Manufacturing & Distribution Monitor
Spring 2011 Report

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Preface

Karen Kurek
National Manufacturing Practice Leader
RSM McGladrey, Inc.

Welcome to the Spring 2011 edition of the McGladrey® Manufacturing & Distribution Monitor Report. After delivering five years of annual industry snapshots, McGladrey has expanded its study to provide surveys on a quarterly basis. Our primary objective is to provide industry leaders and policymakers with a continuous stream of fresh, focused data and insight.

The so-called "Great Recession" that began December 2007 officially ended June 2009.[1] Manufacturers and distributors were hit very hard during the economic downturn, but have made a remarkable comeback and are leading the path to recovery for the U.S. economy. Our 2010 annual survey indicated some decent progress along this path and many respondents had hopes for a solid recovery in the coming year. These hopes are now being realized as discussed in our first quarter spring 2011 survey.

Consider the following:

- Ninety percent of the respondents are optimistic about their businesses. Furthermore, 45% indicated their businesses are "Thriving and Growing," nearly *double* the percentage from last year's numbers and the highest level we have seen since 2007.
- Interestingly, the industry sectors that report the highest levels of "Thriving and Growing" are Industrial Machinery and Equipment and Transportation Equipment—the bedrock of the manufacturing industry. Also, Energy and Cleantech (a new sector we are tracking) reports high levels of "Thriving and Growing," underscoring the momentum in the "green" sector.
- Only 3 percent of the companies report their businesses are in decline—the lowest percentage we have seen since we began collecting the data. Now that's recovery!
- Good news on the job front: over half of the respondents plan to increase their work force in the next 12 months.

International activity continues to move forward. Expectations for international sales are up modestly from 2010, but we are seeing a very interesting trend we look forward to tracking: the growing emphasis on pursuing opportunities in emerging markets. We have said since 2006—and the song remains the same—that internationally active companies are generally stronger and more profitable than those that sell only within the United States.

Perhaps the greatest concern expressed this spring is the oil-led rise in commodity prices. Over 90 percent of the respondents are expecting increases in raw material costs, with an average increase in the double digits. One indication of the pressure U.S. companies are feeling from rising costs is in their growth strategies, where plans to raise prices are the third most popular measure to achieve growth. Not a welcome move in a country where unemployment still stands at 9 percent, but a necessity for maintaining healthy margins.

My thanks and deep appreciation to our spring survey respondents for their time and insights, as well as to the industry and business associations that encouraged their members to participate. I look forward to reporting back next quarter!

Karen L. Kurek

[1] (Source: The Business Cycle Dating Committee of the National Bureau of Economic Research)

Table of Contents

Executive summary

The McGladrey® Manufacturing & Distribution Monitor Spring 2011 edition was fielded on March 11 and completed data collection on April 4. The survey analysis includes aggregated responses from 904 executives and managers of U.S.-based manufacturing and wholesale distribution enterprises. This is the first of four 2011 surveys, delivered quarterly, that will capture and identify significant trends on highly topical issues relevant to U.S. business in general, and to manufacturing and distribution in particular. In addition, each quarter we will address key management performance benchmarks as core issues alongside special Monitor topics.

McGladrey has conducted an annual national study of the manufacturing and distribution industry since 2006. When appropriate, our quarterly reports will compare current findings with data gleaned from previous studies.

This year the Monitor has added a new feature: the opportunity for survey participants to view their individual responses on a dashboard in the context of other responses. The dashboards will remain available to respondents throughout the year as data from each quarterly survey accrues.

Following is an overview of key findings.

Overall perceived and anticipated business conditions

Condition of business. Manufacturers and distributors are reporting rapid improvement in their overall economic condition and optimism for continued growth. Almost twice as many respondents (45%) say their businesses are "thriving and growing" as indicated such in 2010 (24%).

At 45 percent, the "thriving and growing" segment is not yet back up to 2006 levels (57%); however, this year only 3 percent of respondents say their companies are declining, compared to 4 percent in 2006, when the first national survey was conducted, and 10 percent just last year. Companies that trade outside the U.S. are more likely than others to report they are thriving and growing, as international sales are playing a strong role in the recovery.

All but one industry sector show substantially higher levels of prosperity in 2011 than in 2010. **Food and Beverage**, last year's leader, reports a slight decline year-to-year. Standout industries include **Industrial Machinery**; **Computers and Electronics**; **Fabricated Metal**; and **Energy and Cleantech**. Notable laggards include **Building Materials**; **Furniture and Fixtures**; **Wood, Paper and Printing**; and **Textiles and Apparel**.

Expectations for growth

Business optimism. Respondents expect the good times to continue for at least the next 12 months. A large majority of respondents (90%) report they are "somewhat" or "very" optimistic about their own companies' prospects. Focusing on the most optimistic ratings, we find 26 percent very optimistic about their own companies and 14 percent very optimistic about growth in emerging markets. However, they are significantly less enthusiastic about growth prospects for their industries (8%), and only a handful are very optimistic about the U.S. (2%) or world (1%) economies. The contrast between optimism for emerging markets and for the U.S. is striking.

Key internal benchmarks. Domestic sales, which 80 percent of respondents expect to increase, show a strong upward trend, advancing 9 percentage points from growth expectations reported in 2010. Growth expectations are high across all industry segments, led by the resurgent **Automotive** and Industrial Machinery sectors. Expectations for international sales are also significantly (8%) higher than in 2010. Of the respondents whose companies are internationally active, 72 percent expect international sales to increase.

Other encouraging signals include an increase in unfilled orders from the previous quarter (reported by 50 percent of respondents) and growth in workforce (projected by 56 percent).

Challenges to growth

Rising commodity prices. Respondents overwhelmingly agree (92%) that rising cost of key inputs and raw materials will create challenges in the coming 12 months. While two-thirds anticipate a negative effect on margins, passing the costs on to consumers may be problematic in an economy characterized by continuing high rates of unemployment. Fewer respondents see risks to overall sales volume, plant, and human resources, but 40 percent worry that commodity price increases could adversely affect their entire business model.

