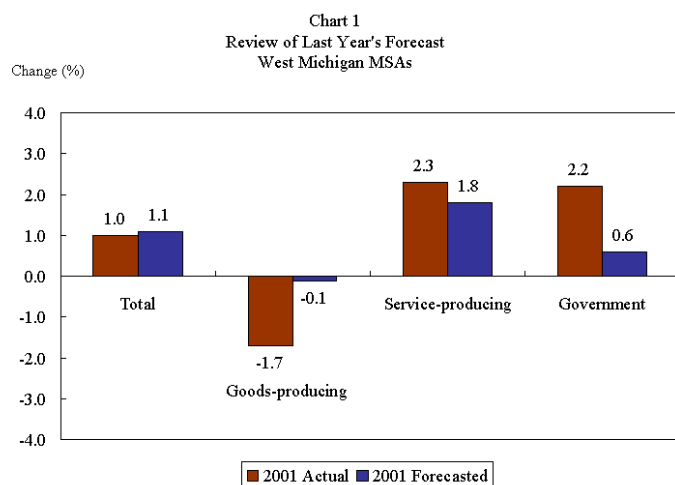


WEST MICHIGAN VIEWPOINT

West Michigan Economic Outlook for 2002 and 2003

A Recession That Wasn't?

With gross domestic product (GDP) posting a 1.4 percent annualized gain in the final quarter of 2001, some forecasters are predicting that the worst is over and that we experienced a mild, one-quarter downturn. In fact, some are arguing that the current slowdown does not constitute a true recession since it did not span two quarters. Still, for the west Michigan area and the Great Lakes states, the current slowdown continues to generate severe recession-like conditions. This is especially the case regarding the area's furniture industry, as well as automotive suppliers.



Moreover, the national economy must still overcome several major challenges in the coming months before the tiny fourth-quarter improvement can be heralded as the start of the next expansion. These challenges include sluggish international markets, excess capacity across manufacturing industries, debt-ridden consumers, and a continued but diminishing sense of uncertainty triggered by the September 11 terrorist attacks. Although most forecasters firmly believe an economic recovery will occur in 2002, the timing is still in debate. While the most optimistic forecasters believe we are already there, the most pessimistic forecasters fret that the first quarter could still dip into negative territory and that a full recovery will not take hold until summer.

Before turning to our forecast for the metropolitan areas of west Michigan for 2002 and 2003, it has always been our tradition to review our past performance, give our national forecast, and highlight the local factors that we account for in making our forecast.

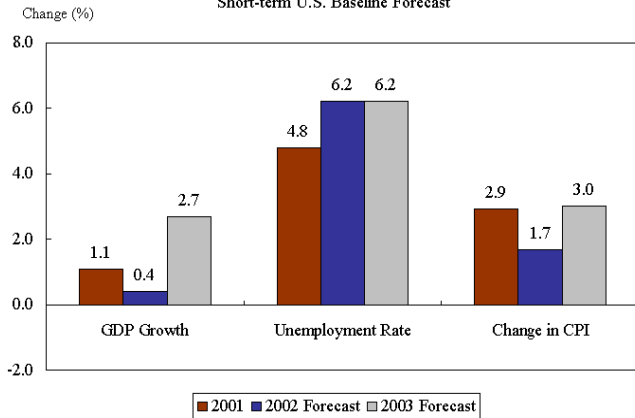
Revisiting Last Year's Forecast

Our overall forecast for employment growth in 2001 for the three metropolitan areas in west Michigan was right on target; however, it was due only to major offsetting errors. Employment in the three metropolitan areas of west Michigan rose 1.0 percent, and we had predicted 1.1 percent. However, as shown in Chart 1 and Table 1, we had forecast goods-producing employment to decline by only 0.1 percent, and it fell by 1.7 percent. Our overly optimistic employment forecast for goods-producing employment offset our underestimation of service-producing and government employment. A look at our individual metropolitan forecasts also reveals that we, to put it simply, were seriously off the mark.

