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Public Sector Reports

ECONOMIC FORECAST

This forecast provides an overview of the current United States and Michigan economies, examines national activity and policy, discusses several sectors of the Michigan economy, and provides a 1988 outlook for the national and state economies. A glossary of some of the terms used in this forecast appears on page 2.

OVERVIEW

National economic growth (GNP) during the third quarter (July, August, September) was a healthy 4.1 percent, well above the second-quarter growth of 2.5 percent. The October numbers on national employment and industrial production suggest that the fourth quarter also will be good. For 1987 as a whole, GNP growth is expected to average 2.9 percent above the 1986 level. Although the full effect of the turbulence on Wall Street has not yet been felt in the economy, some repercussions are likely in 1988.

For Michigan, economic growth has been anemic this year despite substantial employment gains in some industries. Continuing cutbacks in vehicle production nationally have meant a loss of high-paying automotive jobs here; employment in Michigan's automotive sector has been declining since the last quarter of 1985. Thus, although Michigan employment is expected to be up about 4 percent in 1987, well above the 2.6 percent national figure, much of the gain has been in lower-paying, nonautomotive jobs.

NATIONAL ECONOMY

The healthy 4.1 percent GNP growth in the third quarter was propelled by increases in investment, government spending, and the sale of durable goods. Producers' investment in equipment rose at an annual rate of 25 percent. Gross private investment in nonresidential structures also posted a substantial gain, 21 percent above the second quarter. These significant investment increases are indicators of future improvements in productivity. Consumer purchases of durable goods increased 22 percent; this large gain reflects continued consumer confidence in the market. These positive contributions to the national economy were dampened by negative activity that kept the economy from growing faster: an increase in the trade deficit, a decline in consumer purchases of nondurable goods, a decline in federal nondefense spending, and a sharp reduction in the rate of inventory accumulation.

Modest GNP growth during the third quarter kept prices down, and the national rate of inflation declined for the second consecutive quarter. For 1987 as a whole, the inflation rate, as measured by the implicit price deflator for GNP, will be about 3 percent. That figure compares with 2.6 percent for 1986 and 3.2 percent for 1985. (See Exhibit 1.)

In the fourth quarter, early indicators suggest robust growth despite the recent record stock market losses. October gains in manufacturing and services employment were pronounced; industrial production surged as well, reflecting growth in exports and resulting in large backlogs in orders. The crash on Wall Street signifies basic problems in the U.S. economy, but it alone was unable to derail the economic momentum of 1987.

International Trade

Americans like foreign goods and services. Imports as a share of total U.S. consumption increased from 10 percent in 1970 to 16.4 percent in 1984 and to about 22 percent in 1987. Unfortunately, as producers, we have not been able to balance our imports with sufficient exports of goods and services to pay for them. The trade gap has climbed from $6.2 billion to $108.6 billion since 1983.

America's appetite for imported **goods** has sent the volume of imported durables from $147 billion in 1983 to more than $250 billion (annual rate) during the second quarter of this year. The value of automotive imports has almost doubled since 1985, rising from $43.5 billion in the second quarter of 1985 to $84 billion in the second quarter of this year. One bright spot in the balance-of-trade picture is petroleum imports, which have declined; the second-quarter 1987 figure was $38.2 billion compared to $55 billion in the same quarter in 1983.

Imports of **services** (travel, transportation, and payments for the use of foreign capital, labor, and land) increased from $87.4 billion in 1983 to $127.3 billion in the second quarter of 1987. Government interest payments to foreigners increased from $17.8 billion in 1983 to $25.6 billion this year.

In the years ahead, this country will find it increasingly difficult simply to pay interest on debt held by foreigners, let alone close the trade gap. The realization of this grim fact may have contributed to the bust on Wall Street.

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The U.S. trade deficit will probably be helped by expansionary foreign monetary policy. Most capitalist governments fear an international recession in the wake of unsteady financial conditions around the world and are trying to coordinate easier money policies. Easier money overseas will increase demand for American goods in foreign markets. American policymakers are also arguing in favor of more stimulative fiscal policies in countries such as Germany and Japan to increase the demand for U.S. exports.

The U.S. trade balance likely will improve if the United States-Canada Trade Agreement is ratified by Parliament and Congress. The agreement will eliminate many trade protection barriers immediately and others gradually. The measure will create opportunity, especially for small, U.S. service businesses located near the border. Michigan is well situated to benefit from the agreement because our neighbor, Ontario, is the largest, most prosperous market in Canada.

The position of the United States as an exporter of vehicles is likely to improve during the 1990s because our new, efficient factories will help keep prices down relative to the cost of vehicles produced elsewhere. Chryslers, Cadillacs, Lincolns, Mazdas, and other Michigan-made vehicles will find increasing acceptance outside of North America because of cost, quality and styling, and a cheaper dollar.

The weaker dollar will sharply improve the merchandise trade balance in the months ahead, although some U.S. industries, such as consumer electronics, may not be able to respond quickly enough to meet the increased demand from abroad. This is because a number of U.S. industries have severely reduced their production capacity by outsourcing to foreign producers rather than producing their own components.

