



MICHIGAN FUTURE BUSINESS INDEX October 2012

FINDINGS REPORT

- *Business is pumping the brakes. After showing signs of growing economic momentum in the June survey, Michigan's small to medium-size businesses now anticipate another possible stall in the recovery.*
- *Many feel the pressure of expanded regulatory and business costs. Expanded government regulations and business expenses — specifically health care costs and impending implementation of the ACA — are expected to trim profits.*
 - *Uncertainty is causing employers to temper wage increases and hiring, and consider reducing health care benefits.*

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INTRODUCTION

Conducted semi-annually since 2006 by Accident Fund Insurance Company of American, headquartered in Lansing, Michigan, the Michigan Future Business Index (MFBI) surveys owners of small to medium-sized businesses in Michigan, to provide a business perspective of economic conditions in the state. The survey also measures business owners' expectations for future economic and business sector growth. Results provide data to track trends and offer insights into the small to medium-sized business sector's contribution to regional and statewide economic prosperity.

Lansing, Michigan-based Marketing Resource Group, Inc. (MRG) conducted the MFBI survey in partnership with the Accident Fund Insurance Company of America and the Michigan Business Network. MRG is a Michigan-owned public affairs and public opinion research consulting firm that advises corporate, association, education, and coalition interests. The Michigan Business Network provides perspective on business and industry developments across Michigan.

METHODOLOGY

- MRG conducted the 2012 Fall MFBI survey primarily with owners and C-suite executives from small to medium-sized businesses across Michigan between October 14 and 31, 2012.
- The mixed-mode survey included telephone and web interviews with 1,015 business executives from Michigan companies with 500 employees or fewer. It has a margin of error of ± 3 percent within a 95 percent degree of confidence.
- Thirty-one percent (n=316) of the sampled respondents were randomly selected from the Lansing tri-county region (including Clinton, Eaton and Ingham Counties) and the remaining respondents were randomly selected from businesses across the state.
- The survey gleaned business owners' assessment of business performance over the previous six months and their expectations for the next six months. In addition, the survey garnered various perceptions and personal experiences regarding doing business in Michigan.

MFBI CONCLUSIONS: OCTOBER 2012

According to this latest survey of business leaders in Michigan, a full economic recovery for the state may be on hold, at least for the near future. Many say that added regulatory and health care policies are shrinking their bottom line, causing them to slow their earlier stated plans for increasing wages and benefits. When specifically asked about health insurance benefits, there is an increasingly larger group of job providers who are considering a reduction of benefits, including placing a larger burden of health insurance premium costs onto their employees.

While the June MFBI showed significant positive signs that Michigan's business owners believed the state's recovery was gaining momentum, recent setbacks in the national economy, the fear of a looming fiscal cliff, and the uncertainty of the then-unrealized national election for President may have contributed to these emerging "wait and see" attitudes gleaned in October.

The good news is that there are still signs of a recovery trying to materialize. Respondents continue to report growing sales, and more are now revealing plans for new product and service launches. However, significant percentages are also telling us that newly realized government mandates are squeezing profits. Additionally, growing fears of added taxes and health care costs are causing business owners to rethink their previously planned human resource investments.

Having said that, there are continued signs that business leaders believe the Michigan economy is still trending upward. A majority still believes the outlook for business remains positive and the state tax structure is fair. The questions that remain are largely pertaining to compliance with new and upcoming federal mandates.

Michigan is in a vulnerable position at this stage of its developing recovery. If concerns over the so-called fiscal cliff are not quickly resolved and the growing anxiety over added health care costs is realized, it's likely businesses will be forced to again cut capital and human resource investments, possibly triggering a second recession. The President and Congress need to move quickly to reduce this uncertainty and restart the recovery.

