RSM US MIDDLE MARKET

BUSINESS INDEX

IN PARTNERSHIP WITH THE U.S. CHAMBER OF COMMERCE

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RSM US MIDDLE MARKET BUSINESS INDEX

IN PARTNERSHIP WITH THE U.S. CHAMBER OF COMMERCE

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 April 7 to April 28, 2021, and based on the responses of 404 participants.

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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.

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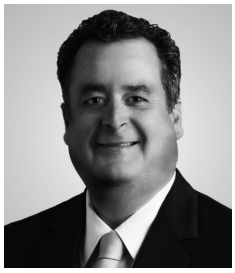
WHEN LOOKING TO THE NEXT SIX MONTHS, 74% OF RESPONDENTS EXPECT AN IMPROVED ECONOMY, 72% ANTICIPATE BETTER REVENUES AND 71% EXPECT RISING NET EARNINGS.

JOSEPH BRUSUELAS, CHIEF ECONOMIST, RSM US LLP



Joseph Brusuelas is the chief economist for RSM US LLP. Brusuelas has 20 years of experience analyzing U.S. monetary policy, labor markets, fiscal policy, economic indicators and the condition of the U.S. consumer. As co-founder of the award-winning *Bloomberg Economics Brief*, Brusuelas was named one of the 26 economists to follow by the *Huffington Post*. In addition, he was named 2020 Middle Market Thought Leader of the Year by The Alliance of Merger & Acquisition Advisors. A member of the *Wall Street Journal*'s forecasting panel, Brusuelas regularly briefs members of Congress and other senior officials regarding the impacts of federal policy on the middle market and the factors by which middle market executives make business decisions.

"Encouraged by vaccine distribution and loosening restrictions, there is a great amount of optimism from the middle market as business comes back and leaders see more good times ahead," said U.S. Chamber Executive Vice President and Chief Policy Officer Neil Bradley. "The middle market has shown tremendous resilience and has been crucial in leading the country's economic recovery. We'll be working alongside the middle market in 2021 to continue to navigate important legislative and policy issues to get back to business."

The increase to 132.1 in April from 128 in March is statistically significant at a 0.05% level with seven of the 10 questions in the survey about business conditions improving over the past months.

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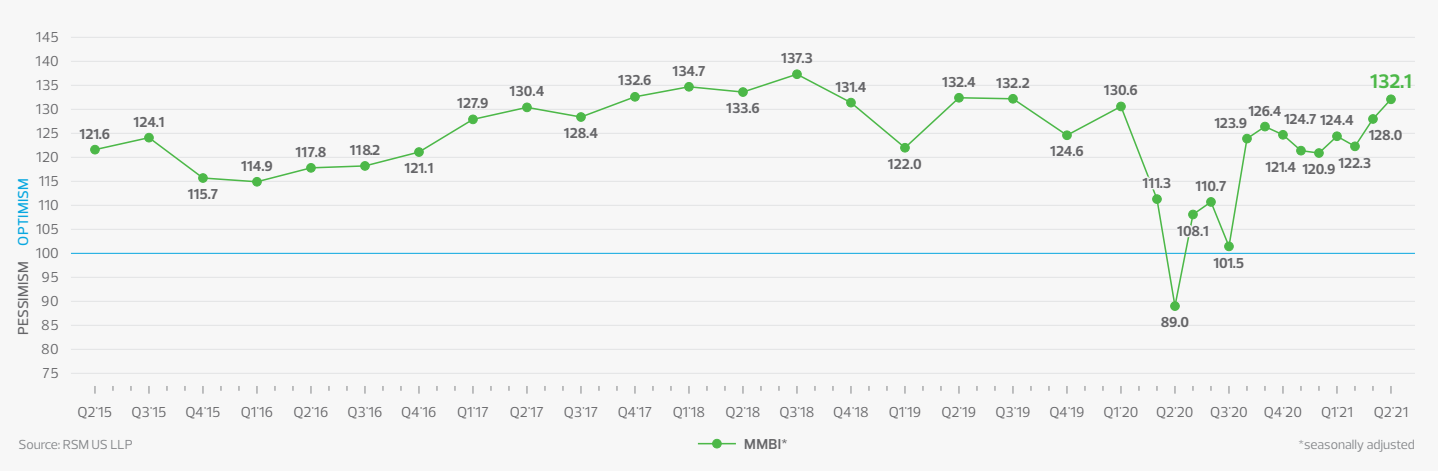


ECONOMIC PROSPECTS IMPROVING AMID COST PRESSURES

Middle market business conditions improved in April as the prospect of rising revenues and net earnings offset cost pressures.

BY **JOSEPH BRUSUELAS**, CHIEF ECONOMIST, RSM US LLP

MIDDLE MARKET BUSINESS CONDITIONS improved in April as the prospect of an economic boom, rising revenues and surging net earnings this year more than offset evidence of increasing prices paid and record expectations of further cost increases.

The increase in the proprietary RSM US Middle Market Business Index to 132.1 in April from 128 in March is statistically significant at a 0.05% level with seven of the 10 questions in the survey about business conditions improving over the past month. The three other questions were either unchanged or declined.

Roughly half of respondents reported an increase in revenues and net earnings in the recent quarter, which is a touch below the pre-pandemic 2019 average and is another sign of the underlying resilience inside the American middle market. The survey was taken from April 7 to April 28, before the Colonial Pipeline shutdown disrupted gasoline distribution on the East Coast.

The undeniable strength in middle market business conditions is best illustrated by the strong jump in current economic prospects over the past two months from 34% of survey respondents indicating an improvement in overall economic conditions in February to 49% in April. This is matched by the increase to 47% of respondents noting an improvement in gross revenues and 48% in net earnings in the most recent quarter.

When looking to the next six months, 74% of respondents expect an improved economy, 72% anticipate better revenues and 71% expect rising net earnings. These responses underscore the noticeably improved condition of the American real economy through the first quarter of the year, which had a 6.4% increase in gross domestic product.