Monetary Policy

Until Black Monday in late October, Federal Reserve Board policy had been relatively conservative because of a concern about reigniting inflation. As a result, interest on three-month treasury bills had risen to nearly 7 percent by mid-October, from about 5.75 percent in July. After the crash, the board, fearful that a deep recession might be triggered by plunging stock prices, made considerably more money available. One result is lower interest rates. Fed policy seems likely to favor continued credit ease to assure growth in the months ahead. With the October decline in the producer price index, the Fed has room to maneuver without immediate fear of renewed inflation.

Worldwide, interest rates in most capitalist industrial nations have declined as a result of the response of central bankers to collapsed stock prices. Because the countries have acted in concert, the international pattern of investment flows in search of the best rates of return have not been altered much by changes in the stock market.

It seems worth recalling that high U.S. interest rates earlier in this decade were the initial cause of much of the global imbalance in trade flows. High returns on financial investment drew foreign capital into the United States, bidding up the dollar, thereby making U.S. goods higher priced elsewhere.

Fiscal Policy

Tax increases and spending reductions being worked out between Congress and the White House promise to pare the federal budget deficit by $25 billion to $35 billion during the current fiscal year. To restore confidence in the economy and keep interest rates down, Washington must further reduce expenditures and/or increase revenues so that the federal deficit reductions continue in future years.

The U.S. economy urgently needs redirection; our federal government's priorities must change. The pres-

GLOSSARY

Conference Board: A management information service for business executives that compiles data, conducts surveys and research, and analyzes trends.

Durable Goods: A product with an expected life of more than one year.

Gross National Product (GNP): The total market value of all final goods and services produced in the economy in one year.

GNP Implicit Price Deflator: A comprehensive index of inflation used to adjust earnings in both Michigan and the United States.

Index of Leading Indicators: Eleven categories of data compiled monthly by the Bureau of Economic Analysis in the U.S. Department of Commerce that are used to predict future economic activity.

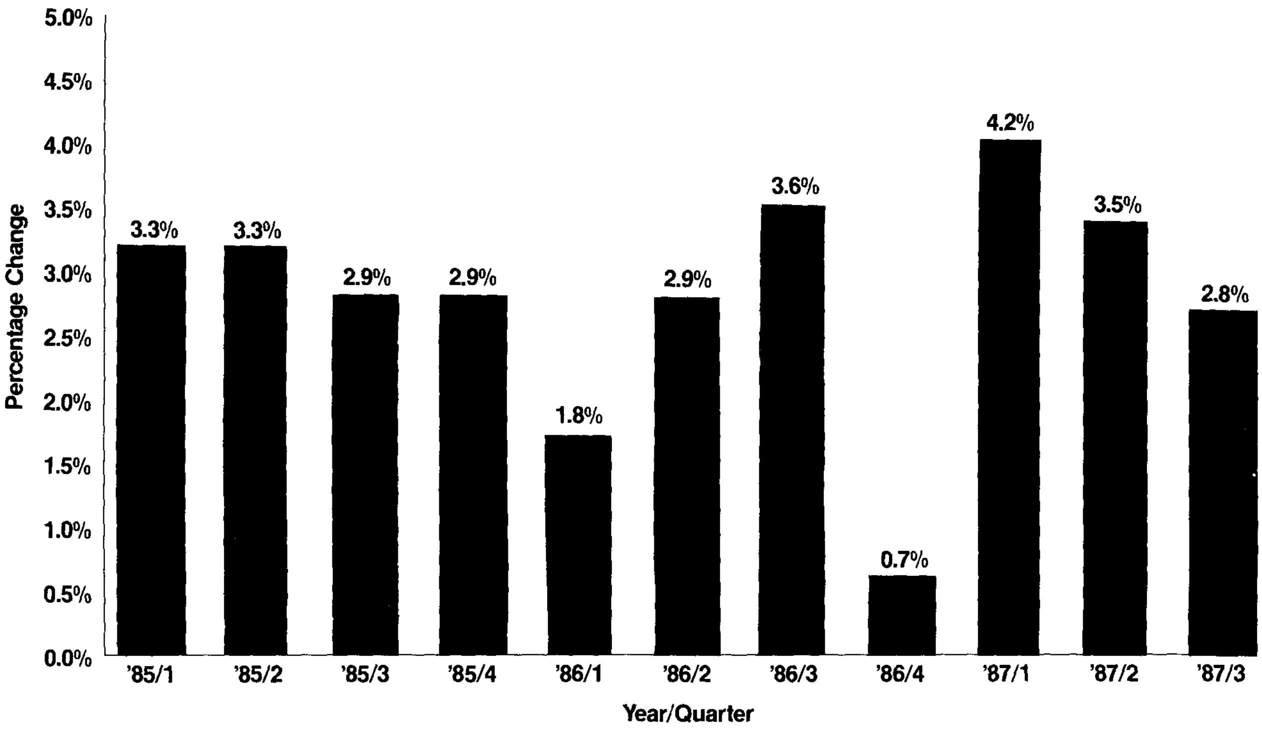
Outsourcing: Use of imported components in the production process.