Table 1
Review of Last Year's Employment Forecast

	% Change		
	Actual	Forecast	Error
Benton Harbor MSA			
Total	1.0	1.0	0.0
Goods-producing	-1.8	-0.2	-1.6
Service-producing	2.1	1.7	0.4
Government	2.5	0.1	2.4
Grand Rapids-Muskegon-Holland MSA			
Total	1.0	1.6	-0.6
Goods-producing	-2.0	0.7	-2.7
Service-producing	2.4	2.0	0.4
Government	2.4	0.8	1.6
Kalamazoo-Battle Creek MSA			
Total	1.1	0.5	1.6
Goods-producing	-0.7	-2.5	1.8
Service-producing	1.8	1.1	0.7
Government	1.6	0.4	1.2
West Michigan			
Total	1.0	1.1	-0.1
Goods-producing	-1.7	-0.1	-1.6
Service-producing	2.3	1.8	0.5
Government	2.2	0.6	1.6

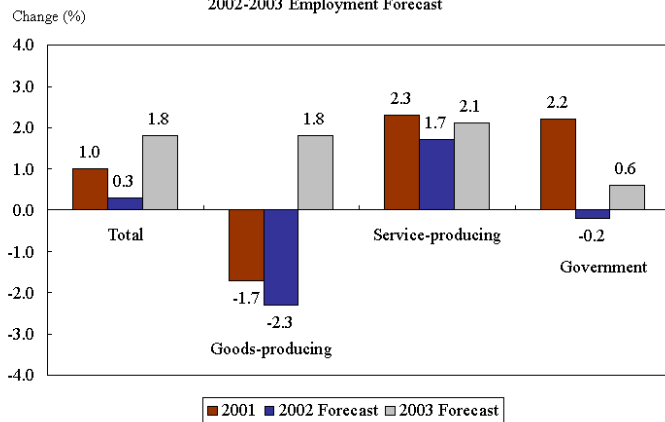
Chart 2
Short-term U.S. Baseline Forecast



SOURCE: University of Michigan

What happened, and what can we learn from our mistakes? The major reason for our regional forecasting errors is that our national forecast, which drives our regional model, was simply too bullish. We did not expect that 2001 would generate such harsh conditions for our manufacturers. This is especially the case for the office furniture industry. The sole exception was in our forecast of the Kalamazoo-Battle Creek MSA, where we believed that December 2000 layoffs in the area's cereal industry, coupled with expected layoffs in the area's paper industry, would send the MSA's employment in its goods-producing sector down by 2.5 percent. Instead, the sector's employment fell only 0.7 percent.

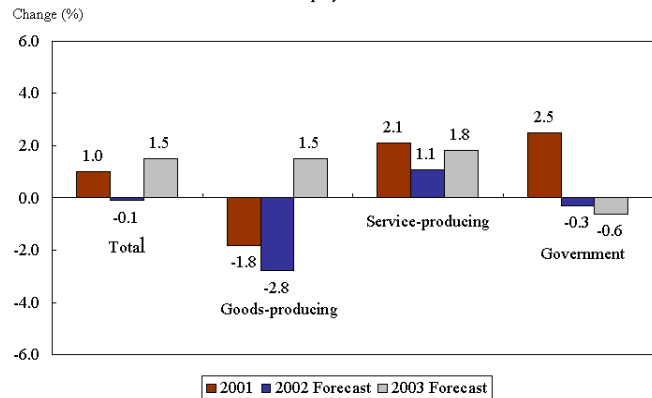
Chart 3
West Michigan
2002-2003 Employment Forecast



The second source of error in our forecast is more troubling: we underestimated the strength of the area's service-producing sector. The traditional regional model, which subordinates a large percentage of a region's service-producing sector to its manufacturing export base, is becoming less useful. The area's service-producing sector has a life of

its own and may have been influenced by the region's strong-performing government sector, which was clearly the source of our third error. Driven by surprisingly strong employment growth in public education, government employment significantly exceeded our forecast in all three metropolitan areas.

