

IAR'S INLAND EMPIRE REPORT ON BUSINESS

Prepared by: *The Institute of Applied Research*

at California State University, San Bernardino

Report for October 2007

Sponsor: ***Riverside County Economic Development Agency***
San Bernardino County Economic Development Agency

Introductory comments:

The Institute of Applied Research and Policy Analysis (IAR) at California State University, San Bernardino, has produced the ***Inland Empire Report on Business***, a monthly economic forecast, since 1993. From July through September of this year we took a "hiatus" from producing the report. But now we're back thanks to the generosity and efforts of our new sponsors:

San Bernardino County Economic Development Agency
Riverside County Economic Development Agency

IAR utilizes basically the same methodology and questionnaire as the national report produced by the Institute for Supply Management. Specifically, Purchasing Managers of major manufacturing firms are surveyed monthly and asked to indicate whether their production level, new orders, inventory, employment, and speed of supplier deliveries have increased, decreased, or stayed the same when compared with the previous month. Those indices are then combined into a diffusion index called the PMI – Purchasing Managers Index, an index which has been shown on the national level to be one of the most accurate leading indicators of the economy since 1931.

Our local report is released to the press on the first business day of each month to coincide with the monthly release of the national report, and generally receives extensive coverage from the local papers. This report has also been cited in various publications, including Kiplinger's California Report, and is increasingly referred to by various local economists and key business leaders. According to Kevin Palmer, Economic Development Director of the San Bernardino EDA, "**Strong research and analysis, such as the Institute of Applied Research at CSUSB provides, is critical to San Bernardino County's role as a strategic leader of our dynamic economy. This type of information will form a critical foundation as we work to shape San Bernardino County's nearly \$100 billion economy.**" And Robin Zimpfer, Executive Director/ Assistant County Executive Officer for Riverside County EDA states: "**In this growing, dynamic region timely information is crucial for the health of Inland Southern California; this is why the Riverside County Economic Development**

Agency is proud to sponsor the *Inland Empire Report on Business*, prepared by the Institute of Applied Research.” These sentiments have been echoed by leaders in the public and private sector repeatedly over the past 14 years the report has been prepared by IAR.

Each month the report is available the first business day of the month on our web site at <http://iar.csusb.edu/reports.htm>. Because of the campus closure due to recent fires, this month’s report was delayed a few days. Further, unlike previous reports which compared each month to the previous month, this report focuses only on a single month (October) since IAR is resuming the report after the three-month hiatus.

ALL KEY ECONOMIC INDICATORS MANIFEST WEAKNESS, AND PURCHASING MANAGERS ARE PESSIMISTIC ABOUT THE STATE OF THE LOCAL ECONOMY

According to Shel Bockman, Barbara Sirotnik, and Christen Ruiz (Co-Directors of the Institute of Applied Research and Policy Analysis -- IAR), this month’s PMI (41.9) is well below the 50% benchmark, with all key indicators displaying marked weakness. This figure indicates that the **local manufacturing sector** is contracting. In addition, this month’s PMI is below the 44.5% mark, suggesting a contracting **local economy**. Moreover, the New Orders index (one of the best predictors for future economic growth) is especially low. And only 8% of Purchasing Managers project a strong economy for the coming quarter.

On the other hand, this month’s findings must be understood relative to the methodology underpinning the report which for predictive purposes requires that the findings for any particular month must be interpreted and understood in the context of the findings for three prior consecutive months. Since IAR is resuming this report after a three-month hiatus, this month’s findings must be understood in that light. Of course as we continue producing these reports, trends will become clear.

Although this month’s figures must be interpreted with caution given the lack of data for the previous three months, our findings appear to be somewhat reinforced by other indices, including the national PMI produced by the Institute for Supply Management (ISM’s *Report on Business* notes that the national PMI is at its lowest level since March 2007). Further, as noted in comments by various commentators and our survey respondents, the local slowdown is probably due to a weak housing market, questionable quality of materials from China, and a weak dollar.