Personal Income: Earnings, dividends, interest, rent, and transfer payments received by households.

Structural Adjustment: Changes in the labor intensity of production.

EXHIBIT 1

Percentage Change in GNP Implicit Price Deflator from the Preceding Quarter: First Quarter 1985 to Third Quarter 1987 (annual rates)



ent emphasis is on high levels of consumption and military spending; higher priority should be assigned to policies that encourage exports, domestic investment in human capital, spending for public infrastructure, and investment in producers' equipment. Foreigners, especially the Japanese and Germans, are reluctant to commit to stimulative domestic economic policies to boost U.S. exports to their countries until we reorder our own priorities. The November 7, 1987, *Economist*, a British publication, states:

> Every day that passes without some credible action to reduce America's budget deficit adds to the pressure.... Foreigners are shouting that they will not cover America's savings-investment gap by lending more of their own savings. Without a cut in the budget deficit, the gap will therefore have to be closed by something that reduces American investment. It is called a slump.

With the political gridlock in Washington, it seems unlikely that anything more than interim measures can be agreed upon; it will be left to the next administration and Congress to shape the mechanisms to pay for America's economic excesses of the 1980s.

Leading Indicators

The composite index of eleven leading economic indicators declined in October. This was the second straight drop, and the seventh during the past two and one-half years. If the index also declines in November, December, and January, it could portend a decline in national economic activity in the first or second quarter of 1988, perhaps even a recession.

In October, six of the eleven indicators were positive: more companies reported slow deliveries from vendors, initial claims for state unemployment insurance were down; orders for plant and equipment increased; the money supply grew; the length of the work week of production workers was up; and prices of materials sensitive to demand were higher. Negative indicators were drops in the index of 500 common stock prices listed on the New York Stock Exchange, manufacturers' orders for consumer goods and materials, and the number of new private housing units authorized by local building permits. The preliminary October figures for inventory change and the change in consumer and business borrowing were not available at this writing.

Investment

Although investment in nonresidential, privately owned structures posted a gain in the third quarter—the first since the fourth quarter of 1986—the figure still is well below the peak reached in the second quarter of 1985. The third-quarter level was $126.8 billion (1982 dollars, annualized), compared with $151.7 billion in early 1985.

Investment in producers' equipment reached a new high in the third quarter, standing at $337.4 billion, compared with $317.5 billion in the second quarter. The increase was caused by a rising level of exports coupled with increased domestic demand for goods produced here; this has increased the pressure on manufacturers to expand capacity. Recent analysis suggests there will be a 5 percent rise in capital spending this year by U.S. manufacturers and a 5 to 6 percent increase in 1988. The Conference Board recently reported that its second-quarter capital investment and appropriations survey of the 1,000 largest manufacturers

> confirms what we anticipated for almost a year—the manufacturing sector has finally gotten back on its feet. Almost all of the major indicators for the sector signal strength. One of the most encouraging signs is the recent growth in manufacturing employment, which suggests that manufacturers are confident that the recent pickup in activity will continue.
>
> The results of this survey and the high utilization rates in some industries suggest that capital spending may in fact be a major engine of growth for the U.S. economy in the final two quarters of this year and may sustain overall economic growth well into 1988.

Typically, Michigan is one of the top states in new manufacturing investment. The latest compilation puts us second, behind California. (See Exhibit 2.)

Income and Consumption

U.S. per capita real disposable income (in 1982 dollars) was $10,952 in 1986. This represents a gain of only 3.1 percent over the 1985 average of $10,622. Per capita real disposable income is expected to grow faster in the months ahead due to rising manufacturing employment and increasing exports.

Personal consumption expenditures grew by an inflation-adjusted 4.8 percent during the third quarter compared with a 1.9 percent gain during the second quarter and a -0.7 percent decline in the first. Third-quarter spending on consumer durable goods soared by 22.4 percent. The less volatile services component grew by 4.1 percent, while nondurable goods slipped by 1.2 percent.

The latest survey of consumer attitudes and buying plans conducted by The Conference Board prior to the October Wall Street debacle showed a significant increase in optimism. Consumers were especially ebullient in their plans to purchase vehicles and to take vacations. The momentum is expected to carry into the rest of the fourth quarter. According to a post-crash poll taken by the University of Michigan's Survey Research Center, the crash had a negative effect on consumers' expectations. How this will affect future behavior is not yet known, but consumers, especially stock market investors, seem likely to be more cautious in 1988 than they were prior to the stock market crash.

Vehicle sales data for November suggest a mood of restrained buying. Consumers, wary of economic uncertainty, are spending less, which will stimulate personal savings. Consumer durable goods purchases, especially of expensive automobiles, can be expected to decline.