Perhaps most encouraging is that 62% of survey respondents said that they intended to engage in productivity-enhancing capital expenditures over the next six months in contrast with the 35% who in April said they did so over the recent quarter. We do anticipate a hypercompetitive post-pandemic economy that will feature the pulling forward of a decade's worth of technology into the next few years, so this is a positive development in both the long run and in the near term.

Why the near term? Because it is clear that pricing pressures associated with the reopening of the economy are at the forefront of middle market business concerns. Roughly 82% of respondents said they expect to pay more for the inputs used in their operations over the next six months, breaking the record set in last month's survey.

Surging demand will continue to constrain supply chains, which remain impaired because of the chaos of the past year. It was clearly easier to shut down the economy than it is to reopen one. Restoring those supply chains will not

be a linear process. It will be profoundly nonlinear, causing production and delivery headaches and placing additional upward pressure on prices.

That being said, despite 69% of respondents stating in April that they paid higher prices for goods this quarter compared to the previous quarter, only 43% noted in April that they received prices downstream this quarter, which is broadly in line with the long-term average in the history of the time series.

While there is little argument that prices are on the rise following steep declines into the depths of the pandemic last year, they are moving back toward pre-pandemic levels, and for now, the majority of survey participants are not facing significant problems linked to inflation. Otherwise, we would be observing a much greater rate of pass-through in inflation to downstream clients.

Traditionally, early in economic recoveries, goods prices tend to increase first, followed by service costs, which compromise the overwhelming majority of the modern economy. But it is important to note that there are some ways to go before service-sector prices move back toward their pre-pandemic levels.

For example, airfares rose 10% in April and are up more than 16% compared to May 2020. Yet they are down 17% from where they were before the pandemic. This is a perfect example of price variation and volatility and not inflation. Despite an increase in prices paid at earlier stages of production and what are clear constraints in the supply of available services, whether they be commercial aircraft or hotel rooms, we are not yet ready to label this price recovery a precursor of 1970s-style inflation.

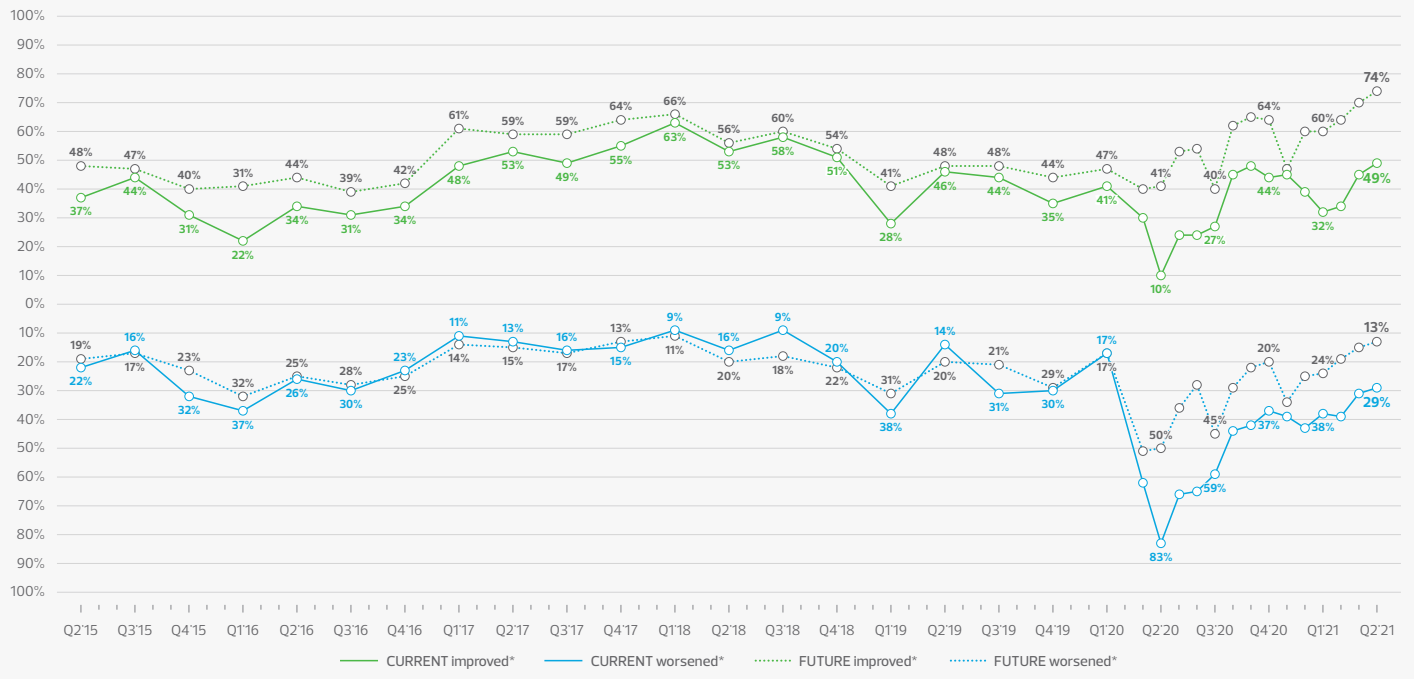
Service sector inflation, which the economy has not materially experienced since the 1980s, is driven by wage gains. The April middle market business survey tends to suggest that wage gains are restrained, but could pick up later this year.

Employment remains muted with only 39% of respondents indicating in April that they stepped up hiring in the recent quarter compared to the previous one, with 60% indicating they intend to do so over the next six months. Compensation increases also remained restrained, with 39% in April noting they paid more for labor, and 64% implying they will pay more to recruit and retain labor. This denotes that service-sector inflation, which is up 2.4% on a year-ago basis, will most likely rise as it traditionally does emerging from economic downturns.

Middle market survey participants continue to carefully manage inventories with only 33% of respondents in April noting an increase in the level of existing stock during the recent quarter compared to the previous one. As one would expect given middle market anticipation of growth as the economy fully reopens later this year, 54% of respondents expect to increase inventory purchases over the next six months. ■

GENERAL ECONOMY PERFORMANCE

Forty-nine percent of respondents said the economy improved in April, up from 32% in January.