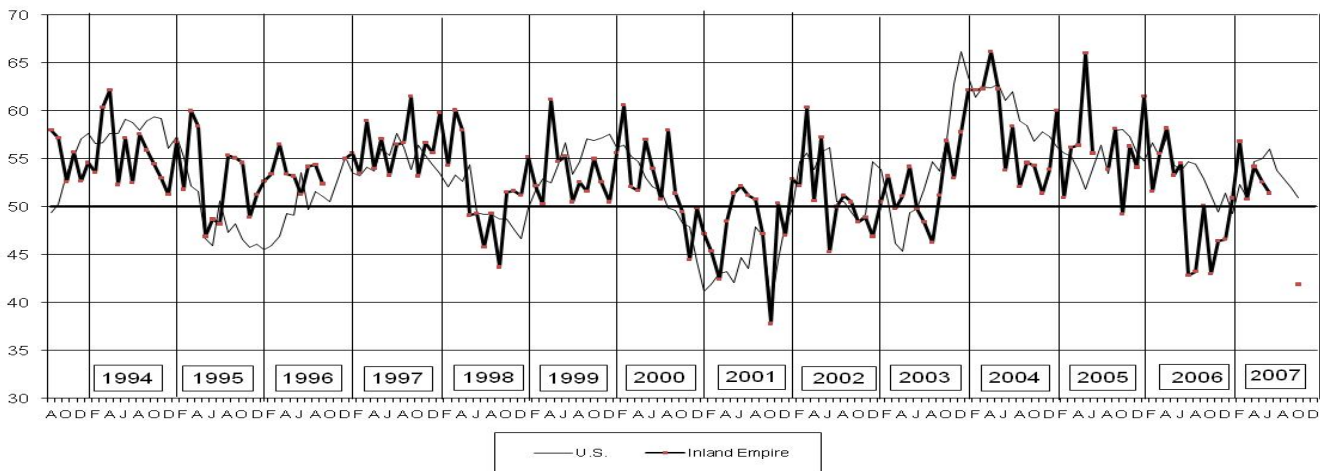
Finally, since this report focuses only on this month’s findings (rather than a comparison of this month with previous months), it is best viewed as a condensed version of future reports. It is also IAR’S intention to include in future reports additional comparisons and data sources.

Following are some highlights from this month’s surveys:

- Local PMI: 41.9 (Manufacturing sector and local economy are contracting)

- Commodity prices: 67.3 (Prices are increasing)
- Production: 46.2 (Production levels are decreasing)
- New Orders: 36.5 (New orders are decreasing)
- Inventory: 38.5 (Inventory is decreasing)
- Employment: 40.4 (Employment is decreasing)
- Speed of supplier deliveries: 50.0 (Unchanged from September)
- When Purchasing Managers were ask to rate the local economy for the coming quarter:
 - 8% predict the local economy will become stronger in the upcoming months
 - 46% believe the local economy will become weaker
 - 46% feel that the economy is in a “holding pattern” and expect the local economy to remain unchanged for the next three months

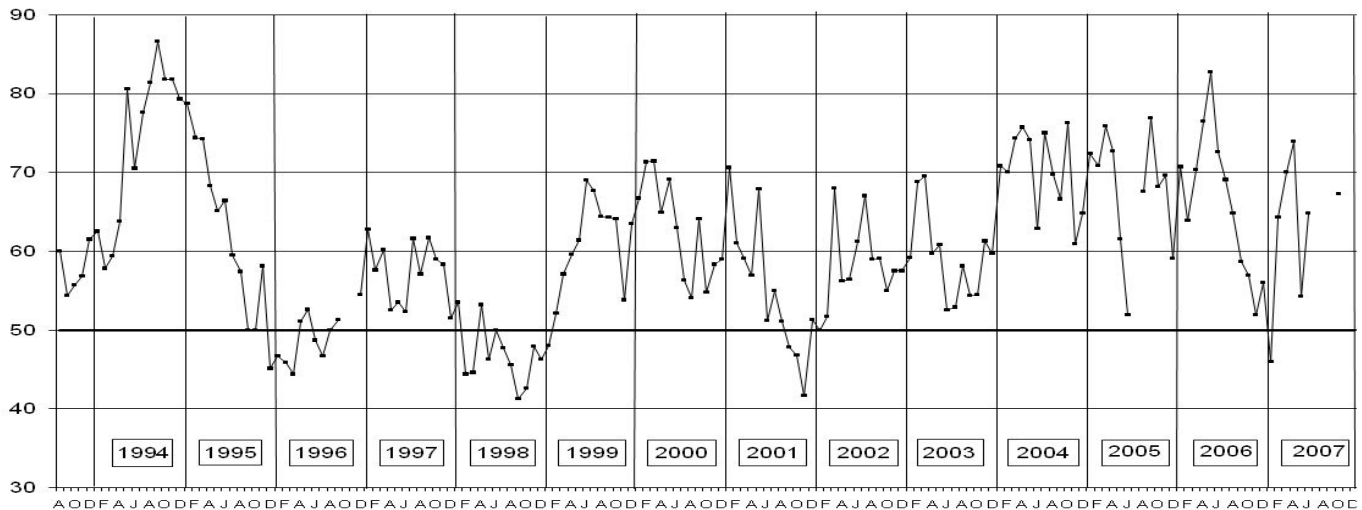
Purchasing Managers' Index



- NOTE: Inland Empire data were not collected for the months of October and November 1996, July 2005, and July through September 2007

October's Commodity Price Index (67.3) remains above 50 indicating that inflationary pressures continue to exist in the Riverside and San Bernardino County.