Geopolitical risk. While perceptions of the international environment are dynamic and heavily influenced by events, at the time the survey was fielded almost half (48%) of respondents saw political unrest in the Middle East as posing at least a moderate risk to their goals for sales growth. Across the board, the greatest concerns involve economic challenges, specifically commodity prices and the conditions of the U.S. and global economies. In addition, concerns about U.S. government regulations and oversight, as well as legislative gridlock, were cited by more than half of all respondents.

Paths to growth

Sales growth. Not surprisingly, the key priorities for growing sales emerged as “innovate” (e.g., new products and processes) and “expand” (e.g., expand sales to current customers, to prospective U.S. customers, and to new customers outside the U.S.).

Sensing great opportunities, but sensitive to potential challenges, businesses are pursuing an array of approaches and tactics.

Managers are focusing on growing business with current customers while courting new customers with comparable energy. Notwithstanding the increasing emphasis on international markets and opportunities, focus on the U.S. market is a priority for more than 70 percent of all respondents.

The trend toward international marketing and exporting seems likely to continue and strengthen. Almost half (48%) of participating companies plan to expand sales in non-U.S. markets where they currently have a presence, or stage an entry into a new global market. When they look outside the U.S., managers are increasingly likely to look beyond Canada or Mexico, traditionally the United States’ largest trading partners. Increasing sales in emerging markets is important to a growing minority (approximately 25%) of all businesses participating in the Spring 2011 survey.

Industrial Machinery has been a powerful driver of exports during the recovery. Challenged by recent declines in domestic manufacturing, companies in this sector have been forced to look elsewhere and have done extremely well internationally. Also pursuing growth outside North America are highly innovative sectors such as Computers and Electronics; **Biotech and Medical**; and Energy and Cleantech.

Tactics and Priorities. "Introducing new products" is a key sales growth strategy for more than 60 percent of respondents, outstripping all other rated tactics. New product introductions are important for increasing sales among current customers, for expanding in the U.S. market generally, and for the acquisition of new customers.

Somewhat surprisingly, businesses also identified "price increases" as their second highest priority, following closely behind "increasing brand recognition" and ahead of "entering new global markets." Reducing prices, often considered a key tactic for seizing market share, was the least employed tactic among all those rated. The emphasis appears to be on aggressive expansion rather than strategic retreat or "buying new business."

Outlook for growth

Current business conditions

Over the past three years, the number of businesses reporting they are "thriving and growing" has increased significantly—from 9 percent in 2009 to 45 percent in 2011. Sales, sentiment and more robust hiring figures have joined the earlier economic indicators to suggest a true end to the recession that began in 2008 and hit businesses hard in 2009. The current picture is the most positive seen since 2006, with only 3 percent of respondents reporting their businesses are in decline, versus 4 percent in 2006.

Chart 1: Business conditions

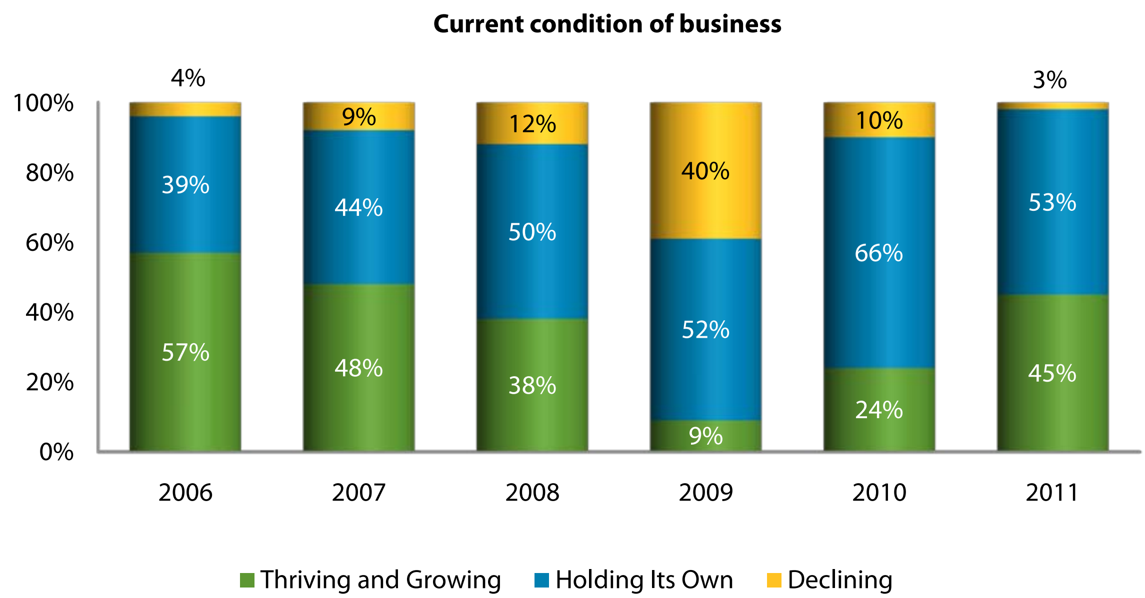


Chart 1 compares survey responses from 2006 through 2011 to the (paraphrased) question: "Which of these terms best describes the general condition of your business at the current time?"

The steady increase in companies "thriving and growing" and "holding their own" is a powerful indicator of continued economic rebound. While companies across the U.S. are prospering, the data confirm that internationally active U.S. companies (50% "thriving and growing") are out-performing those focused solely on the domestic market (37% "thriving and growing"). Companies that intend to expand their international sales are also more likely (53%) than others (38%) to consider themselves thriving and growing.