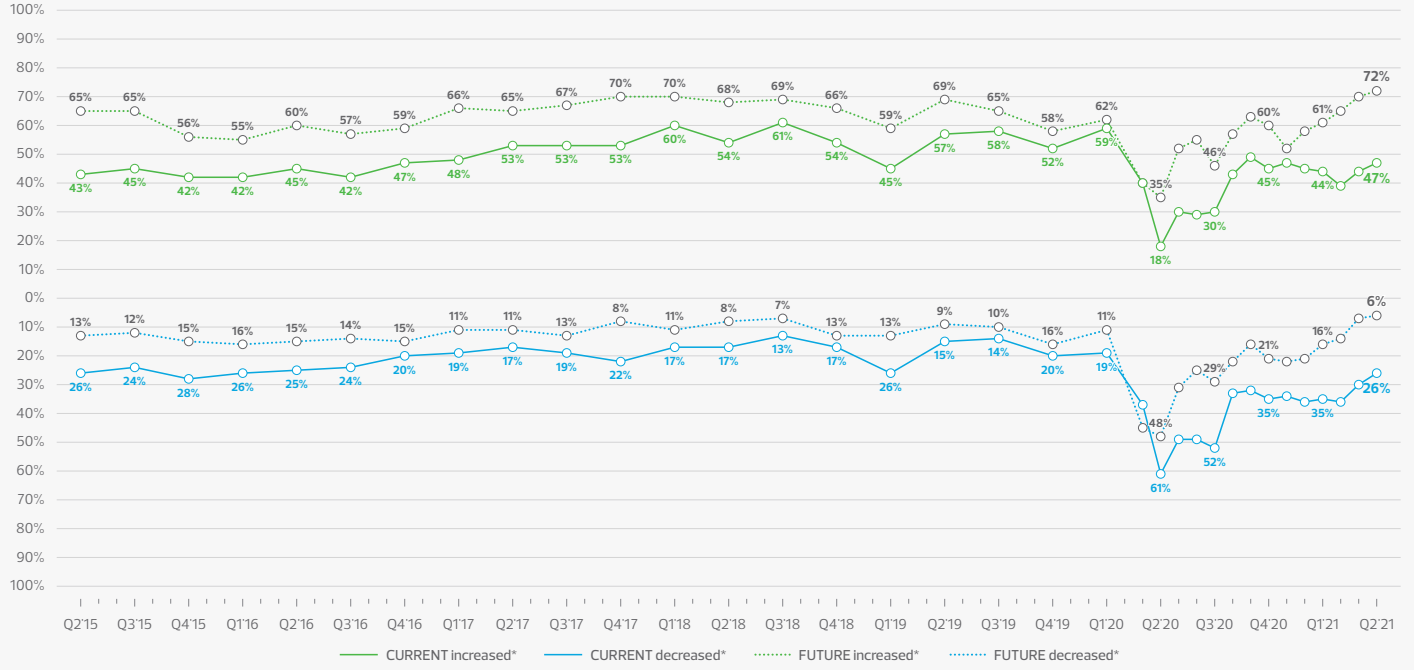
- First, thinking about the general economy this quarter versus last quarter, how would you describe the current general economy? Would you say the general economy has . . .?
- What are your expectations regarding the general economy over the next six months? Do you expect the general economy will . . .?

SQUARE/CIRCLE = Significantly higher/lower than previous quarter, respectively, at 0.05 level of significance

*seasonally adjusted

GROSS REVENUE PERFORMANCE

Forty-seven percent of executives surveyed said gross revenues improved, an uptick from the month prior.



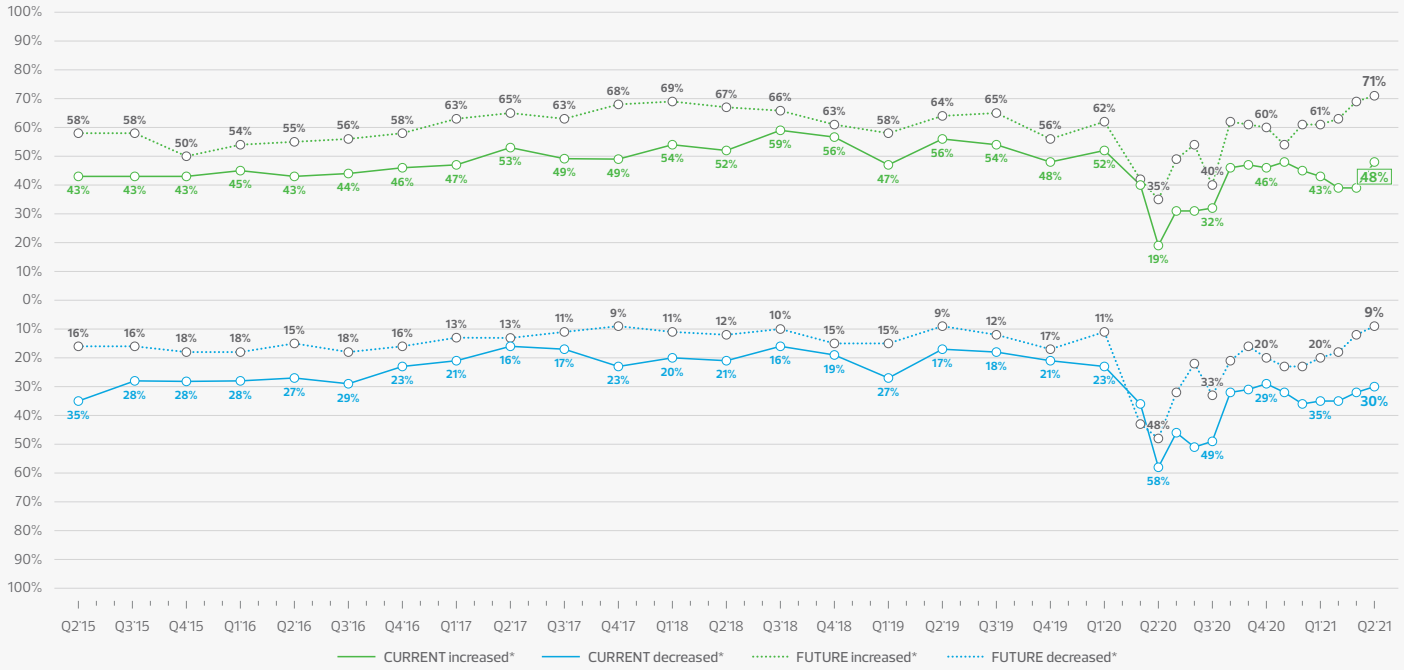
- Thinking about your organization's gross revenues/all incoming funds this quarter versus last quarter, how would you describe current gross revenues/all incoming funds? Would you say gross revenues/all incoming funds have . . .?
- What are your expectations regarding your organization's gross revenues/all incoming funds over the next six months? Do you expect gross revenues/all incoming funds to . . .?