Commodity Prices



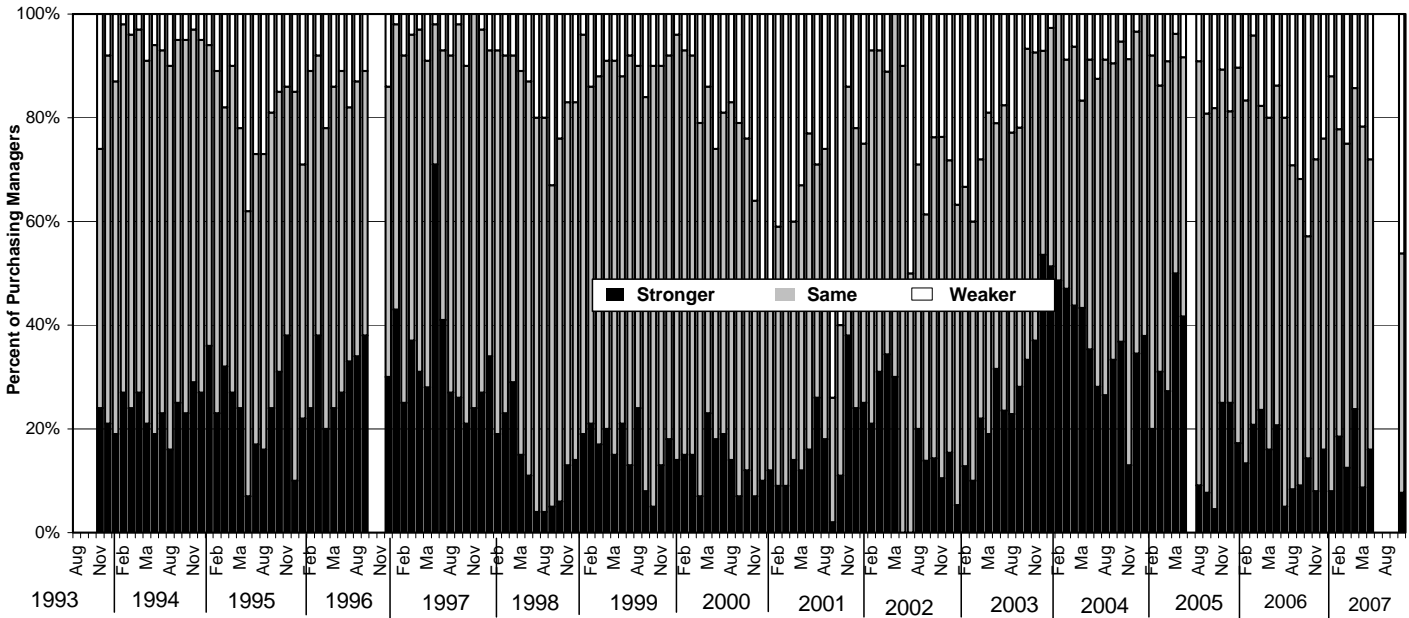
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Purchasing Managers continue to be “less than optimistic” about the state of the local economy for the coming quarter. Only 8% of purchasing managers predict that the local economy will become stronger in the upcoming months, whereas 46% of purchasing managers believe the local economy will become weaker by next quarter. The remaining 46% feel that the economy is in a “holding pattern” and expect the local economy to remain unchanged for the next three months.

STATE OF THE ECONOMY: DATA FROM 10/2006 THROUGH 10/2007

| | Oct | Nov | Dec | Jan | Feb | Mar | Apr | May | Jun | Jul | Aug | Sep | Oct |
|-----------------|-----|-----|-----|-----|-----|-----|-----|-----|-----|-----|-----|-----|-----|
| Weaker | 43 | 29 | 24 | 12 | 22 | 25 | 14 | 22 | 28 | - | - | - | 46 |
| Same | 43 | 63 | 60 | 80 | 59 | 63 | 62 | 69 | 56 | - | - | - | 46 |
| Stronger | 14 | 8 | 16 | 8 | 19 | 12 | 24 | 9 | 16 | - | - | - | 8 |

State of the Local Economy



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When Purchasing Managers were asked to make comments on the general business conditions that affected their company, only one provided a positive comment: "Business is picking up."

Meanwhile, other managers remarked negatively: "Construction now causing a slow down in our company," "Housing market has 2 influences: Seasonal winter is slow and market industry is struggling," "Questionable quality of materials from China is affecting supply and prices," "Business has been slow for 3 months," "Q4 2007 revenues forecast to decline 5% from Q4 2006," "Housing and new construction slow down is starting to eat away at future business and hiring freeze continues," "Heavy industries are struggling with the weaker dollar and foreign competition," "Slow," "Housing extremely slow, but commercial still strong," and "Prices overseas have increased."

FOR QUESTIONS OR FURTHER INFORMATION, CONTACT:

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