MICHIGAN ECONOMY

Some sectors of the Michigan economy are performing well, others are suffering. Michigan's brightest sectors this year have been construction and associated industries. Housing as well as nonresidential construction have been growing rapidly with the result that finance, insurance, and real estate industries in the state have experienced good gains. Mining and government also are performing well. On the down side, Michigan's manufacturing sector has been severely affected by the cutbacks taking place nationally in vehicle manufacturing. Michigan wholesalers, transportation, and utilities companies that depend on the automotive industry also are performing poorly in comparison with the national industrial sectors. Agriculture and industries associated with farming also are depressed.

Michigan is not the only state experiencing a slow economy. The economies of many states in the Great Lakes, Plains, Southwest, and Rocky Mountain regions have been depressed by troubled farming, manufacturing, and mining sectors. (Among the Great Lakes states, Illinois experienced the slowest growth in the latest period followed by Indiana, Michigan, Ohio, and Wisconsin.) In contrast, New England, the Mideast, and the Far West economies have performed well.

EXHIBIT 2

Ranking of Top Dozen States in New Capital Expenditures By Manufacturers: 1983, 1984, and 1985

Rank	State	Value of New Capital Investments, 1983	State	Value of New Capital Investments, 1984	State	Value of New Capital Investments, 1985
1	California	$6,932.4	California	$8,757.1	California	$9,157.8
2	Texas	5,429.4	Texas	5,606.6	**Michigan**	**5,718.6**
3	New York	3,545.6	New York	4,342.3	Texas	5,634.4
4	Ohio	3,132.2	**Michigan**	**4,239.2**	Ohio	5,061.2
5	Pennsylvania	2,998.3	Ohio	3,979.6	New York	4,845.5
6	Illinois	2,935.7	Pennsylvania	3,557.6	Illinois	4,069.0
7	**Michigan**	**2,546.8**	Illinois	3,363.9	Pennsylvania	3,987.6
8	North Carolina	2,419.1	North Carolina	3,114.3	North Carolina	3,221.2
9	Indiana	2,069.5	Indiana	2,627.9	Indiana	3,141.8
10	Louisiana	2,035.4	North Dakota	2,286.7	Massachusetts	2,678.1
11	South Carolina	1,859.9	Massachusetts	2,152.5	New Jersey	2,535.9
12	North Dakota	1,859.1	Georgia	2,127.0	Florida	2,311.4

SOURCE: Bureau of the Census, *Annual Survey of Manufacturers, Geographic Statistics* (Washington, D.C.: 1983, 1984, and 1985), table 1.

Personal Income and Earnings

Second-quarter data from the Bureau of Economic Analysis show that Michigan labor and proprietors' earnings grew by .5 percent during the second quarter compared with 1.2 percent nationally (Exhibit 3); but after adjusting for inflation and annualizing this measure, it declined in Michigan by 1.4 percent.[1]

For 1987 as a whole, Michigan's earnings are projected to gain by 2.7 percent in nominal (actual, unadjusted for inflation) terms, which translates into a decline of .2 percent in real terms (1982 dollars). Nationally, real earnings gains are projected to be 3 percent.

The immediate outlook for Michigan has worsened as 1987 has worn on and the state's economy has grown weaker in successive quarters. The stream of poor earnings statistics is expected to continue through at least the first half of 1988. This will result in a slight decline in nominal earnings for the coming year as a whole, and a 3 percent decline in real earnings. Nationally, real earnings are expected to rise by 2.5 percent in 1988.

Exhibit 4 examines Michigan's share of the national population, employment, and personal income. In 1978, Michigan had 4.1 percent of the national population, but Michigan workers earned 4.4 percent of the U.S. personal income. This reflected the higher-than-average wage rates of the Michigan labor force. By 1987, Michigan had 3.8 percent of the population and earned only 3.7 percent of national income. This reflects a higher-than-average unemployment rate and a shift in the state from high-paying manufacturing jobs to lower-paying service sector jobs.

Employment

Although the rate of Michigan employment growth slowed in October compared with the first nine months, 1987 employment will be 4 percent above that for 1986, compared with a 2.6 percent increase for the nation. This has occurred in the face of automotive layoffs that have cut more than 50,000 vehicle manufacturing jobs and another 20,000 closely related jobs since the high in late 1985. Since then, however, the state has gained about 300,000 nonautomotive jobs, most of which have been in nonmanufacturing sectors such as services and construction.

Exhibit 5 shows the levels of wage and salary employment in Michigan and the United States in the second and third quarters. Mining and construction continue to be the main strengths of the Michigan economy. Among nondurable goods, employment in Michigan paper, printing, chemicals, and food processing industries is up this year. Textile employment, which includes the manufacture of interior trim on motor vehicles, has slumped.

[1]For want of a better output index for the state, labor and proprietors' earning have been employed to measure economic growth.