Chart 2: "Thriving and growing" by industry

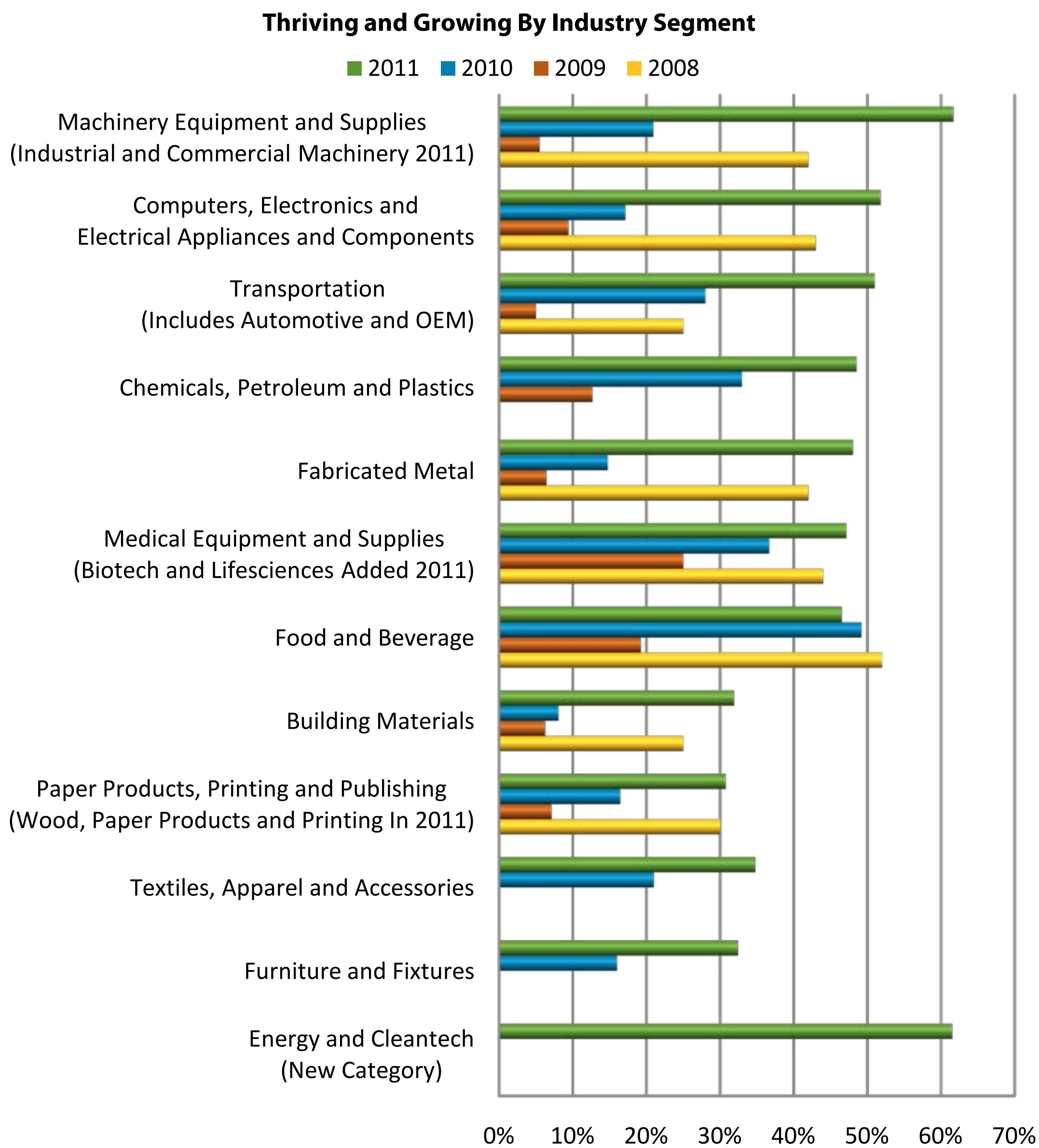


Chart 2 shows the percentage of "thriving and growing" companies within industry segments for 2011 and for prior years (where historical data was available). Note that for comparison with previous years Transportation includes Automotive OEMs and aftermarket. From this point forward Automotive and Transportation are treated as discrete industry sectors.

Thus far in 2011, most industry sectors are showing a substantial increase in companies reporting to be "thriving and growing." While traditional manufacturing sectors are leading the rebound (e.g., within the Industrial Machinery sector, 62 percent are thriving and growing, compared to just 21 percent last year), they have been joined by a new industry sub-segment: Energy and Cleantech. Striking improvements are also evident in the Transportation, Computers and Electronics and Fabricated Metal sectors.

> The dominance of three sectors most associated with traditional American industry: Industrial Machinery, Computers, and Electronics and Transportation (which includes companies selling into the automotive market), is a clear indication of the strong resurgence in the U.S. economy in spring 2011. – Karen Kurek, National Manufacturing Practice Leader, RSM McGladrey.

Food and Beverage, the sector with the most "thriving and growing" companies in 2010, fell to seventh place in the current survey and is the only industry group showing a decline from last year. The most significant factor in this decline is apparently spikes in the prices of key commodities, which companies in the sector are finding difficult to pass on to consumers. Although doing much better than last year, Building Materials and Furniture and Fixtures are comparative laggards – suffering from continued depression in commercial and residential construction. The Wood, Paper and Printing sector appears to be suffering both from depressed construction activity and from the rapid growth of online and electronic communications. Textiles and Apparel is also lagging due to competition from traditional rivals in emerging and third world markets, along with the rising cost of cotton.

> Consider that 95 percent of the world's market is outside the United States.
>
> On December 7, 2010, Governor John Engler, then president of the National Association of Manufacturers, joined Commerce Secretary Gary Locke and Russ Fleming, FedEx vice president for international marketing, to announce the launch of the New Market Exporter Initiative. This program, an extension of the National Export Initiative announced earlier in the year by President Obama, makes it easier for U.S. small- and medium-size manufacturers to export their products into new markets and reach new customers around the world.
>
> In addition to receiving a personal call from an expert trade analyst who will help the company identify new markets and trading partners, applicants get access to a number of free resources and tools through a nationwide network of international trade experts and global shipping specialists. For more information, contact the National Association of Manufacturers or the Department of Commerce.

As in 2010, larger companies are rebounding faster than small ones. Companies with less than $25 million in revenue continue to lag in comparison to the larger companies, possibly because they are less inclined to enter into the global marketplace.

Level of optimism for growth

The next 12 months look positive, with 90 percent of respondents reporting they are "somewhat optimistic" or "very optimistic" about growth prospects for their companies, compared to 83 percent in 2010 and 48 percent in 2009.

