RSM US LLP and The Harris Poll have collected data on middle market firms from a quarterly survey that began in the first quarter of 2015. The survey is conducted four times a year in the first month of each quarter: January, April, July and October. The survey panel, the Middle Market Leadership Council, consists of 700 middle market executives, and is designed to accurately reflect conditions in the middle market. The data is weighted to ensure that they correspond to the U.S. Census Bureau data on the basis of industry representation.

A reading above 100 for the MMBI indicates that the middle market is generally expanding; below 100 indicates that it is generally contracting. The distance from 100 is indicative of the strength of the expansion or contraction.

In March 2020, RSM began conducting the economic portion of the MMBI survey on a monthly basis to capture the effects of the COVID-19 crisis on the middle market. The report was fielded between Jan. 11 to Jan. 29, 2021, and based on the responses of 400 participants.
RSM US LLP and the U.S. Chamber of Commerce have joined forces to present the RSM US Middle Market Business Index (MMBI)—a first-of-its-kind middle market economic index developed by RSM in collaboration with Moody’s Analytics, the financial intelligence provider. We publish the MMBI quarterly to give voice to the middle market and raise awareness of this crucial, yet underrepresented, segment of the economy.
DESPITE THE CHALLENGES POSED BY THE MOST INTENSE PHASE OF THE PUBLIC HEALTH CRISIS, SENTIMENT AMONG MIDDLE MARKET BUSINESS EXECUTIVES ROSE IN JANUARY.

JOSEPH BRUSUELAS, CHIEF ECONOMIST, RSM US LLP

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This publication represents the views of the author(s), and does not necessarily represent the views of RSM. This publication does not constitute professional advice.
“Buoyed by the vaccine distribution and the promise of a fully reopened economy, we are seeing growing optimism from the middle market about the economy’s future,” said U.S. Chamber Executive Vice President and Chief Policy Officer Neil Bradley. “Back to business is the way forward, and the middle market is at the crux of the U.S. economic recovery. There are important legislative and policy initiatives ahead, and we’ll be working alongside the middle market to create a robust business environment in 2021.”

The RSM US Middle Market Business Index for the first quarter rose to 124 on the month, up from 121 in December. It is the highest reading since October, though it is still below its pre-pandemic level.
INDEX FOR JANUARY REACHES HIGHEST LEVEL SINCE OCTOBER

BY JOSEPH BRUSUELAS, CHIEF ECONOMIST, RSM US LLP

DESPITE THE CHALLENGES posed by the most intense phase of the public health crisis, sentiment among middle market business executives rose in January, according to the proprietary RSM US Middle Market Business Index.

The index, part of the RSM US Middle Market Business Index survey for the first quarter, improved to 124 on the month, up from 121 in December. It is the highest reading since October, though it is still below its pre-pandemic level. The increase in the seasonally adjusted and nonseasonally adjusted index in January is significant at levels of 0.05 and 0.10.

The juxtaposition of the rising sentiment in the RSM survey and the tepid economic data over the past few months remains in place.

Current sentiment around the economy, gross revenues and net earnings remains challenged at best among those surveyed, while the forward-looking questions on the same topics in the RSM survey point toward a rapid reflation of the economy with the return of constructive net earnings and revenues as the economy reopens.

Most important, as the economy reflates, the majority of middle market firms are not passing along price increases associated with the reconstitution of demand, although a majority of executives said that they intended to do so later this year, which requires close monitoring as the economy reopens.

The economic deceleration into the first quarter of the year is clear in the data. Only 29% of executives noted an improvement in overall economic conditions, 39% noted a deterioration and 28% implied no change. That rather bleak view is tempered by the 56% of executives who expect improvement in the next six months.

While the current view of the economy is somewhat bleak, a plurality of respondents, or 44%, noted a current improvement in gross revenues and 43% indicated an improvement in net earnings. Like their forward view on the economy, 60% of the executives indicated they expect an improvement in gross revenues over the next six months and 59% anticipate growth in net earnings.