EXHIBIT 3

Labor and Proprietors' Earnings in Michigan and the United States, By Broad Economic Sector: First and Second Quarter 1987 (dollars in millions)

	Michigan			United States		
Sector	First Quarter	Second Quarter	Percentage Change	First Quarter	Second Quarter	Percentage Change
Agriculture	$ 862	$ 732	-15.1%	$ 58,280	$ 54,338	-6.8%
Agricultural services, forestry, and fisheries	307	295	-3.9	13,927	13,460	-3.4
Mining	503	523	4.0	34,951	35,780	2.4
Construction	4,815	5,163	7.2	172,007	173,990	1.2
Nondurable goods manufacturing	6,741	6,516	-3.3	203,729	205,496	0.9
Durable goods manufacturing	31,118	30,494	-2.0	350,062	350,548	0.1
Transportation and public utilities	5,470	5,522	1.0	184,005	186,406	1.3
Wholesale trade	5,786	5,800	0.2	169,654	171,611	1.2
Retail trade	9,127	9,303	1.9	261,048	265,983	1.9
Finance, insurance, and real estate	4,674	4,829	3.3	202,564	204,901	1.2
Services	20,177	20,432	1.3	614,662	627,522	2.1
Federal civilian payrolls	1,559	1,570	0.7	86,641	87,085	0.5
Federal military payrolls	371	372	0.3	42,172	42,268	0.2
State and local government payrolls	11,363	11,837	4.2	294,530	300,316	2.0
TOTAL EARNINGS	$102,872	$103,388	.5%	$2,688,232	$2,719,702	1.2%

SOURCE: Bureau of Economic Analysis, Regional Economic Information System.

EXHIBIT 4

Michigan Percentage Share of Total Population, Employment, and Personal Income in Relation to the United States: 1978-1987

Year	Population	Employment	Personal Income	Per Capita Personal Income
1978	4.1%	4.1%	4.4%	107%
1979	4.1	4.0	4.4	106
1980	4.1	3.8	4.2	102
1981	4.0	3.8	4.0	99
1982	3.9	3.6	3.8	97
1983	3.9	3.6	3.8	98
1984	3.8	3.7	3.8	99
1985	3.8	3.7	3.8	101
1986	3.8	3.7	3.8	101
1987	3.8	3.7	3.7	99

SOURCES: Bureau of Economic Analysis, special release; Bureau of Labor Statistics, special release.

Durable goods employment is declining in Michigan, reflecting restructuring in vehicle manufacturing. The forecast is for more of the same with General Motors plant closings taking place late this year and other, temporary layoffs next year. The ripple effect will take its toll on wholesaling, transportation, and utilities. Indirectly, almost all Michigan industries will be affected by plant closings.

An encouraging sign in the durables sector can be found in electronic and electrical equipment and in instruments industries; third-quarter data from the Michigan Employment Security Commission (MESC) reveal modest increases in employment here in the face of a national decline. Michigan's plastics industry also continues to exhibit strength. We have a strong comparative advantage in specialty plastics fabrication because of the increasing use of such materials in the automotive industry, many new applications centers have opened in southeast Michigan during the past decade to share in the development activity.

Among durable goods not related to producing vehicles, employment in lumber and wood products and furniture and fixtures production continue to grow rapidly. Employment in stone, clay, and glass industries is also growing. The health of these construction-related manufacturing industries is linked to the construction boom taking place here.

In transportation, Michigan airlines employment is up, but the sector as a whole exhibited employment declines during the third quarter. Gas and electric utilities also experienced declining employment, whereas the communication industry showed gains.

In the wholesale sector, nondurable goods sellers added to their payrolls, but at a rate insufficient to offset declines among durable goods wholesalers. Among retailers, Michigan department stores and general merchandisers are laying off workers while clothiers are adding employees. The restaurant business remains expansive. The data show that we, as a state and nation, are trading in high-paying jobs in durable goods manufacturing for lower-paying ones in service sectors.

In the services sector, growth in business services leveled off during the third quarter, but it is not clear whether this is a pause or a new trend. This sector merits close watching because it includes high technology computer and data processing services as well as research laboratories.

Much of the growth in Michigan business services earlier in the decade was due to Electronic Data Systems (EDS) employees being transferred here from Texas. (EDS is the giant computer service firm purchased by General Motors.) As EDS missions here are completed, GM is shifting the employees to new assignments in other locations. After EDS adjustments are concluded, the overall category of business services seems likely to resume its rapid growth. Business services also include advertising, another Michigan specialty, as well as photofinishing laboratories, management and public relations, detective and protective services, janitorial and other building services, employment agencies, credit reporting and collecting agencies, equipment leasing, and mailing, reproduction, and stenographic agencies.

Another major component of the broad service category is health services. Within this group, private hospitals are troubled by declining demand. Hospitals simply are pricing themselves out of the health care market while outpatient care facilities, nursing consultants, medical and dental laboratories, physicians, and dentists are enjoying growing demand. Nursing and personal care facilities are growing because of the aging population and the attendant need for long-term care.

