue."

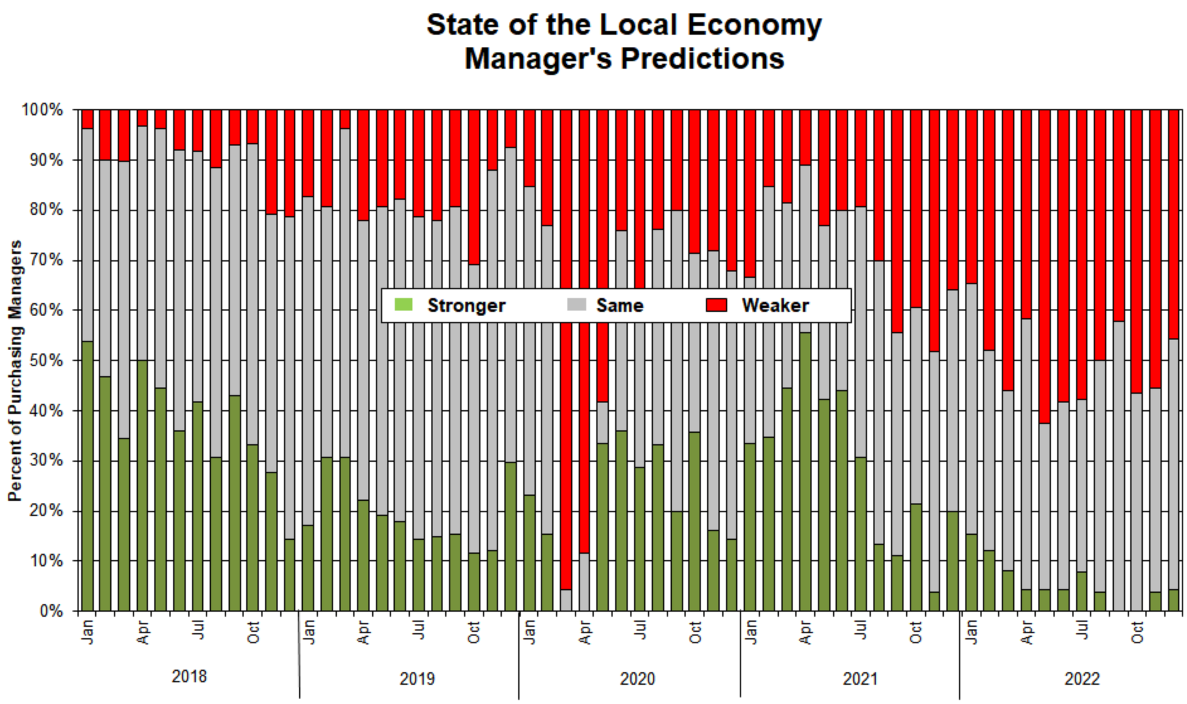
The **Commodity Price Index** for the Inland Empire declined from last month's 61.1 to **51.9** this month. This is the lowest figure since April of 2020. As noted by one of the panelists: "We have seen some downward movement in material pricing." And one said: We think inflation will flatten by 2nd quarter 2023 for our raw materials. We had to increase prices by 10% for 2023." It is possible that falling demand for goods, an easing of supply chain issues, and the Fed raising its key interest rate by half-point in December, are all helping to alleviate inflationary pressures.



The **Supplier Deliveries Index** is a measure of the speed of supplier deliveries, with numbers above 50 indicating *slower* deliveries. The index decreased from 55.6 last month to **53.7** this month, indicating that the rate of slowing has decreased slightly. One comment made, "Old open orders are shipping at faster rates now. Suppliers are catching up with orders faster." That comment is confirmed by remembering that a year ago, over a hundred freighters were lingering off the California coast waiting to be unloaded at the ports of Los Angeles and Long Beach, whereas this year that is not the case.

The **overall Inventory level** (units, not dollars) including raw, MRO (Maintenance, Repair, Operating), intermediates, etc. registered at **40.7**, a significant decrease from last month's 51.9 (perhaps because raw materials required to produce holiday goods have depleted inventory). Although **29.6%** of panelists (up from last month's 22.2**%**) indicated that their **inventory level of finished goods** has *decreased* (meaning sales were "good" and they were able to clear out inventory), the majority (**55.6%** down from last month's 59.3%) reported that their inventory level of finished goods is the same as the previous month (meaning that production of finished goods is "staying even" with sales). Only **14.8%** (down from last month's 18.5%) reported that the level of finished goods has increased.

The past several months we commented that "optimistic" is not the word we would use when it comes to our panelists' evaluation of the state of the local economy for the coming quarter. That continues to be the case. Only **4%** stated they believe the next quarter's economy will be stronger (the same figure as last month). Less than half (**46%**, slightly down from last month's 50%) believe that the local economy will become weaker in the coming quarter, and the remaining **50%** (up from last month's 41%) believe that the next quarter's economy will continue to be "the same" as it has been (where "same" means an economy struggling to return to pre-pandemic levels).