SQUARE/CIRCLE = Significantly higher/lower than previous quarter, respectively, at 0.05 level of significance

*seasonally adjusted

NET EARNINGS PERFORMANCE

Forty-eight percent of respondents noted an increase in net earnings in April, while 71% expected improvement over the next six months.



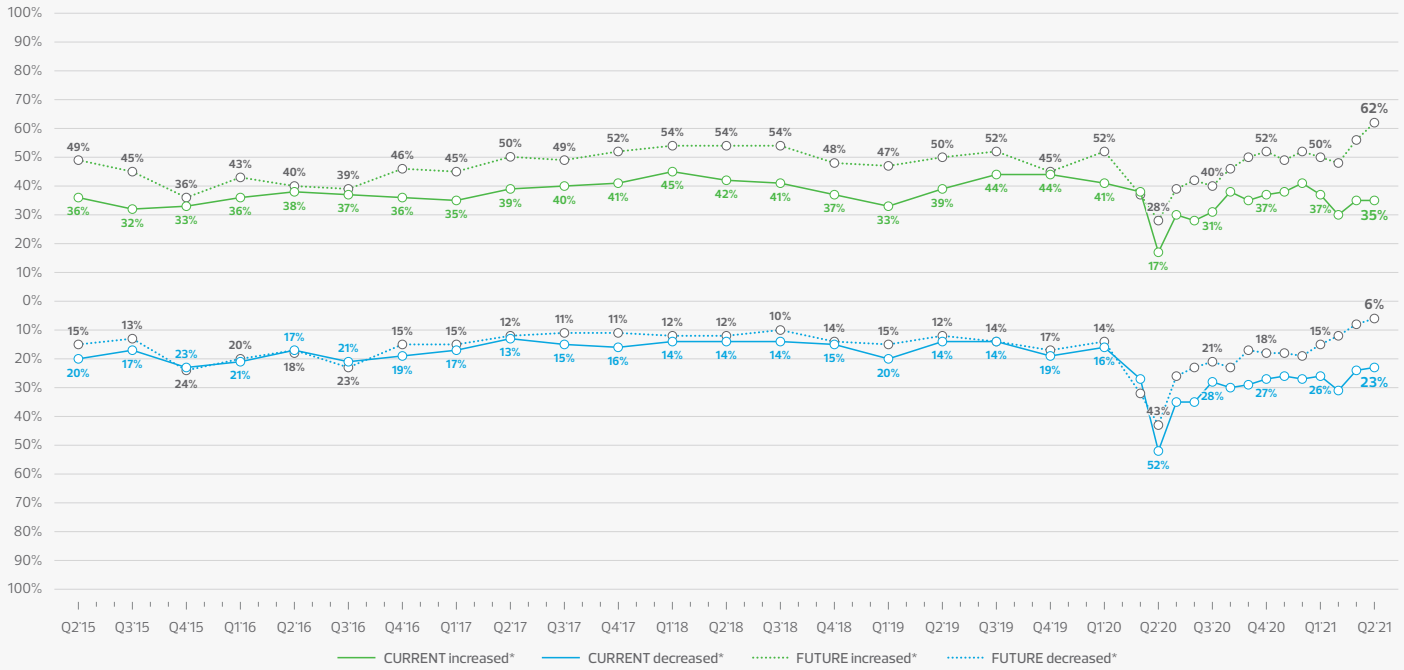
- Thinking about your organization's net earnings (after expenses, etc.) for the most recent quarter results versus the prior quarter results, how would you describe the level of your most recent quarter net earnings results? Would you say net earnings results have (among those not nonprofits) . . .?
- What are your expectations regarding your organization's net earnings results (after expenses, etc.) over the next six months? Do you expect net earnings results to (among those not nonprofits) . . .?

SQUARE/CIRCLE = Significantly higher/lower than previous quarter, respectively, at 0.05 level of significance

*seasonally adjusted

AGGREGATE CAPITAL EXPENDITURES/INVESTMENTS PERFORMANCE

Thirty-five percent of executives said their businesses made capital investments in April, on par with the month prior; however, 62% expected to increase expenditures over the next six months—an all time high for the MMBI.