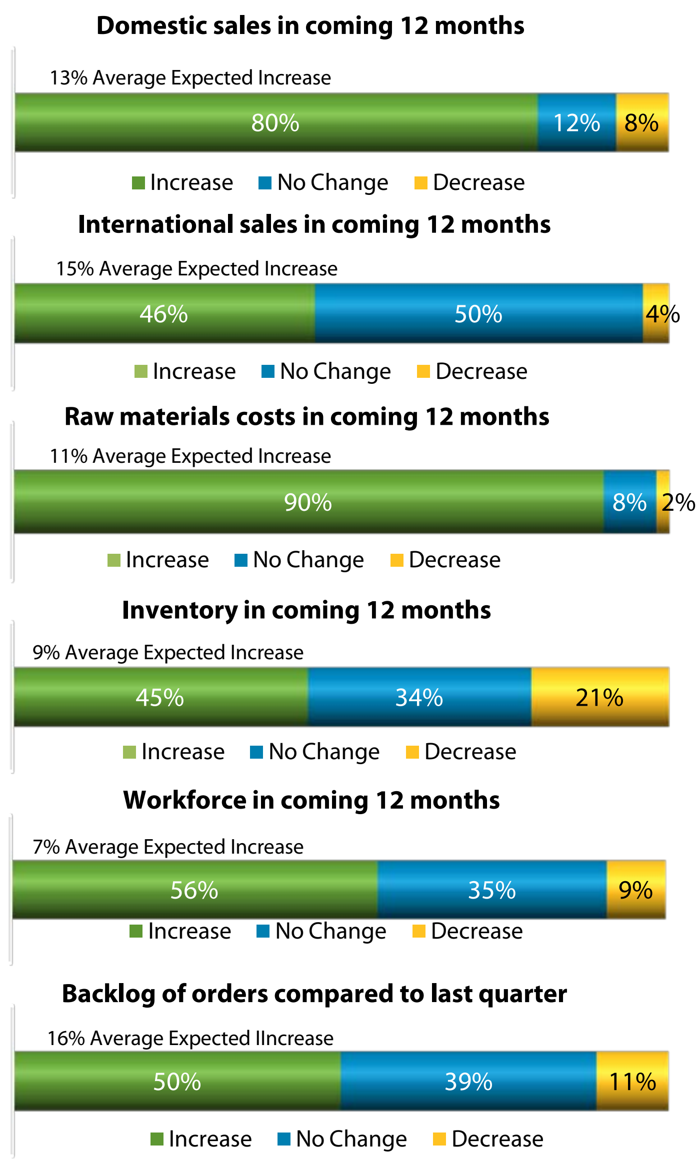
As in years past, respondents express more optimism about their own companies' economic prospects than for their industries overall. And they are far less optimistic about the U.S. or the world economy. They do see promise in emerging markets, however, and enthusiasm for emerging markets should draw smaller companies to Department of Commerce programs created to help firms ramp up export sales.

The most optimistic sectors overall are Computers and Electronics (41 percent "very optimistic") and Energy and Cleantech (36 percent "very optimistic"), mirroring their current strong performance. Optimism about the future tracks very closely with current prospects, with Furniture and Fixtures and Building Materials trailing all others.

Internal indicators overview

Each quarter, the Monitor will track and report anticipated changes in the coming 12 months for domestic sales, international sales, raw material costs, inventory, workforce, and change in backlog of orders. These quarterly benchmarks are key factors in assessing the current state of the industry and trending. Participants are able to track their individual responses on a web-enabled dashboard to gain more insight into how they compare to their peers over the quarters.

Quarterly benchmarks: Spring 2011



Key internal indicators all point to growth in the coming 12 months.

Most industries expect an increase in domestic sales this year. Automotive is particularly optimistic, with 92 percent of industry respondents reporting expected increases in domestic sales, as is Industrial Machinery with 87 percent expecting increases. Even the Textile and Apparel sector, which reports low current growth and optimism, has hope for the coming 12 months, with 72 percent forecasting gains in domestic sales.

Domestic sales optimism carries to respondent companies, which overwhelmingly (80%) expect to grow at an average of 13 percent over the next 12 months, while just under half (46%) of companies that expect to grow their international sales report a similar expected increase (an average of 15%).

"We're developing new products to reach new customers with raw materials coming from China for price competitiveness." – CFO, Automotive

More than half of the companies expect to increase their workforces by an average of 7 percent, and half see a more robust backlog of orders compared to last quarter—powerful signs of a recovering economy.

If there is one area of significant concern, it is the rise in raw material costs, which 90 percent of respondents expect to increase an average of 11 percent. However, commodity pricing is volatile. We have seen upward and downward changes since mid-April.

Other internal metrics

The table on page 11 ranks industry sectors by anticipated increase over the next 12 months and reported increase over the last quarter for backlog. The Automotive sector, for example, ranks highest (#1) for domestic sales (92% respondents in this sector expect an increase), whereas Textiles and Apparel rank lowest at 14th place with 72 percent expecting an increase.

Led by Transportation, Industrial Machinery and Energy and Cleantech, most industry groups report that half or more of their companies have larger backlogs this quarter than last. Those same industries show similar rankings in their workforce numbers, further supporting their elevated thriving and growing claims (Chart 2). Notable exceptions are Food and Beverage (25%), and Wood, Paper and Printing (26%).

Sectors reporting largest increases in backlogs and workforce are Industrial Machinery, Transportation and Energy and Cleantech.

Across all industries, 80 percent or more expect higher materials costs over the coming 12 months. Larger companies (i.e., those with annual revenue of $500 million or more) are less likely to expect increases in materials costs, because their size and buying power give them an edge unavailable to smaller companies. Companies in the Furniture and Fixtures, Transportation, and Metal Fabrication sectors are most likely to expect an increase in costs; those in Biotech and Medical are the least likely.

Three sectors—Automotive, Transportation, and Industrial Machinery—are more likely than the other industries surveyed to expect an increase in inventory. Carrying inventory of this type is typically expensive, so inventory levels were kept low during the recession in an effort to control cash flow and reduce interest costs. Because sales are projected to increase, on-hand inventory is now being increased to meet demand.

Two out of three industry sectors expect workforce increases over the coming 12 months, an excellent indication of returning economic health. As in other areas, Food and Beverage, Textiles and Apparel, and Wood, Paper and Printing have the lowest expectations of an increase.