Following is a summary of the figures shown in this month's report:

December 2022 Business Survey at a Glance					
	Series Index		Direction from 50	Rate of Change from Last Index	Trend Months
	Last Month	This Month			
Local PMI	49.6	47.0	Contracting	Faster	3
Commodity Prices	61.1	51.9	Increasing	Slower	42
Production	55.6	46.3	Contracting	From Growing	1
New Orders	37.0	46.3	Contracting	Slower	3
Inventory	51.9	40.7	Decreasing	From Increasing	1
Employment	48.1	48.1	Contracting	Unchanged	2
Supplier Deliveries	55.6	53.7	Slowing	Slower	39
Purchasing Managers' Confidence in the State of the Local Economy					
% Stronger	4%	4%			
% Same	41%	50%			
% Weaker	55%	46%			

Our survey always includes an overall question asking the panelists to give general remarks regarding any business condition (local, national, or international) that affects the purchasing operation or the outlook of their company or industry. Positive to mixed remarks included:

- “December was more of the ‘business as usual’ that we have seen the second half of 2022. It was not quite as hectic as the first half of the year but still at levels above 2021. From what we can tell given the outlook from our customers, business should remain at this level for at least the first half of 2023. Our suppliers are only slightly better at getting us the material we need. So, we will continue to place extra orders knowing that they will be late in everything that they eventually deliver.”
- “I do believe orders will bounce back in January.”
- “New orders are brisk which is unusual this time of year. We have also seen some downward movement in material pricing. Cost of Labor and finding new employees still an issue. We start lowering our inventory about the middle of November only keeping a level to keep our customers out of trouble.”
- “Old open orders are shipping at faster rates now. Suppliers are catching up with orders faster.”
- “Outlook is good as infrastructure projects need to get done.”
- “Things seem to be staying steady. We are actually now busier than we usually are this time of year. 2023 may be a good year after all. We ended up doing more business in 2022 than we expected.”
- "We think inflation will flatten by 2nd quarter 2023, for our raw materials. We had to increase prices by 10% for 2023."

Some comments, however, were cautionary/negative:

- "Fears of a recession looming. Low season for our business."
- “No imports coming in.”
- “Sales orders slowing since mid-November.”
- “Slow”
- “We have had some supply chain issues with one of our main suppliers which has caused a factory slow down, coupled with orders still not quite where they need to be. We are still having to send employees home when there is no work which is affecting morale especially at holiday time.”

Special question: This month we asked an open-ended “special question” regarding changes over the past year and panelists’ perspectives on the future: “*Finally, since this is the LAST survey of the year, please step back and give us your perspective on changes you’ve seen in Inland Empire’s manufacturing sector and the economy over the past year. Also, do you see any “clouds on the horizon” for the economy in 2023, or do you see clear skies ahead?*” Following are the **optimistic** comments:

- “2022 was a record year for our company. Overall sales were up nearly 30%. This is unusual with previous years in the 10% range. There are still issues with some types of polymers being very scarce, but overall the majority of materials have been easier to acquire. Though the last 45 days have slowed, our feeling is January will be busy again. There are some changes occurring in our industry that should push more business our direction. 2023 looks to be very promising."

- "2023 looks promising in our line of business."
- "Our company is actually optimistic for 2023! We understand that 2022 had its challenges with supply chain issues, global economy problems and leftover Covid residual effects, so in the latter half of 2022 we started to focus on new business partnerships/opportunities that could change our trajectory and start off the new year strong. We feel that the supply chain issues, for the most part, are now over and with the new leads we have generated, coupled with reinforcing our current business partnerships; we will have a strong Q1 which should set us up for a good year!"
- "This last year has been our best year ever with over a 35% increase from 2022 revenue. I have not seen any clouds forming yet, and hope they stay away while the IE continues to grow."
- "It is hard to tell what the local manufacturing scene will look like in 2023. From a more state or country level, it appears that it is mostly sunny out there. Obviously home builders are going to have a rough go of it in 2023. Those in the aerospace, defense, auto, semiconductor, medical and the general manufacturing sector all look to be very positive for the next 12 months. Maybe not all of them will be at all-time highs, but inventories are still low, so they are all still buying product at above average levels. We still are looking to hire more workers (we have added three in the past three months) and I am not curtailing my purchasing of inventory."

Unfortunately, some of the panelists made comments reflecting business difficulties:

- "Economy will slow."
- "The economy this year has been difficult for our company and our customers. It is especially difficult for us because we are in California competing with companies outside of the state with much lower costs for labor. California needs to ease up on manufacturers if they want us to stay here. I have two companies outside the state trying to buy us and move the company. We have not made a decision yet. As far as 2023, I am actually cautiously optimistic if we decide to stay. We have changed up some of our processes, made some management changes and gained new customers this year. We hope these changes will allow us to increase our profits next year."
- "We expect the 1st quarter of 2023 to dip into a recession. If not, then by the 2nd qtr. We do not see clear skies ahead."
- "We have hope that the inflation will moderate. Transportation costs are hurting everyone, and this relates back to the price of diesel. The best that could happen is a leveling of inflation."
- "We haven't seen much change over the past year. The economy is like a rollercoaster, we seen some costs go up and now they are a little stable but for

how long? I do see some clouds and I hope I'm wrong. I think we're going to see raw materials harder to get in the summertime."

- "We see it cloudy with fears of a recession."

In summary, the PMI remained below 50 for the third month in a row, officially indicating that the manufacturing sector is in decline. If that trend continues, it could portend an economic downturn in 2023. But two panelists put these data into a more positive perspective:

- "*I don't see clear skies, but I also don't see a large funnel cloud steamrolling towards us. I think that there are still challenges to be overcome, but, if we keep it together, and move forward, the economy will be improving in 2023*."
- "*As we close the year realizing our highest sales and profitability since the founding of our company over 46 years ago, we continue to observe the general economic trends. We do see impact on us and our industry of higher prices, a diminishment on off-shored products from China, supply chain challenges, workforce limitations, but we also see the validity of having pursued a course of self-dependence with minimum reliance on outside sources to meet our basic needs to manage our company. Without question there have been and continue to be risks that impact us and the markets we serve, but our diversification and self-reliance for our basic needs to manage our company have reduced those risks and contribute to the results we have achieved this year and we expect for the future*."

We will continue to track the opinions of our business leaders over the coming months.

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