Chart 4
Benton Harbor MSA
2002-2003 Employment Forecast

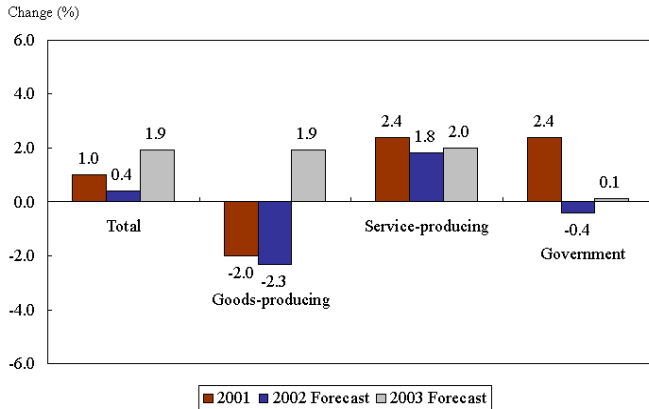


National and State Outlook

This year we selected the University of Michigan's national forecast, released in November, to power our regional model of west Michigan. It's major predictions are highlighted in Chart 2. It calls for GDP to grow only 0.4 percent in 2002 and by 2.7 percent as the economy rebounds in 2003. The forecast also calls for growth to be near zero in the current first quarter and then increase throughout the year, hitting a 2.7 percent annualized rate in the final quarter. Unemployment is expected to reach 6.2 percent this year and stay there in 2003, as productivity gains, coupled with employers' attempts to limit their labor costs, will hold employment back for the year. Consumer prices are expected to be stable in 2002. Our forecast for auto sales, a key factor in forecasting growth in any part of Michigan, is not shown in the chart. We call for car and light truck sales to reach 15.6 million units for the year, a good year historically, but far short of last year's stellar performance of 17.1 million units.

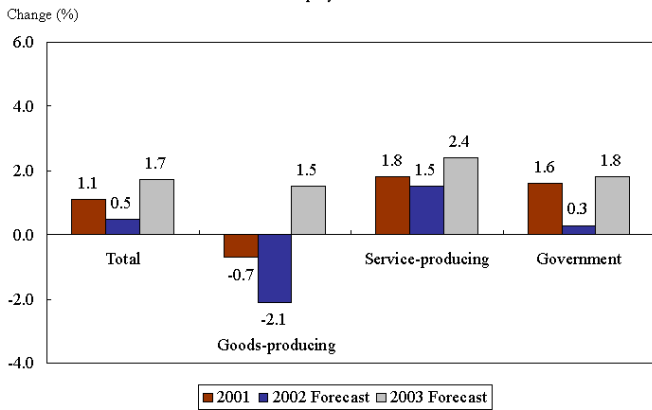
The University of Michigan forecast is a cautious one. In comparison, the current Federal Reserve Bank of Philadelphia consensus forecast, which is based on a survey of 35 leading business forecasters, predicted that GDP will increase to 1.4 percent and that the nation's unemployment rate will climb to 6.0 percent.

Chart 5
Grand Rapids-Muskegon-Holland MSA
2002-2003 Employment Forecast



While we do not incorporate a state forecast into our model of west Michigan, it is important to consider what forecasters are predicting for the state. In November, the University of Michigan predicted that employment in the state would decline by 0.3 percent in 2002 before climbing by 1.3 percent in 2003. Goods-producing employment is forecast to drop by 3.4 percent in 2002, while private service-producing and government would post employment gains of 1.6 percent each.

Chart 6
Kalamazoo-Battle Creek MSA
2002-2003 Employment Forecast



West Michigan 2002 and 2003 Forecast

In preparing this year’s forecast, we took into consideration the following developments:

- isolated employment reductions in the region’s large auto supplier base
- major employment reductions in the area’s office furniture industry, and
- government employment remaining in check due to the state’s severe budgetary constraints.

As was the case last year, our forecast was much improved by four focus group sessions held in Battle Creek, Grand Rapids, Muskegon, and, new this year, Holland. We greatly appreciate the assistance of the region’s economic development organizations in these efforts.

We forecast employment to increase only 0.3 percent in 2002 and then to rebound 1.8 percent in 2003. Cutbacks in the area’s furniture industry, coupled with more modest employment declines in the region’s auto suppliers, will push goods-producing employment down by 2.3 percent in 2003. Government employment is expected to be off by 0.2 percent in the year, as the budget problems in Lansing filter through local governments and local state service providers, including area schools. Pulled down by the sluggish conditions in the region’s manufacturing and government sectors, employment in the service-producing sector is forecast to increase by 1.7 percent in 2002. Forecasts for each of the three metropolitan areas are shown in Charts 4 through 6.

Concluding Thoughts

Forecasters are notoriously bad at predicting turning points, and 2001 proved to be no exception. Looking solely into the past, it is difficult to see the curves of the future. As we concluded last year, “Economists are often the last to know when an economy turns.” This is especially true when the traditional road signs point in the wrong direction. Car sales are not supposed to reach 17 million in a recession year, and, according to historical trends, the national economy should have responded more rapidly to the aggressive actions of the Federal Reserve Bank.

When we look back on 2001, the horrors of September 11 will, of course, quickly come to mind. The tragic events of that day did not cause the current economic slowdown, and the resiliency of the American people never allowed it to impart further hardship to the U.S. economy.