Table 1

Sector Ranking Table: Anticipated and Reported Increase

	Domestic Sales (Coming 12 Months)		**International Sales** (Coming 12 Months)		**Material Costs** (Coming 12 Months)		**Inventory** (Coming 12 Months)		**Workforce** (Coming 12 Months)		**Backlog** (Since Last Quarter)	
	Rank	%	Rank	%	Rank	%	Rank	%	Rank	%	Rank	%
Automotive	1	**92%**	4	**80%**	3	**95%**	2	**57%**	6	65%	5	**55%**
Biotech and Medical	10	79%	11	73%	14	81%	4	**55%**	4	**66%**	12	40%
Building Materials	11	78%	6	79%	10	89%	8	47%	9	57%	6	53%
Chemicals, Oil and Plastics	3	85%	7	78%	9	91%	11	46%	8	60%	11	47%
Computers and Electronics	8	**80%**	5	79%	12	88%	12	43%	7	63%	8	52%
Energy and Cleantech	9	**79%**	1	**85%**	7	92%	10	46%	3	**69%**	2	**64%**
Fabricated Metal	5	83%	8	77%	4	**95%**	6	48%	5	**66%**	4	**58%**
Food and Beverage	12	77%	10	74%	11	88%	13	38%	12	43%	14	25%
Furniture and Fixtures	4	84%	14	55%	1	**97%**	5	**49%**	11	49%	9	51%
Industrial Machinery	2	87%	9	77%	5	94%	3	**56%**	2	**70%**	3	**64%**
Textiles and Apparel	14	72%	12	69%	6	93%	7	48%	13	41%	7	52%
Transportation	6	**82%**	3	84%	2	**96%**	1	**58%**	1	**71%**	1	**71%**
Wood, Paper and Printing	13	**74%**	2	85%	8	92%	14	31%	14	36%	13	26%
Other	7	82%	13	63%	13	87%	9	46%	10	56%	10	50%

Focus on sales growth goals and strategies

Overview of sales growth initiatives and strategic directions

Each quarter, the Monitor includes a topical selection of salient business issues. The Spring 2011 edition focuses on the ways companies are seeking to grow sales, including targeted markets and strategies they plan to employ. There is also an emphasis on international marketing initiatives, including where such initiatives are directed, the tactics used to advance them, and the implementation challenges companies anticipate.

Chart 3: Sales growth strategies by adoption and importance

With 80% of respondents expecting an increase in domestic sales, their companies are placing strong emphasis on both increasing sales to current customers and acquiring new customers. While focusing primarily on the domestic market, companies are also looking outward. As indicated in Chart 3, targeting sales outside of North America is more prevalent in 2011 than is the reliance on sales to Canada and Mexico, the nation's traditional trading partners.

While only 24 percent of respondents overall plan to target emerging markets, this segment of the sample considers it key to their strategic planning, with 37 percent rating it as "important" and 32 percent as "very important."

Approximately half of the respondents in the Automotive (52%) and Energy and Cleantech (51%) sectors plan to target Canada or Mexico. The sectors most likely to target markets outside North America are Energy and Cleantech; Computers and Electronics; Biotech and Medical; and Industrial Machinery.

"New product strategies will introduce value added engineered solutions that differentiate us in the marketplace. Expansion of business into Mexico and China will provide new sales opportunities." – Department Director, Metal Fabrication

New product introductions will play an important role in increasing sales to current customers and in acquiring new ones. In addition, companies plan to use new product offerings to increase their sales outside the U.S.

Implementation measures: pricing, geographic expansion and new products

Innovation is critical for increasing revenues to existing and new customers, including those operating both domestically and abroad. Innovation is not limited to the introduction of new products; it also can include enhancements to existing products, changes in the material inputs, improvements in supply chain and the identification of new applications. Ensuring successful innovation requires committing appropriate funds, without which companies risk inefficiently expending critical resources. – John Lanza, Partner, McGladrey & Pullen

Several tactics will be implemented during the coming 12 months as companies strive to make up for time and money lost during the recession. As previously discussed, the introduction of new products tops the list of growth-generating ideas. In addition, increased brand recognition will play an important role as companies begin to invest and focus once again on the basics of their business.

Chart 4 shows answers to the following question: Which of these tactical measures will your company rely on for achieving growth in the coming 12 months?

Chart 4: Percent of respondents employing each tactic

The primary difference in tactics between manufacturers and distributors: distributors are more focused on modifying sales structure and programs, including but not limited to rebates and purchase incentives.

Somewhat surprisingly, businesses also consider price increases a close second in priority to increasing brand recognition and ahead of entering new global markets. Clearly, respondents feel more confident about their business and the economy to increase prices given the downward pressure in 2009 and 2010. Reducing prices, often considered a key tactic for seizing market share, is the least employed tactic among all those rated. The emphasis is on aggressive expansion rather than strategic retreat or "buying the business." Manufacturers are more likely than distributors to consider raising prices.

Industries in which more than 60 percent of respondents indicate plans to raise prices include Textiles and Apparel, Food and Beverage, and Computers and Electronics. Least likely to consider price increases are Energy and Cleantech and Industrial Machinery. Also less likely to consider raising prices are companies focused on entering new international markets or increasing sales in their existing international markets.

International growth prospects

Overall, 17 percent of companies surveyed have a presence in Canada and/or Mexico and 24 percent of companies in the survey have a presence outside North America. Manufacturers report a slightly larger presence in international markets than do distributors. Manufacturers that outsource are influenced by distribution agreements, which may have geographical limitations, and the preference to work with local distributors.