EXHIBIT 5

Michigan and United States Wage and Salary Employment, Second and Third Quarter 1987 (employment figures in thousands of jobs)

Sector	Michigan Second Quarter	Michigan Third Quarter	Michigan Percentage Change	United States Second Quarter	United States Third Quarter	United States Percentage Change
Mining	10.8	11.1	2.8%	734	751	2.3%
Construction	131.5	135.1	2.7	5,009	4,994	-0.3
Nondurable goods	222.8	222.8	0.0	7,839	7,898	0.8
Durable goods manufacturing	752.7	726.1	-3.5	11,182	11,239	0.5
Motor vehicles and equipment	321.7	297.0	-7.7	844	933	-1.3
Other durable goods	431.0	429.1	-0.4	10,350	10,449	1.0
Transportation, communication, and public utilities	150.0	149.4	-0.4	5,347	5,375	0.5
Wholesale trade	179.0	178.5	-0.3	5,776	5,802	0.5
Retail trade	658.7	662.1	0.5	18,209	18,284	0.4
Finance, insurance, and real estate	179.8	180.9	0.6	6,573	6,621	0.7
Services	800.6	799.4	-0.1	24,102	24,267	0.7
Government	607.2	610.0	0.5	17,033	17,033	0.0
TOTAL	3,693.0	3,675.4	-0.5%	101,708	102,271	0.6%

SOURCES: Michigan Employment Security Commission, special release; Bureau of Labor Statistics, special release.

Automotive Sales and Production

To keep the production lines rolling and demand up, U.S. auto companies have tempted consumers with cash rebates and low interest rates on car loans. In October, Chrysler Corporation tried something novel: price cuts on a few slow-moving models. In 1987, most foreign manufacturers adopted sales incentives for the first time. In spite of this, total U.S. vehicle sales will be 15 million units this year compared with more than 16 million in 1986. By year end, sales of domestic autos are projected to be down 7 percent and sales of imports down 9 percent compared with last year. Imported trucks, also affected by the sales slump, are down 15 percent. On the up side are increased sales of domestic trucks, up 2.5 percent, and domestic minivans. The latter are doing very well; they have not only cut into the Japanese minivan market, but also have invaded the domestic passenger car market.

Productivity improvements by the U.S. auto industry in the last few years are noteworthy; coupled with improvements in quality and design, this finally has prepared the U.S. industry to meet the challenges of the 1980s. Exhibit 6 shows the productivity record of American workers in vehicle manufacturing from 1977 through 1986. Between 1977 and 1980, productivity declined sharply. Since 1981, productivity has increased by an average of 6.3 percent per year. Average hourly wages, on the other hand, have risen by about 5 percent. In other words, labor cost per unit of production has declined. During 1986, while output per production worker hour increased by 2.7 percent, average hourly wages barely crept ahead, up .4 percent. So far, 1987 appears to be a repeat of 1986 in that the productivity of blue-collar labor is improving sharply relative to its cost.

In addition to the productivity gains in the industry, Chrysler and GM are closing plants to further cut overhead costs. Chrysler has to shed capacity that it acquired with the purchase of American Motors Corporation, and General Motors has to close plants to eliminate excess capacity created by opening several new plants during the past half-decade. Ford capacity and demand for its products are relatively well balanced. Both the productivity gains and the plant closings will help the industry keep prices down in order to continue to regain market share from imports and, at the same time, enjoy good profits. The domestic industry is further benefiting at present from the weak dollar, which has driven up the prices of imported vehicles.

In addition to the "Big Three," five other auto companies produce vehicles in this country: Volkswagen, Nissan, NUMMI (a Toyota-GM venture), Honda, and Mazda. In 1988, the five are expected to produce about 900,000 units compared with about 650,000 in 1987. In 1988, U.S. vehicle production is expected to total 10 million units, of which 31 percent will roll from Michigan assembly lines. Michigan vehicle production will decline more than the national average because of plant closings that will more than offset production from the new Mazda plant in Flat Rock.

Tourism

Michigan's lodgings industry continues to post modest employment gains. The industry has added about 12,000 rooms since the motel-hotel building boom started here in 1985. As a consequence of the rapid expansion in capacity, occupancy rates are down; according to Laventhol & Horwath, consultants to the industry, the occupancy rate is below year-ago levels. Occupancy is especially depressed in southeast Michigan, where growth in the number of units has been strongest.

According to data from the Michigan State University Travel, Tourism and Recreation Resource Center, vacation travel is well above 1986 levels in all sections of Michigan. State park use also posted good gains this summer and fall. The Upper Peninsula is enjoying an especially good year in outdoor recreation.

MESC employment figures show substantial gains for amusement and recreation service industries. Sales tax data from the state Treasury Department show a hefty 15 percent gain in receipts for lodgings establishments and gains of 9 percent for restaurants and 19 percent for taverns.