FINDINGS

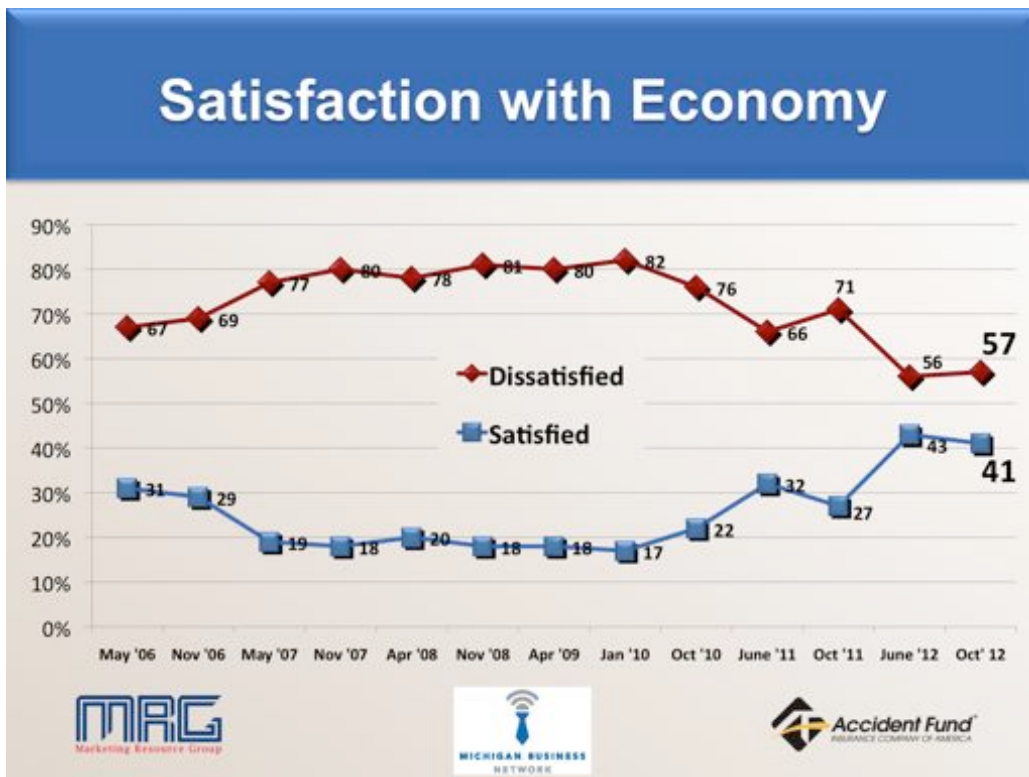
SATISFACTION WITH ECONOMY STALLS

SIGNIFICANT POSITIVE TREND HALTED

After seeing a significant jump in satisfaction with the Michigan economy in June, the October 2012 MFBI survey shows leaders of small to medium-sized businesses across Michigan have slowed their enthusiasm. Dissatisfaction with the state economy has ticked up one point since June to 57 percent, while satisfaction has dropped two points to 41 percent. That being said, satisfaction with the economy is still 14 points stronger now than it was a year ago in October 2011.

Highlights

- The positive trend that started back in October of 2010 has stalled for the time being.



SALES CONTINUE TO IMPROVE BUT HIRING, WAGES, INVESTMENTS AND PROFITS ARE NOW ALL TRAILING

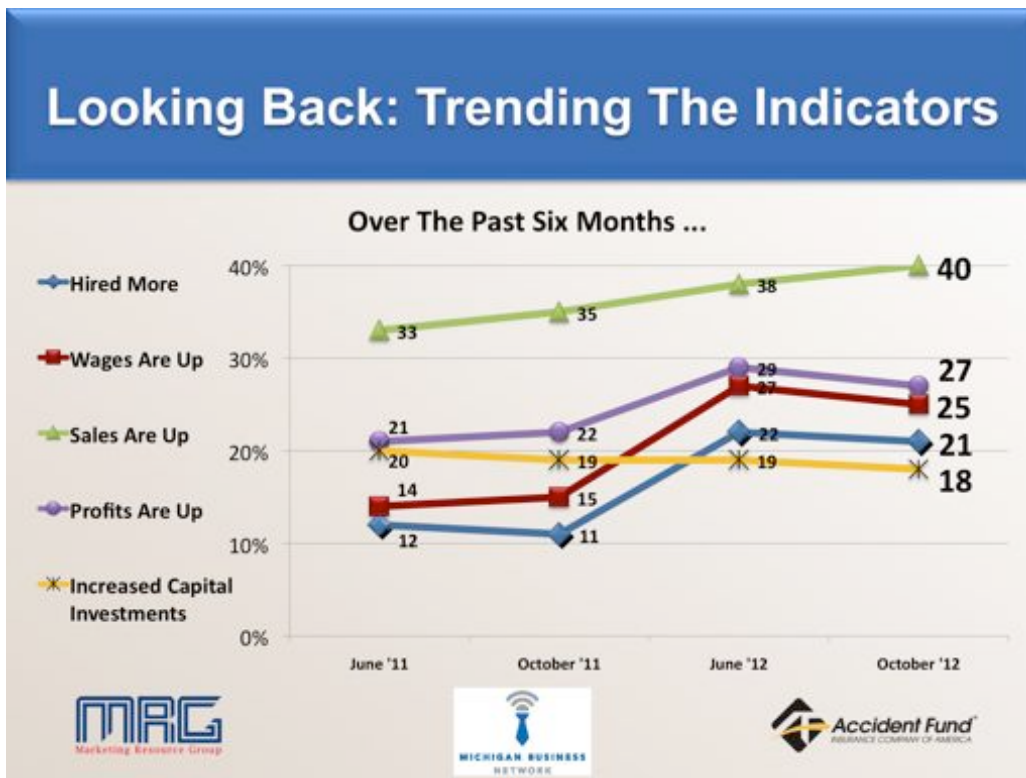
When respondents were asked to assess the performance of their business operations over the previous six months, only sales measures have shown an improvement. That is a significant shift in direction from June, when all performance indicators were trending up. This is a clear