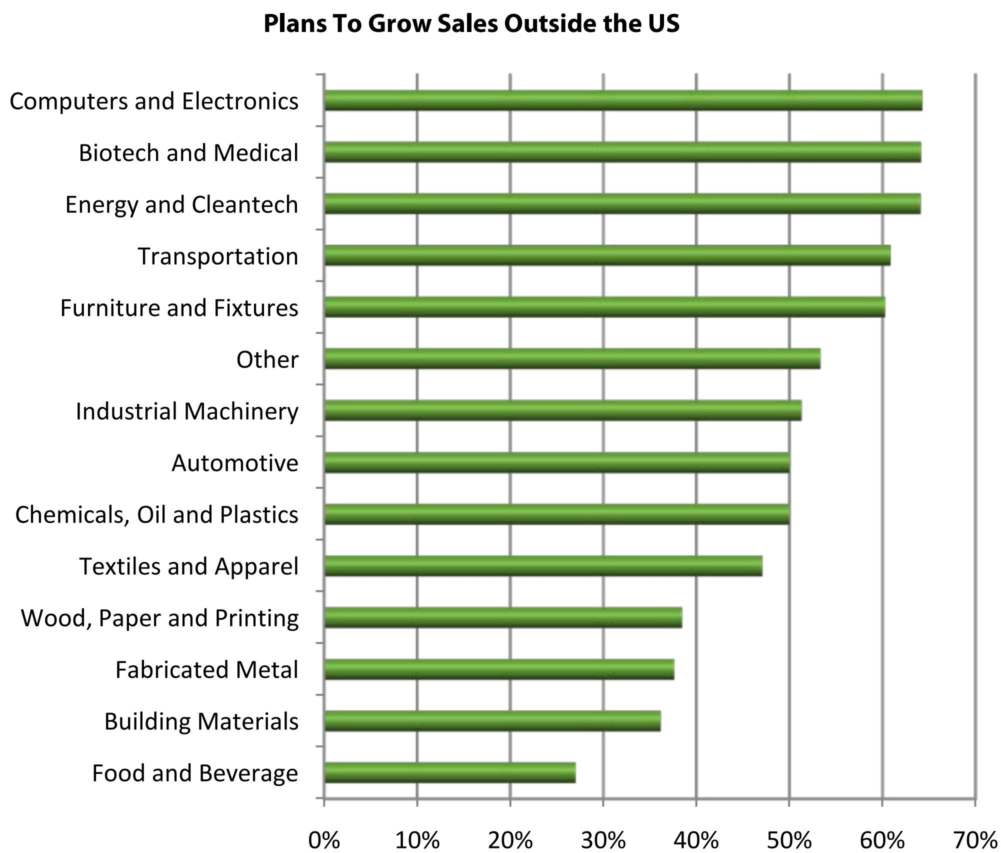
Hot sales markets include Canada, Mexico, Western Europe, and China, with manufacturers reporting a larger sales presence than distributors.

Companies expect to continue their international sales push this year, with 48 percent overall reporting plans to enter or expand sales in non-U.S. markets. Manufacturers take a large lead here, with 58 percent reporting this intention, compared to only 19 percent of distributors.

Every industry reports some level of intent to tackle markets outside the U.S., but the leaders are technology-related industries: Biotech and Medical; Energy and Cleantech; and Computers and Electronics.

U.S. monetary policy, coupled with stronger international expansion in general, have made U.S. exports more attractive. Agreements with manufacturers usually restrict distributors to regional and national territories; transportation and other logistics issues can also play a role. However, a number of distributors have developed exclusive relationships with manufacturers allowing them to expand in selected foreign markets; others have identified foreign market needs for which they provide an effective supply chain solution. – Bob Jirsa, Partner, McGladrey & Pullen

Chart 5: Percent of respondents planning to expand sales outside the U.S. by industry sector



> We have seen a 70% increase in our clients who are seeking advice for working with companies in Brazil. There is much economic activity taking place in this part of the world. Our clients need assistance with understanding the complex regulatory and tax landscape as they look to enter or expand into this market. – Karen Kurek, National Manufacturing Practice Leader, RSM McGladrey

Regardless of the geographic target, the primary goal is to expand sales in current markets versus opening up new ones. Canada and Western Europe, in particular, are prime expansion areas. Brazil, China and India (the so-called "BRICs" minus Russia) and Southeast Asia top the list of markets targeted for entry.

Biotech and Medical is the sector most focused on emerging markets, while Automotive is the most likely to target Canada and Mexico. Energy and Cleantech is the industry sector most focused on selling outside North America.

> We have seen an increase in revenues for clients operating on a global basis; however, most have sales in excess of $100 million. The challenge for small and medium-sized manufacturers is determining how to leverage both government and private resources to enter and expand in new markets. There are costs of both money and time associated with competing internationally. – Frank Le Bihan, Managing Director, RSM McGladrey

The Biotech and Medical sector is most interested in *entering* the Brazilian market, while Industrial Machinery is keenest to *expand* sales in Brazil. Companies in the Biotech and Medical sector, along with those in Computers and Electronics, are most eager to break into India, while Industrial Machinery leads others in plans to expand Indian sales. The industry most eager to enter the Chinese market is Textiles and Apparel, while the sectors most interested in expanding sales there are Chemicals, Oil and Plastics; Industrial Machinery; and Metal Fabrication.