Retail Sales

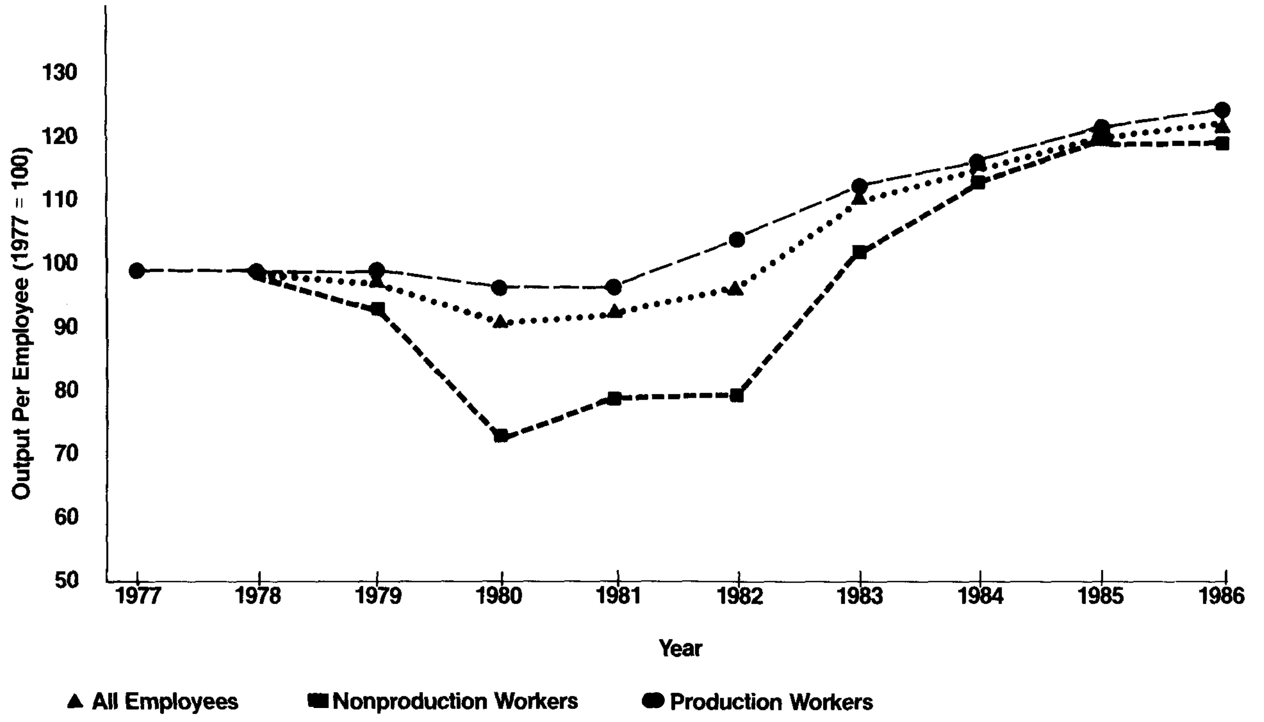
Midwestern retailers posted sales gains of only 2.9 percent over the first eight months of 1986. By comparison, retail sales in the South grew by 5.6 percent; in the West, by 5.3 percent; and in the Northeast, by 5.0 percent. Among nineteen large states for which the U.S. Bureau of the Census compiles monthly figures, Virginia led with a 10.5 percent gain the first eight months. Tennessee was second (10.3 percent) and Michigan, eleventh (3.3 percent). Among the Great Lakes states, we trailed Indiana and Illinois but led Ohio and Wisconsin. In the Detroit region, retail sales grew more rapidly than in the state as a whole. Among 23 metropolitan areas in the United States, Detroit was ninth.

Construction

Michigan's attraction as a place to do manufacturing-related business is evident in data compiled by the U.S. Bureau of the Census. In 1985 we were second only

EXHIBIT 6

Productivity and Earnings in U.S. Motor Vehicle Manufacturing: 1977-1986



to California in the valuation of permits issued for industrial buildings; in 1986, we were third. (See Exhibit 7.) This year, factory construction is expected to decline from the 1986 level in all the larger states; for Michigan, permit activity is 3 percent below the 1986 level, suggesting that this state will hold its own compared with other industrial states. As a share of the national total, Michigan's industrial construction permit valuation is compared with valuation in several other important categories in Exhibit 8. These figures corroborate other evidence that manufacturing remains our strong suit.

Three-fourths of Michigan's industrial building permits (valuation) issued during the first nine months of 1987 were in Oakland, Wayne, Saint Clair, and Macomb counties. Oakland, Macomb, and western Wayne counties typically are hotbeds of new industrial building. Port Huron is attracting such investment because it is the terminus of two interstate highways and a gateway to Canada; Sarnia, across the river from Port Huron, now is linked to Toronto by the Canadian freeway system.

The Kent and Ottawa counties area, home to several multinational office systems manufacturers, is a magnet for new manufacturing investment. Grand Rapids is also profiting from General Motors' substantial investment in its operations there.

In the construction of new office buildings, nearly 40 percent of the activity is taking place in Oakland County. Better than 20 percent of the total is accounted for by western Wayne County. Considerable office construction activity also is taking place in Kalamazoo, Kent, Ingham, Ottawa, Washtenaw, and Genesee counties.