indication that revenue from increased sales is not keeping up with the expansion of business costs, including wages, benefits, taxes and regulatory compliance.

Please see accompanying trend graph on the following page.

Highlights

- The percentage of businesses with new hires is still 20 points higher than one year ago, but it is statistically unchanged (within the margin of error) since June 2012. Twenty-one (21) percent now say they've hired more employees over the past six months, which is down one point since June.
 - New **hiring** remains strongest in West Michigan (27%). There is also a significant increase in hiring among larger businesses (35%) and among those in construction, manufacturing and distribution (26%).
- While **wage increases** for employees have slowed since June (two points down), more than one in four (26%) businesses in Detroit and West Michigan say they have increased employee wages in the last six months. Those percentages have remained statistically unchanged since June.
- Only twenty-seven (27) percent said **profits** have increased in the last six months – a two-point drop since June.
 - While more than a quarter of businesses in Metro Detroit (27%) and West Michigan (28%) say their profits have increased, those are percentages are significantly lower since June.
- Forty (40) percent of business owners reported in this survey that **sales** had increased over the previous six months. That is a two-point increase from the June 2012 survey, when 38 percent reported that sales had increased. Businesses in Northern Lower Michigan experienced the biggest jump in sales, with 49 percent saying they have grown.
- Nineteen (18) percent of respondents said their **major investments** in facilities and equipment had increased in the past six months. This is the only indicator that has been on a consistently slow downward trend. Small to mid-size businesses continue to make do with the facilities and equipment they currently have.
- Dealing with **government regulatory policy** is now seen as the top challenge to business in Michigan, tied for first place with the **slow economy** at 11 percent. However, the cost of providing **health care benefits** to employees is now also nearly tied at 10 percent.