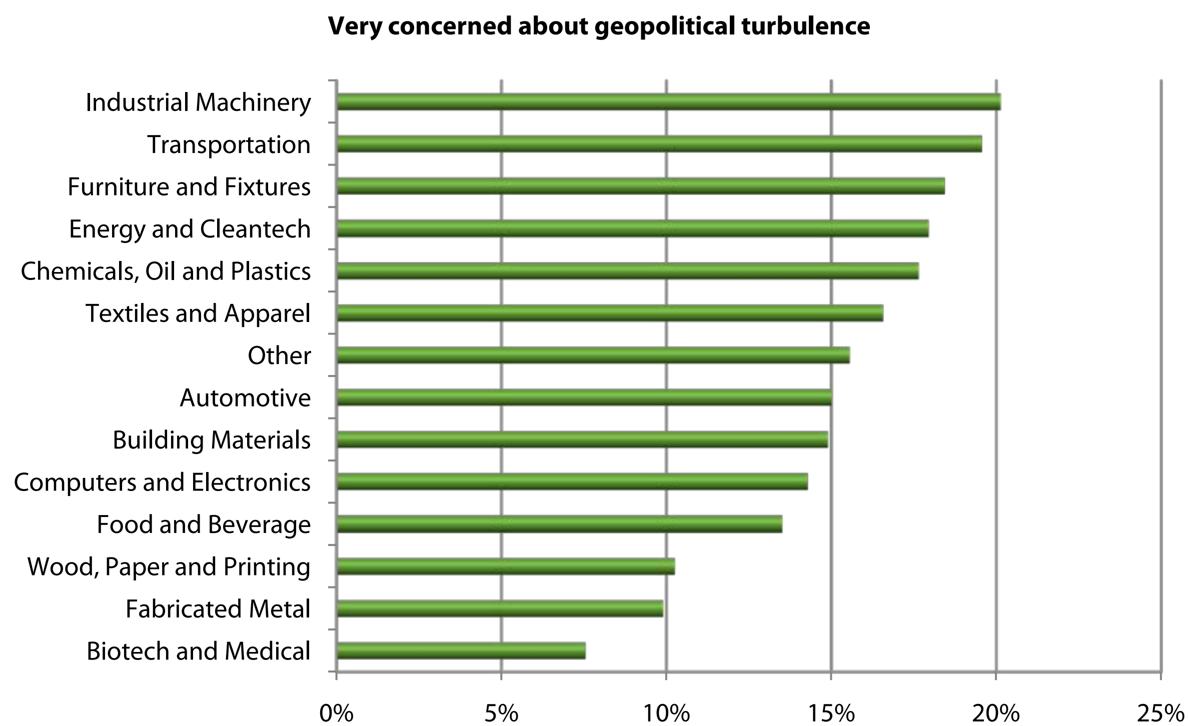
"Our business is based on new product introductions as most of our products are custom to the customer's application. We are focusing our attentions on gaining share in Brazil and growing in the U.S. domestic market." – CFO, Food and Beverage.

Risk profile: challenges to growth prospects

Geopolitical challenges to growth

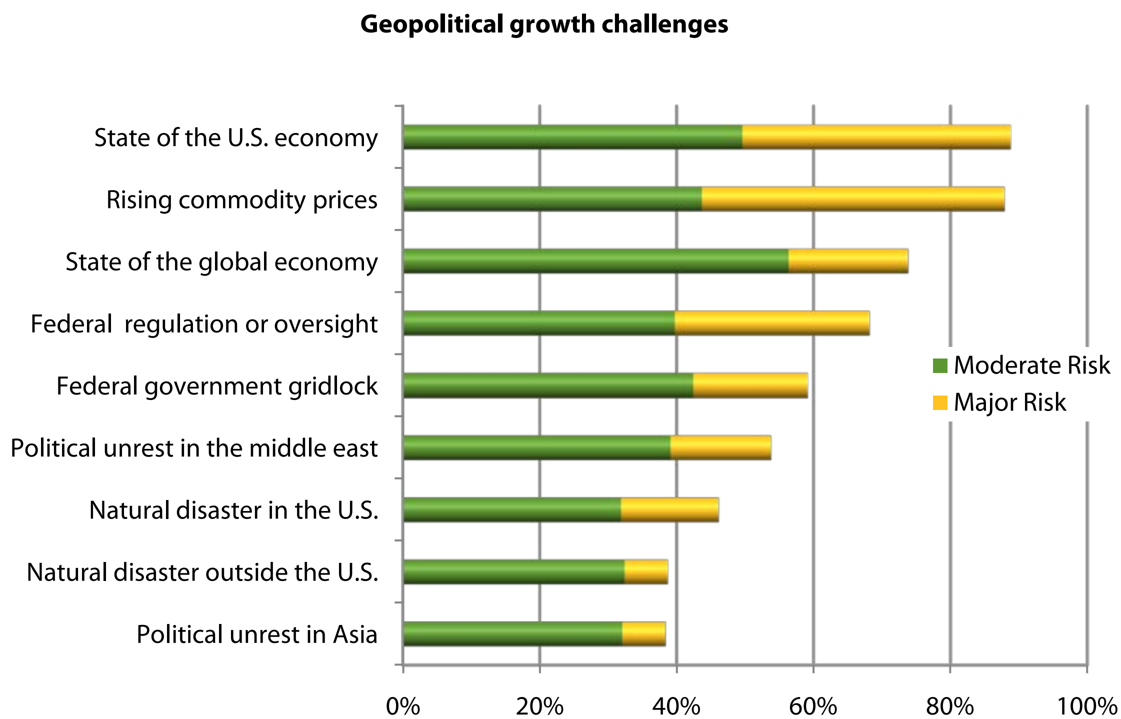
Respondents were asked to rate their concern regarding the potential impact of geopolitical turbulence on their growth prospects. (For context, please note that the day after the survey launched, Japan suffered one of the most cataclysmic earthquakes in history. At the same time, revolutionary events were sweeping through Tunisia, Egypt, Libya and other Middle Eastern nations.)

Chart 6: Geopolitical concerns by industry



There was little difference in responses from manufacturers and distributors, but industry sector did affect perspectives. As Chart 6 indicates, 20 percent of respondents from the Industrial Machinery sector express great concern about the negative impact of geopolitical turbulence, compared to less than 10 percent of the Biotech and Medical industry.

Chart 7: Perceived risk factors domestic and international



Looking a bit deeper, Chart 7 shows the percentage of respondents who expressed "moderate" or "major" concerns about various potential growth challenges. They were asked to sort each event according to the perceived level of risk to their business growth in the coming year.

During 2010, we became increasingly aware of how proposed legislative and regulatory issues were going to impact companies. While uncertainties remain in 2011, the federal and many state governments appear to have heard the cries of business leaders and are responding with promises of less regulation and more pro-business policies. Still, we believe the uncertainty will continue and encourage companies to stay involved and express their views. – Steve Menaker, Partner, McGladrey & Pullen

The U.S. economy and commodity prices led the risk pack, with 86 percent and 85 percent (respectively) seeing them as major or moderate risks to business growth. Commodity prices pose a major risk to 43 percent of the respondents. Upwards of 50 percent see a risk in the federal government's over-regulating of their industries or failing to function due to political gridlock. Almost half are concerned about political unrest in the Middle East.

The day after the Spring 2011 survey was launched (March 10), Japan suffered one of the worst earthquakes in its history. Despite ongoing worldwide coverage of Japan's overwhelming devastation, natural disasters concern the fewest number of respondents.