Given that the economy is operating at near 80% capacity as middle market firms begin to prepare for what we expect to be a hypercompetitive, post-pandemic
The optimism around expectations about the economy, earnings and revenues is the primary impetus behind the improvement in overall middle market business sentiment to kick off the year.

The survey found that 56% of respondents said that they are going to increase hiring, 55% are going to increase compensation and 48% are going to increase outlays on productivity-enhancing capital expenditures.

This should be a clarion call to middle market firms that are now beginning to think through what the economic landscape will look like following a once-in-a-hundred-year pandemic.

That optimism, however encouraging, stands in contrast with the 44% of executives who increased hiring in the current quarter, the 42% who increased compensation and the 38% who increased capital expenditures.

One important note: In the comments that executives could add to their survey responses, participants across a range of industrial sectors said they were moving aggressively to increase spending on improving productivity. Others, in contrast, remained quite cautious and expressed uncertainly about the path ahead on the integration of technology into the production of goods and provision of services.

We strongly urge firms to consider the investment opportunity around real negative interest rates for middle market firms.

One of the more interesting developments inside the middle market outlook is the evolving sentiment on inflation. Currently, 66% of respondents noted an increase in prices paid, but only 41% of survey participants reported passing those prices through to clients. This six-month average of prices paid stands at 60% and that same metric for prices received rests at 42%, both near current levels. Looking forward, 67% expect prices paid to rise over the next six months and 60% state that they intend to pass along those price increases to customers; both figures were above their respective levels of 63% and 52% observed over the past six months.
What executives said about business challenges

The executives who took part in the RSM US Middle Market Business Index survey were asked to describe a top business problem facing their organization. These responses reflected a range of concerns, including the threat of ransomware attacks and the continuing impact of COVID-19. The challenge of securing data—always a concern—has only become more acute as workers have shifted to remote locations during the pandemic.

Among their replies:

- “Due to COVID–19, our organization cannot provide new technology for securing the company data from fraud and cyberattacks,” said an executive in the retail trade sector.
- “Cybercrime and security,” said an executive in the finance and insurance sector.
- “Data protection,” said an executive in the waste management and remediation services industry.
- “Cybersecurity attacks from outsiders and also networking/cloud problems,” said an executive in the finance and insurance sector.

The attacks can have a financial impact on businesses, which led one executive in the retail trade sector to comment on trying to ease the potential damage, saying, “Bought cyber insurance.”

The executives’ responses also showed that the problem is nothing new. “Every year we find ourselves attacked,” said an executive in the construction industry.

And it seemed that the need to keep up with technological advancements—which have only been accelerated by the pandemic—has grown: “Lack of enough funds to buy the best information technology software and hardware,” said one executive who works in educational services.

The concerns were not isolated to cybersecurity when executives were asked to describe a top business problem. One executive whose firm operates in the professional, scientific and technical services sector cited “COVID–19, which has direct impact on sales and marketing, lowering our achievements and goals as a company.”

An executive in transportation and warehousing was more direct, saying: “COVID–19 is very bad and the principal problem.” Same with another executive, who works in the wholesale and trade industry: “Decreased demand due to the pandemic.”

This implies that current concerns about an immediate and permanent increase in the price level—that is the definition of inflation—are overblown. But it will be interesting to see if firms that for years have not been in possession of pricing power suddenly find that power and clients willing to accept higher costs.

Given the modest backup in interest rates and inflation expectations—both remain below 2%—this will be one of the more interesting economic narratives this year. Right now, firms that constitute the beating heart and soul of the real economy are not pointing to a near-term risk in pricing to the economic outlook.

Current and expected fiscal support may be a boon for middle market firms that have access to more credit options as the question on borrowing, or how easy it is to obtain credit, swings back into positive territory. The lending environment is tight, but it is not getting any tighter thanks to help from policymakers.

Survey respondents continue to remain cautious on the rebuilding of inventory levels, with 43% indicating current improvement and 49% stating they expect to do so over the next six months.
GENERAL ECONOMY PERFORMANCE

Thirty-nine percent of respondents said the economy worsened in January, down from 43% in December.