OPTIMISM FOR FUTURE GROWTH STILL REMAINS POSITIVE, EVEN THOUGH A GROWING PERCENTAGE REPORT A SHRINKING BOTTOM LINE

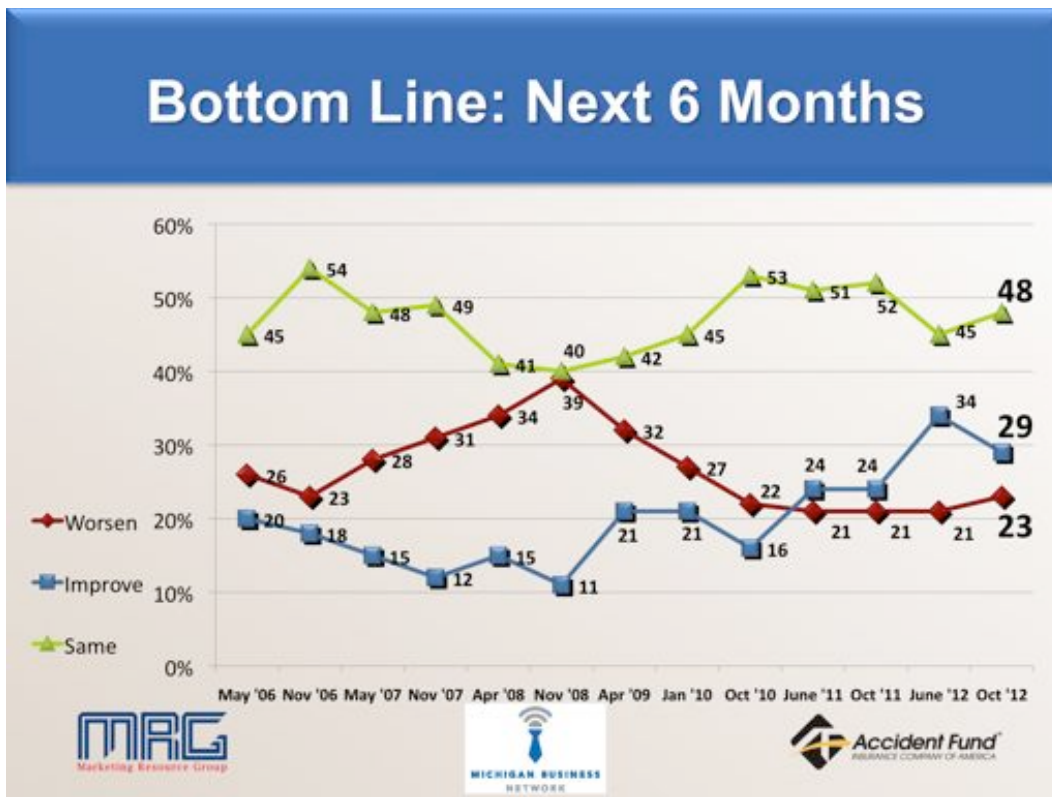
When respondents were asked to give their expectations for the next six months, the June 2012 majority (52%) having a positive outlook for future business remains unchanged. While other indicators may suggest a stall in the recovery, these data point to optimism that the stall may be short-lived.

Highlights

- Fifty-two (52) percent say their outlook for business over the next six months remains good, with 17 percent saying “very good.” Twenty-one (23) percent said the outlook is bad, with only six percent saying “very bad.”



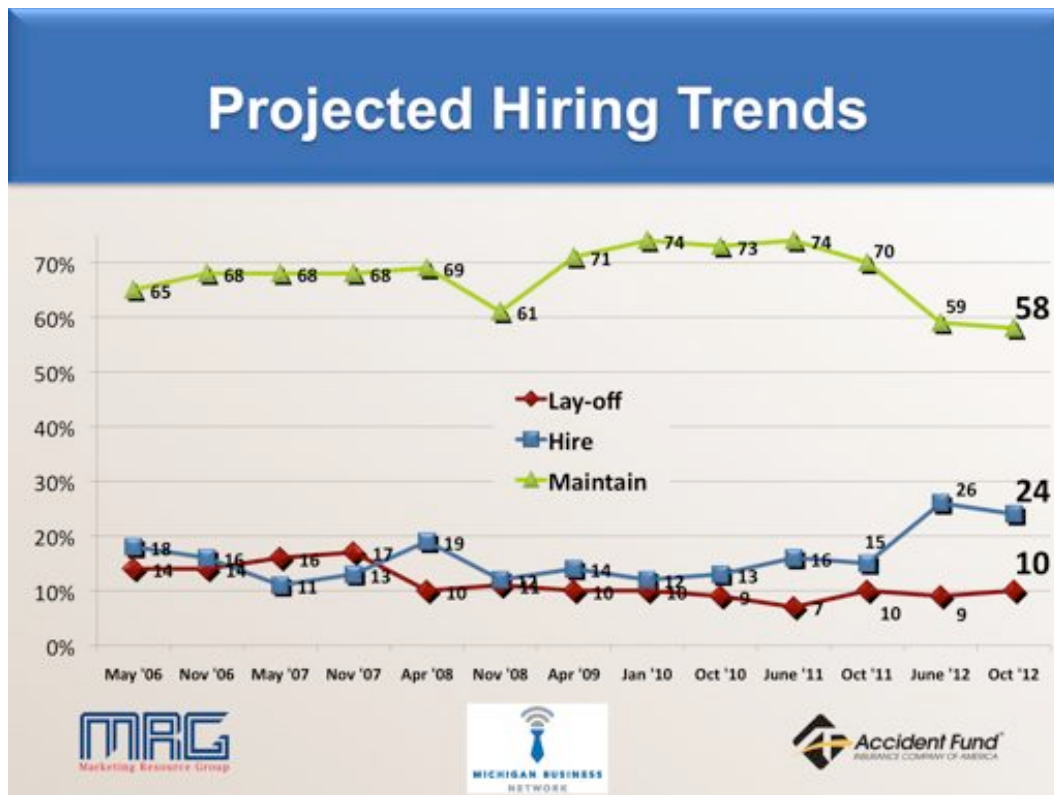
- Forty-two (42) percent of respondents say they expect **sales** to increase in the next six months. That’s a two percent drop since June. The percentage of those who believe sales will decrease has remained essentially unchanged from 10 percent in June to 11 percent now.
 - Expectations for increased sales are again highest in Metro Detroit (48%) and highest in the financial, insurance and real estate sectors (52%).
- Mimicking the recent non-symbiotic relationship between past sales and profits, only thirty-two (32) percent now say they believe **profits** will increase in the next six months, down seven points from June and roughly back to where it was last October 2011. Twenty (20) percent now say profits will decrease, up five points from June.
 - Profits expectations remain rosiest in Metro Detroit, where 36 percent believe they will see increases this year. However, that is eight points lower than what it was in June.
- Given their sales and profits expectations, it’s not surprising that expectations for respondents’ business **bottom line** (expenses compared to profits) have fallen. Thirty-four (34) percent expected their bottom line to improve in the June 2012 survey, but that number now has dropped to 29 percent. Nearly half (48%) believe it will remain the same, while 23 percent say it will worsen.