In the construction of new stores, Oakland, western Wayne, and Macomb counties account for about half of the current activity in this state, although the Grand Rapids and Lansing areas also have a high proportion of such activity. The city of Detroit also is showing some strength in this category, as is Genesee County.

In nonresidential rehabilitation in Michigan, Detroit is the focal point. The city is rich in raw material, namely vacant factories and warehouses. Oakland and Wayne counties have considerable rehabilitation activity as does the Grand Rapids area. Washtenaw, Ingham, Kalamazoo, Saginaw, and Calhoun counties also are experiencing significant rehabilitation of older industrial buildings.

Construction provides a significant number of jobs and earnings as well as spinoff effects on the Michigan

EXHIBIT 7

Ranking of Top Dozen States in Valuation of Industrial Building Permits: 1984, 1985, and 1986

Rank	State	1984	State	1985	State	1986
1	California	$2,015,046	California	$1,930,198	California	$1,991,515
2	Florida	502,171	**Michigan**	**554,069**	Pennsylvania	541,855
3	Colorado	433,598	Florida	553,138	**Michigan**	**523,908**
4	Ohio	432,372	Indiana	530,976	Illinois	503,368
5	New York	407,293	New York	444,534	Florida	466,238
6	Texas	382,232	Texas	398,364	Massachusetts	423,309
7	North Carolina	357,836	Georgia	391,071	Georgia	369,302
8	Pennsylvania	345,720	Arizona	361,396	New York	366,080
9	**Michigan**	**330,995**	New Jersey	337,654	Ohio	305,927
10	Indiana	314,343	Illinois	333,803	Texas	294,995
11	North Dakota	268,304	Pennsylvania	328,303	Virginia	291,872
12	Massachusetts	266,088	North Carolina	315,808	New Jersey	289,610

SOURCE: Bureau of the Census, special release.

EXHIBIT 8

Michigan Relative to the United States in Selected Categories of Construction: 1984, 1985, and 1986

	Percentage of Building Permit Valuation		
Type of Construction	**1984**	**1985**	**1986**
Industrial	3.59%	5.82%	5.42%
Office	2.20	2.24	3.54
Store	1.76	2.07	3.08
Nonresidential rehabilitation	3.33	3.53	4.06
Residential	1.70	2.15	2.49
Lodging	2.42	3.32	2.63

SOURCE: Developed from Bureau of the Census, special release.

economy. It also means jobs in manufacturing, office, mercantile, and other industries after the buildings are completed and start to attract tenants. If a high level of construction activity can be maintained in Michigan, its effects will help offset the loss of jobs resulting from the structural adjustments in our automotive sector.

OUTLOOK

Nationally, earnings and employment will grow in 1988 at a slower rate than last year and at an even slower rate in 1989. Vehicle production nationwide will fall by about 6 percent in 1988.

In Michigan, production of goods and services is declining; inventory cutbacks and permanent plant closings scheduled in the automotive industry are likely to result in continued decline. We can expect Michigan unemployment to rise during the first half of 1988, and both employment and income to fall below 1987 levels during the year. As 1988 progresses, these factors may play out and the picture may improve. Beyond 1988 and into the 1990s, Michigan will be affected by productivity gains that cost jobs at the same time they improve our competitive situation. Other than during cyclical recoveries, job growth cannot be expected to originate with our large industrial corporations, it will come instead from existing small and medium-sized companies, agile enough to take advantage of new opportunities, and from fledgling entrepreneurs prepared to take risks and able to find capital. (The 1988 forecast for key U.S. and Michigan indicators is presented in Exhibit 9.)

EXHIBIT 9

Broad Economic Indicators, Michigan and the United States, Actual and Projections: 1986-1988

Indicator	1986	1987	1988	Percentage Change 1986-1987	Percentage Change 1987-1988
Earnings (current $ in millions)					
Michigan	$100,335	$103,000	$102,800	2.7	-0.2
United States	$2,574,512	$2,729,000	$2,880,000	5.6	5.5
Earnings (1985 $ in millions)					
Michigan	$100,335	$100,100	$97,100	-0.2	-3.0
United States	$2,574,512	$2,652,000	$2,720,000	3.0	2.5
Civilian employment (thousands)					
Michigan	4,007	4,160	4,120	3.8	-1.0
United States	109,600	112,500	115,000	2.6	2.2
Vehicle production (thousands)					
Michigan	3,400	3,450	3,100	1.5	-10.1
United States	11,300	10,600	10,000	-6.2	-5.7
Unemployment rate (% of civilian work force)					
Michigan	8.8%	8.5%	9.7%	—	—
United States	7.0%	6.3%	5.7%	—	—

SOURCES: The 1986 and 1987 data on earnings are from Bureau of Economic Analysis, U.S. Department of Commerce, Washington, D.C.; on civilian employment and unemployment rate from special release, Bureau of Labor Statistics, Department of Labor, Washington, D.C.; on vehicle production from special release, Motor Vehicle Manufacturers Association, Detroit.

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