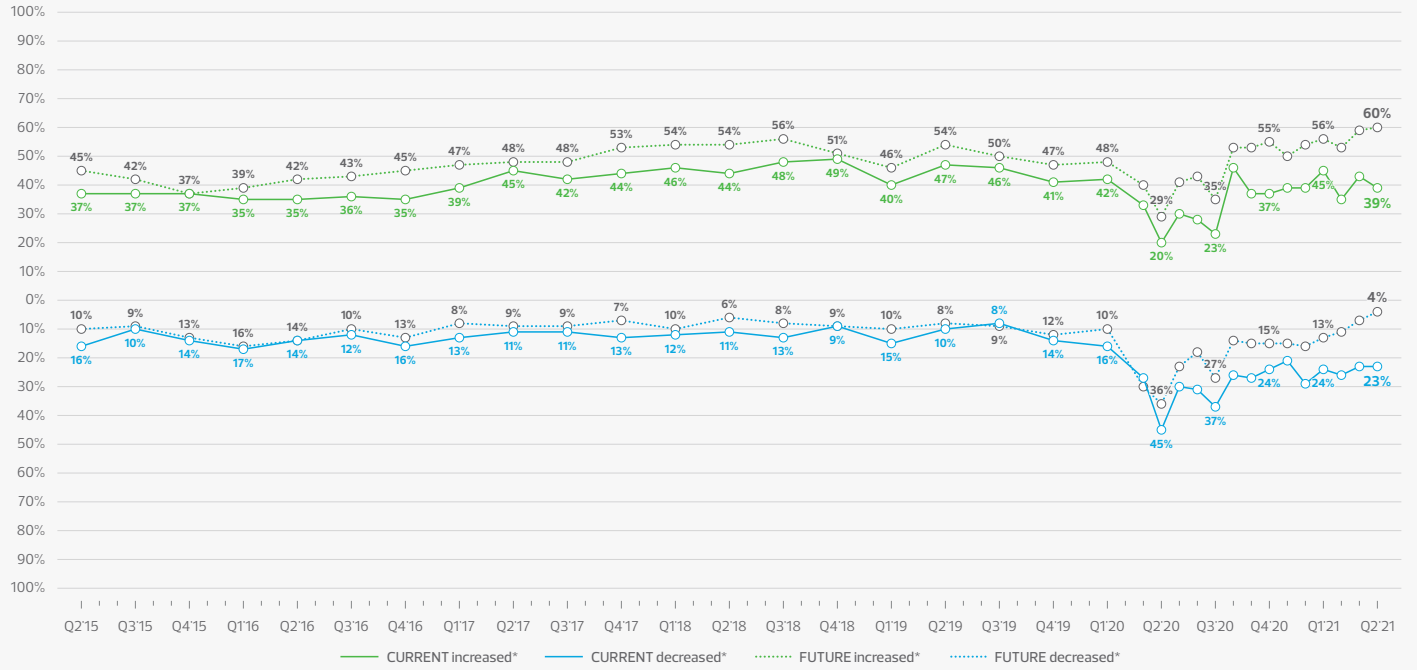
- Thinking about your organization's aggregate capital expenditures or investments this quarter versus last quarter, how would you describe your organization's current capital expenditures/investments? Would you say capital expenditures/investments have . . .?
- What are your expectations regarding your organization's aggregate capital expenditures or investments over the next six months? Would you say capital expenditures/investments will . . .?

SQUARE/CIRCLE = Significantly higher/lower than previous quarter, respectively, at 0.05 level of significance

*seasonally adjusted

OVERALL HIRING LEVELS

Hiring decreased in April, with 39% of executives indicating they added staff, compared to 43% in March; however 60% plan to increase hiring in the next six months.



- Thinking about your organization's overall hiring levels this quarter versus last quarter, how would you describe your current hiring levels? Would you say hiring levels have . . .?
- What are your expectations regarding your organization's overall hiring levels over the next six months? Do you expect hiring levels to . . .?

SQUARE/CIRCLE = Significantly higher/lower than previous quarter, respectively, at 0.05 level of significance

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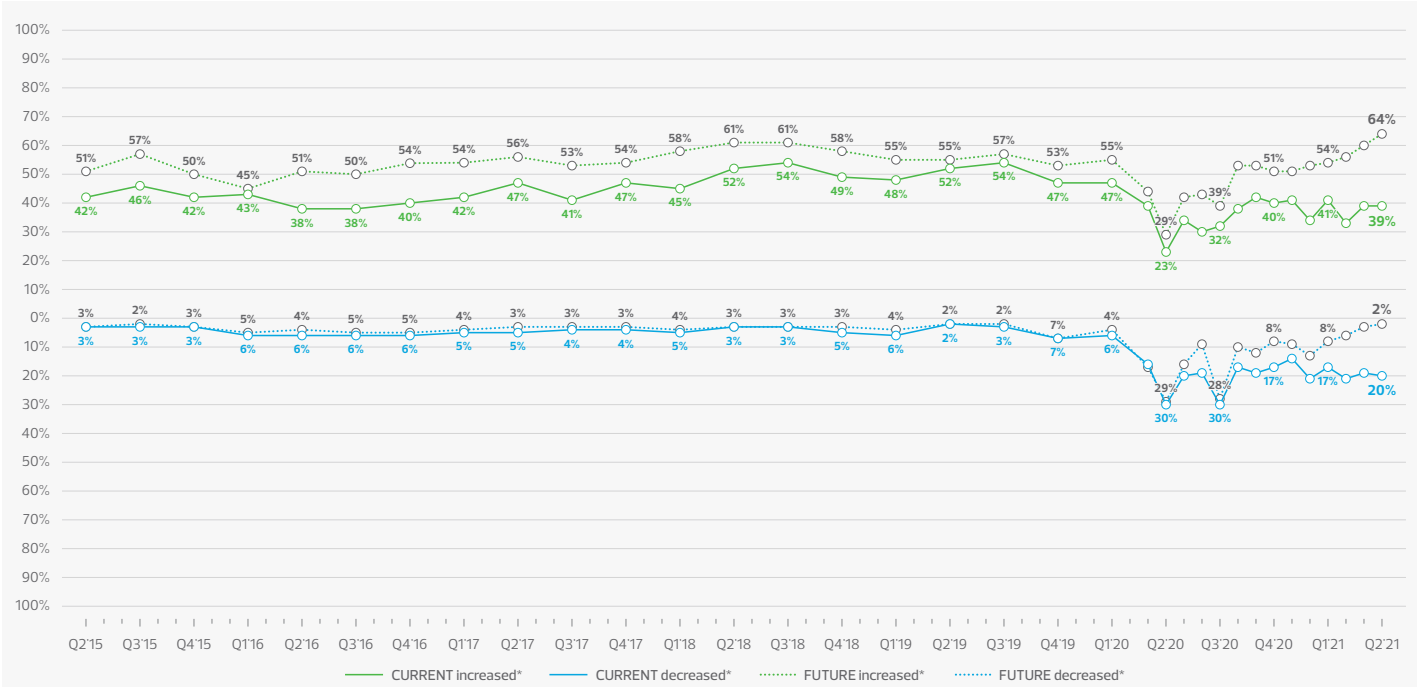
EMPLOYEE COMPENSATION

Thirty-nine percent of executives said their businesses increased compensation in April, unchanged from the month prior, and 64% anticipate increasing compensation in the next six months.