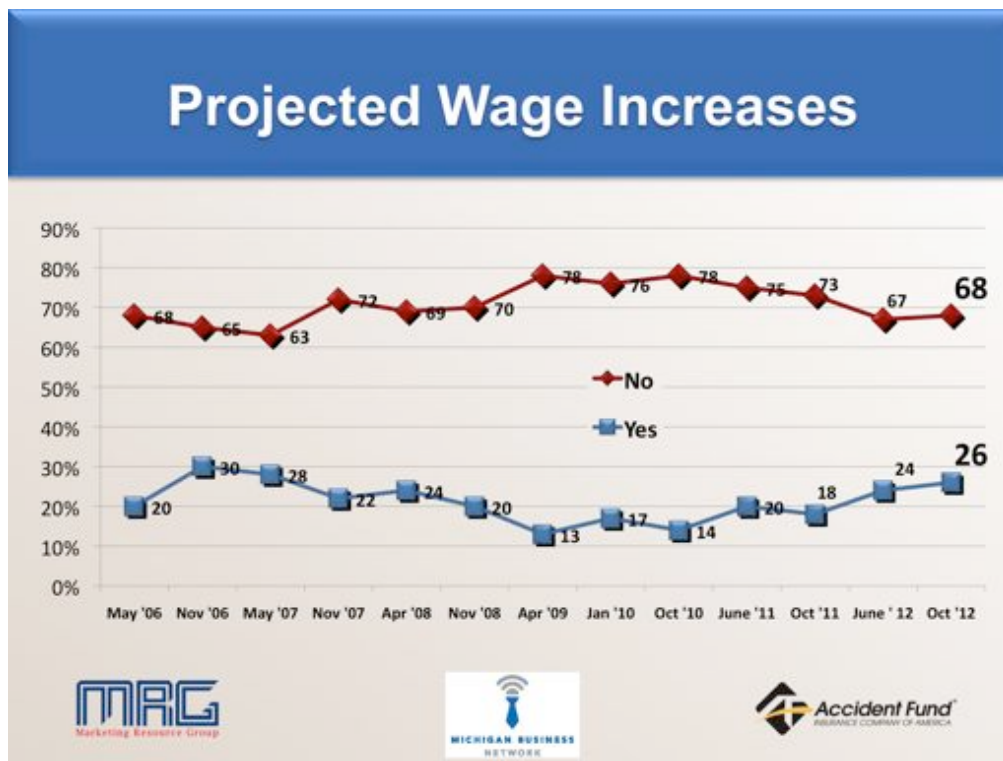
ALTHOUGH EXPECTATIONS HAVE LEVELLED OFF, ROUGHLY ONE IN FOUR BUSINESSES SAY THEY WILL HIRE MORE STAFF IN NEXT SIX MONTHS

Highlights

- Twenty-four (24) percent of respondents say they plan to **hire** more employees in the next six months. While that number is two points lower than it was in June 2012, it's still nine points higher than October 2011.
 - The outlook for new hires remains strongest in the Detroit Metro region (26%).
 - Larger businesses and new businesses, especially childcare, are hiring most (33%).
 - Manufacturing is most likely to lay off workers (17%).