GROSS REVENUE PERFORMANCE

Forty-four percent of executives surveyed said gross revenues improved in January, on par with December.
NET EARNINGS PERFORMANCE
Forty-three percent of respondents noted an increase in net earnings in January, while 59% expected improvement over the next six months.

AGGREGATE CAPITAL EXPENDITURES/INVESTMENTS PERFORMANCE
Thirty-eight percent of executives said their businesses made capital investments in January, down from 41% in the month-earlier period.
OVERALL HIRING LEVELS

Hiring increased in January, with 44% of executives indicating they added staff, compared to 39% in December.

EMPLOYEE COMPENSATION

Forty-two percent of executives said their businesses boosted compensation in January, up sharply from 33% in December. More than half expect to increase compensation over the next six months.
ACCESS TO CREDIT

Access to credit improved in January, with 29% of executives noting more favorable conditions, up from 24% in December.

PLANNED BORROWING

Forty percent of respondents said they planned to increase borrowing over the next six months, consistent with responses from the prior month.
**AMOUNT PAID FOR GOODS AND SERVICES**
Prices paid for goods and services were higher in January, according to 66% of executives surveyed. That’s up from 60% of respondents in December.

**AMOUNT RECEIVED FOR GOODS AND SERVICES**
Sixty percent of middle market executives expected their organizations to charge more for goods and services over the next six months, up from 52% in December.
How the MMBI is constructed

The MMBI is borne out of the subset of questions in the survey that ask middle market executives to report the change in a variety of indicators. Middle market executives are asked a total of 20 questions patterned after those in other qualitative business surveys, such as those from the Institute of Supply Management and the National Federation of Independent Businesses.

The 20 questions relate to changes in various measures of their business; such as revenues, profits, capital expenditures, hiring, employee compensation, prices paid, prices received and inventories. Middle market executives are asked to report the change from the previous quarter and to state the likely direction of these same indicators six months ahead. See a sample of the questions in the table.

The MMBI is a composite index computed as an equal weighted sum of the diffusion indexes for 10 survey questions plus 100 to keep the MMBI from becoming negative. The index is designed to capture both current and future conditions, with five questions on middle market executives’ recent experience and five on their expectations for future activity.
MIDDLE MARKET COMPANIES saw a sharp uptick in cyberattacks in the past year, Middle Market Business Index research found, as they faced new information technology safety challenges amid the shift to remote work during the pandemic. Meanwhile, confidence to thwart attacks remained high, as businesses took steps that included adding security staff, improving the protections of their remote workforce solutions and upgrading hardware, among other measures.

The first quarter 2021 MMBI survey, which gathered responses from 400 executives from Jan. 11 to Jan. 29, included a host of special questions dedicated to data security. Twenty-eight percent of respondents said they experienced a data breach, up from 18% a year earlier, the highest level since RSM began surveying respondents about cybersecurity in the first quarter of 2015.

A full 64% of executives queried said they expected unauthorized users to attempt to breach their systems this year, up significantly from 55% a year ago. Even so, a strong 93% majority remained confident their organizations had the measures in place to guard their customer information from unauthorized use. This may be due, in part, to renewed efforts to protect their flanks; a full 90% said their organizations had taken actions to bolster their IT security.

Thirty-three percent of executives said their companies had experienced a ransomware attack in the past year, and slightly more than half said their organizations had been the target of a business takeover attempt. However, education about cyberthreats is on the rise, with 90% of businesses offering formal training to some or all of their employees, compared to 82% a year earlier.

Data privacy regulation to protect consumer information appears to be gaining traction in the United States, with the Biden administration expected to introduce legislation on the national level. Awareness of this issue was reflected in the survey responses, with 92% of executives indicating their organizations will likely have to comply with privacy regulations during the next two years.

Please watch for the full MMBI special report on cybersecurity issues due in April.
For more information on RSM, please visit [www.rsmus.com](http://www.rsmus.com).

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