- Thinking about employee compensation at your organization this quarter versus last quarter, how would you describe the current employee compensation level on average? Would you say employee compensation, on average, has . . .?
- What are your expectations regarding your organization's employee compensation over the next six months? Would you say employee compensation, on average, will . . .?

SQUARE/CIRCLE = Significantly higher/lower than previous quarter, respectively, at 0.05 level of significance

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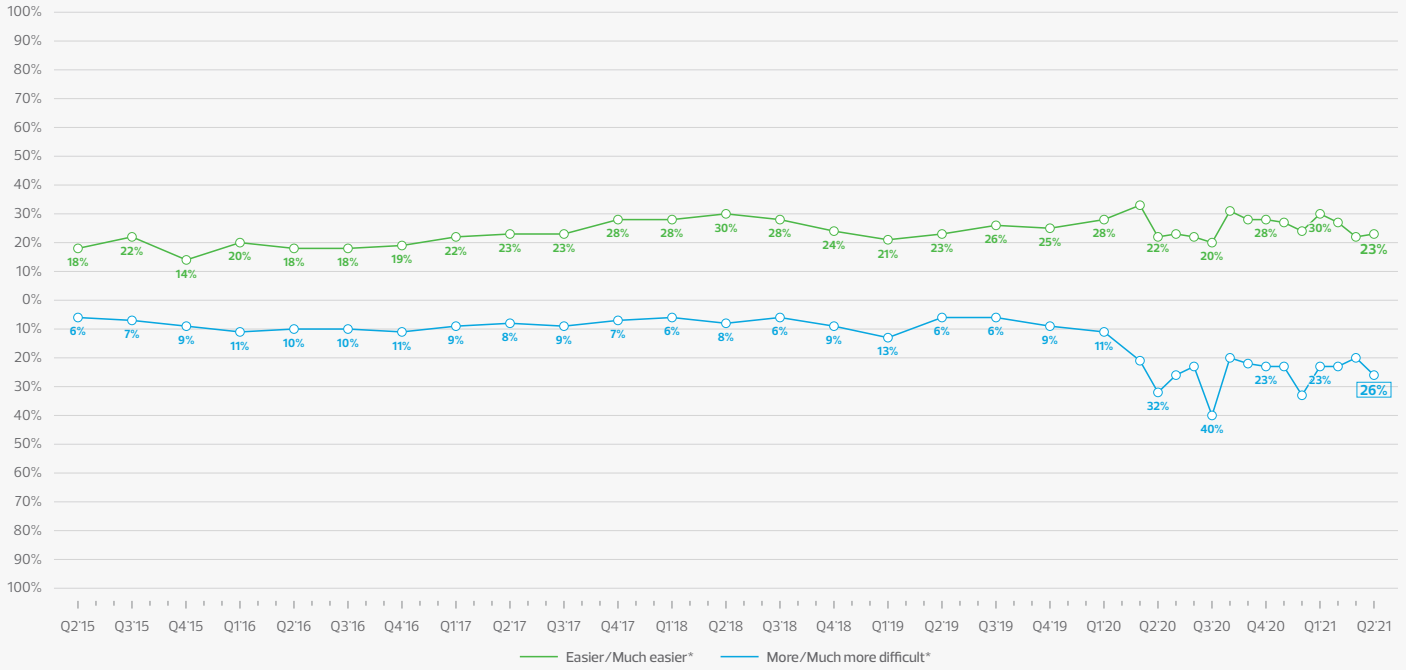
ACCESS TO CREDIT

Access to credit improved slightly in April, with 23% of executives indicating favorable conditions, up from 22% in March.



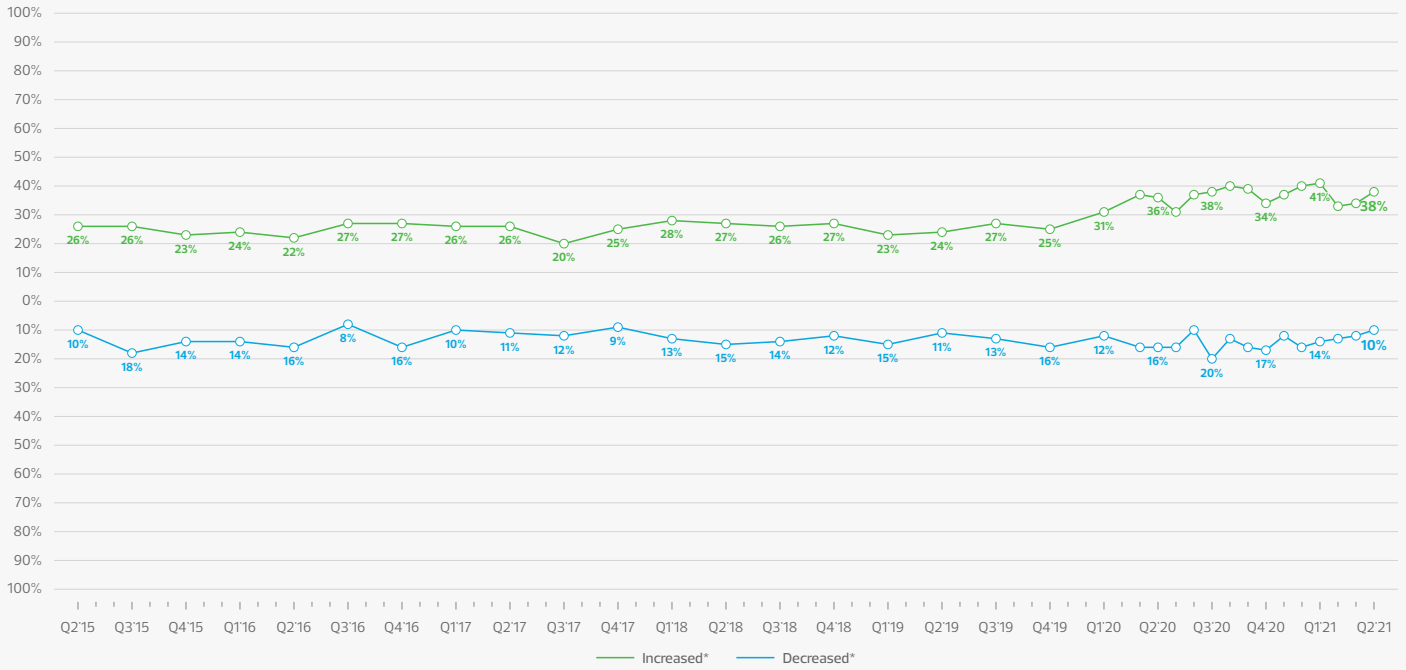
- Thinking about the availability or ease with which your organization can borrow money this quarter versus last quarter, how would you describe current access to credit? Would you say that accessing credit is . . .?