Projected 12 month impact of rising commodity prices

Rising commodity prices are expected to have a negative impact on the majority of industries polled. The strongest impact is anticipated in the form of increased raw materials costs. As costs of materials increase, margins decrease.

Chart 8: Perceived effects of rising commodity prices

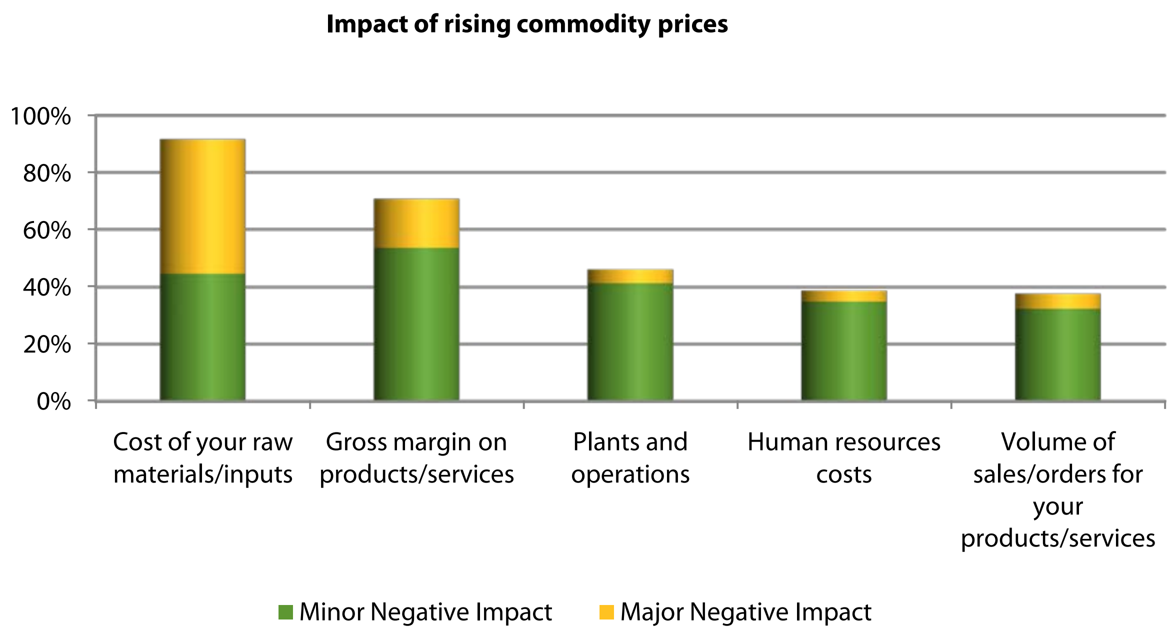


Chart 8 indicates the percentage of respondents who expect a negative impact on various aspects of their businesses from rising costs of raw materials. Concerns about raw material prices and their impact on key inputs are almost universal at 92 percent. Executives in the Textiles and Apparel sector are most concerned: 70 percent of industry managers expect a major negative impact on raw materials costs. Biotech and Medical companies are least worried about the impact of raw materials costs, but 72 percent see some negative impact on gross margins.

Many commodities critical to the manufacturing industry experienced a significant rise during late 2010 and early 2011. While pricing seems to have stabilized, at least temporarily, in the second quarter of 2011, managing commodity pricing is critical. Establishing a formal strategy to deal with these fluctuating prices might include hedging through derivatives, placing long-term purchase commitments or looking for lower cost substitute materials. – Steve Menaker, Partner, McGladrey & Pullen

Almost all (96%) of respondents in the Industrial Machinery sector see either major or minor negative impact on raw materials costs, followed closely by Transportation, Chemicals, Oil and Plastics, and Wood, Paper and Printing.

Industries most likely to expect some negative impact on their gross margins are Energy and Cleantech, Fabricated Metal and Biotech and Medical.

Conversely, rising commodity prices offer potential benefits to one industry in particular: companies in the Energy and Cleantech sector expect rising prices to have a positive impact on their volume of sales, compensating for expected lower gross margins. The Energy and Cleantech field can, of course, be expected to benefit as the price of oil rises to prohibitive levels and companies seek alternative sources of energy.

The Summer 2011 edition of the McGladrey Manufacturing & Distribution Monitor will launch at the beginning of June. For more information, visit our web site, or manufacturing blog.

Monitor respondent composition

Manufacturing and distribution		
Manufacturing	475	53%
Distribution	204	23 %
Mostly Manufacturing, Some Distribution	134	15%
Mostly Distribution, Some Manufacturing	91	10%

Titles and job functions		
CFO, Senior Finance Executive	312	35 %
CEO, President or Chairman	304	34 %
Chief Operating Officer	37	4 %
Chief Marketing or Sales Officer	20	2 %
Principal/Managing Partner/Partner	18	2 %
Executive Management	29	3 %
Finance Managers	127	14 %
HR Managers	8	1 %
Operations Managers	24	3 %
IT Managers	15	2 %
Legal Managers	2	0 %
Marketing/Sales Managers	8	1 %
Other	213	24 %

Employees (full time)		
0-49	187	21 %
50-499	535	59 %
500-1,999	130	14 %
2,000 or more	52	6 %

Annualized revenue		
<$25M	330	37 %
$25M -<$100M	295	33 %
$100M - <$500M	204	23 %
$500+M	75	8 %

Ownership model		
Private or closely held	662	73 %
Private equity owned business	127	14 %
Publicly traded corporation	68	8 %
Division/Unit of Larger Co	47	5 %

Industries		
Metal Fabrication	154	17 %
Industrial and Commercial Machinery	141	16 %
Food and Beverage	101	11 %
Building Materials	94	10 %
Chemicals, Petroleum and Plastics	68	8 %
Automotive (OEM and Aftermarket)	60	7 %
Computers, Electronics and Electrical Components/Appliances	56	6 %
Biotech, Life Sciences and Medical Equipment/Supplies	53	6 %
Textiles, Apparel and Accessories	46	5 %
Transportation Equipment (Other Than Automotive)	45	5 %
Energy and Cleantech	39	4 %
Wood/Paper Products and Printing	39	4 %
Furniture and fixtures	37	4 %
Other	291	32 %