- Respondents continue to give Michigan’s skilled labor pool lower than average ratings. Forty (40) percent give Michigan a poor (10 percent) or only fair (30 percent) rating for access to qualified personnel. That number continues to climb, from 30 percent in October 2011.
- In addition, 51 percent of those who have tried to fill positions over the last year are still having difficulties filling those positions.
 - Eight out of ten say they can’t find qualified applicants to fill the open positions.
- The outlook for increased **wages** continues to improve, albeit marginally. Now, 26 percent of all respondents say they plan to increase wages for their employees within the next six months. That’s up only two points from 24 percent in June.
 - Employers in West Michigan are most likely to increase wages for workers, with 32 percent indicating they will do so.
 - Wages are most likely to climb within the financial, insurance and real estate sectors, with 31 percent of those employers saying they’ll raise compensation.



- Twenty-four (24) percent expect to **invest in office equipment** in the next six months, which is up five points since October 2011. Fifty (50) percent say they will invest in advertising – a seven-percent increase since October 2011. Among those buying ads, Internet advertising continues to be the preferred medium (63%) with direct mail coming in second at 37 percent and magazine ads coming in third at 23 percent.

TO IMPROVE BOTTOM LINE, TRENDS SHOW BUSINESSES ARE BECOMING INCREASINGLY LIKELY TO REDUCE EMPLOYEE HEALTH INSURANCE BENEFITS

For the first time, we now see a significant increase in respondents indicating that they are seriously considering reducing health care benefits or increasing the share their employees pay for health insurance premiums.

Highlights

- Thirteen (13) percent expect to **reduce all benefits** in the next six months. That is up five points from eight percent in June 2012, and up 11 points from two percent last October.
- Regarding **health care benefits**: 18 percent now say they will decrease health care benefits. That is up from 11 percent in June and eight percent last October.
 - Twenty-eight (28) percent now say they will increase employee health insurance

premiums in the next six months, which is up from 23 percent in June and 11 percent last October.

- Only eight percent say they don't expect increased health care costs over the next six months. That's down from 12 percent in June.

BUSINESSES CONTINUE TO FIND REASONS TO BE ENCOURAGED & EXPAND SAYING CONSUMER MARKET AND STATE TAX STRUCTURE CONTINUE TO IMPROVE, MANY MORE LAUNCHING NEW PRODUCTS & SERVICES

Perceptions of Michigan's consumer market continue to improve, while a growing majority of business owners statewide continue to believe the business tax structure is fair.

Highlights

- A plurality (42 percent) of small business owners in this survey says that Michigan is a "pretty good" market for goods and services. That's up from 37 percent in October 2011. The rating of "only fair" has also increased from 33 percent in October 2011 to 36 percent now. The percentage of those giving it a "poor" rating has dropped from 17 percent in October 2011 to 12 percent now. And the "excellent" rating has also decreased, but by a smaller margin, from 12 percent in October 2011 to ten percent now. Overall the ratings are showing continued moderate improvement.
- Fifty-four (54) percent now rate Michigan's business tax system as "fair" – up two points from June and 11 points from October 2011 – while 37 percent now say it's unfair. The unfair rating is down five points from October 2011.
- Eight (8) percent say they will add a new business location within the next six months. That number has doubled since October 2011.
- Nineteen (19) percent now say they will add a new product line (up from eight percent one year ago) and 23 percent now say they will add a new service (up from six percent one year ago).
 - These data are supported by responses to an earlier open-end question that asked for respondents' reasons for optimism. The most, 13 percent, cited an expansion of their business as their reason for being optimistic for the future. Another 14 percent cited their excellent product or service and eight percent said the economy is improving.

INCREASED BUSINESS COSTS AND GOVERNMENT REGULATIONS ADD UNCERTAINTY, SLOW RECOVERY

- Thirty-six (36) percent said they are encouraged for their business ten years down the road. That's a four percent drop since June. Thirty-six (36) percent said they are concerned, which hasn't changed since June. Twenty-six (26) percent now say they are

uncertain about the future of their business. That is up three points since June.

- Again, they indicate that added government regulations and changes to health insurance policy are feeding this uncertainty. As explained earlier, government regulatory policy, the slow economy, providing health care benefits are now seen as the top three challenges to doing business in Michigan.