SQUARE/CIRCLE = Significantly higher/lower than previous quarter, respectively, at 0.05 level of significance

*seasonally adjusted

PLANNED BORROWING

Thirty-eight percent of respondents said they planned to increase borrowing over the next six months, a slight uptick from the two months prior.



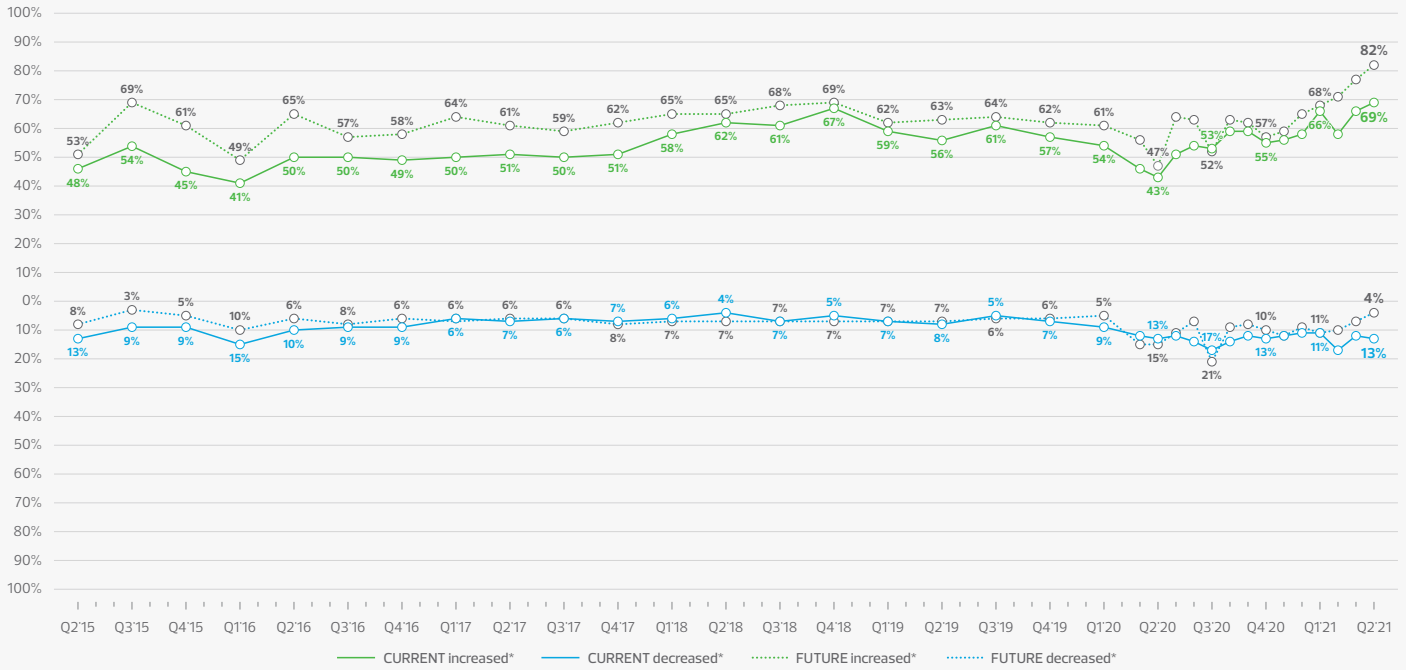
- What are your expectations regarding your organization's planned borrowing over the next six months? Would you say your organization's borrowing will . . .?

SQUARE/CIRCLE = Significantly higher/lower than previous quarter, respectively, at 0.05 level of significance

*seasonally adjusted

AMOUNT PAID FOR GOODS AND SERVICES

Prices paid for goods and services were higher in April, according to 69% of executives surveyed, up from 66% in March.



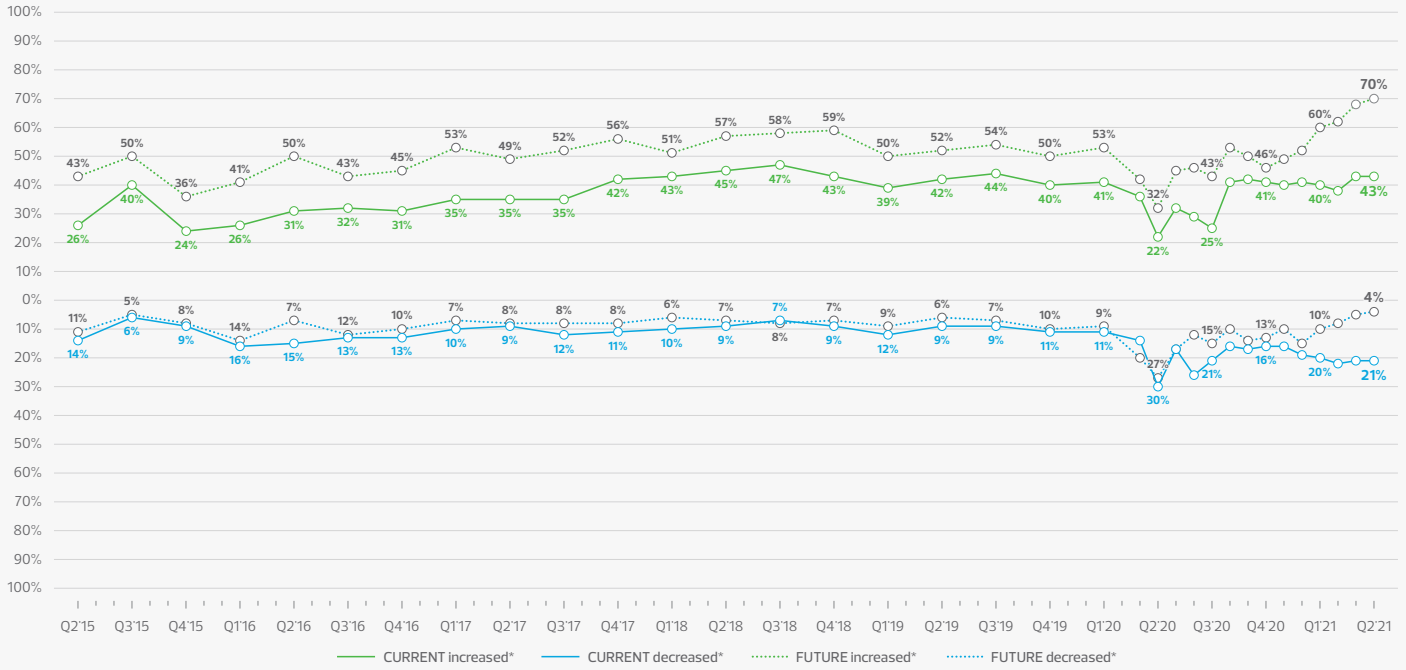
- Thinking about the prices that your organization pays for all goods and services, except labor, this quarter versus last quarter, how would you describe the current general level of prices paid? Would you say prices paid, on average, have . . .?
- What are your expectations regarding the general level of prices that your organization will pay for all goods and services, except labor, over the next six months? Would you say prices paid, on average, will . . .?

SQUARE/CIRCLE = Significantly higher/lower than previous quarter, respectively, at 0.05 level of significance

*seasonally adjusted

AMOUNT RECEIVED FOR GOODS AND SERVICES

Seventy percent of executives expected their organization to charge more for goods and services over the next six months, up from 60% in January.



- Thinking about the prices that your organization received for all of its goods and services this quarter versus last quarter, how would you describe the current general level of prices received? Would you say prices received by your organization, on average, have (among those not nonprofits) . . .?
- What are your expectations regarding the general level of prices that your organization will receive for all goods and services over the next six months? Would you say the prices received by your organization, on average, will (among those not nonprofits) . . .?

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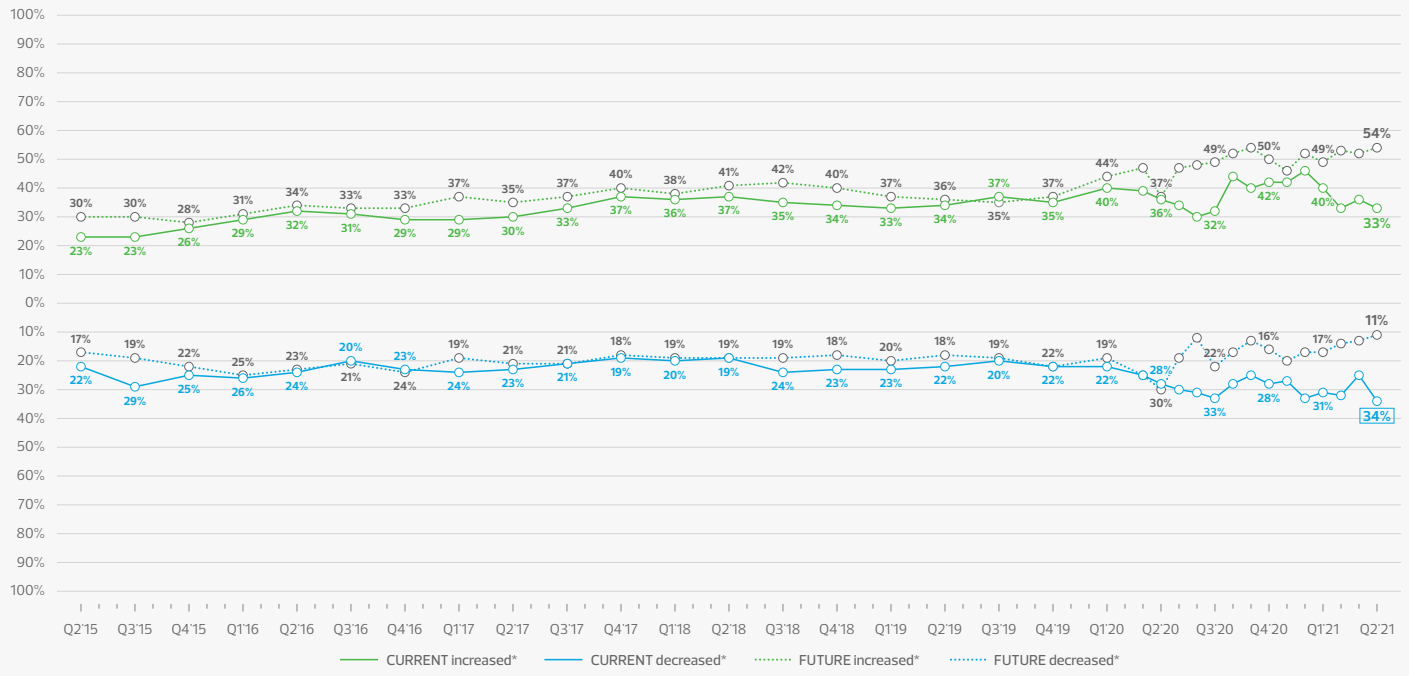
*seasonally adjusted

INVENTORY LEVELS

Thirty-three percent of executives said their inventories were higher in April, while 34% said they decreased.



- Thinking about your organization's inventory levels this quarter versus last quarter, how would you describe current inventory levels? Would you say inventory levels have . . . ?
- What are your expectations regarding your organization's planned inventory levels over the next six months? Would you say your inventory levels will (among those that have inventory) . . . ?

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*seasonally adjusted

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.

RSM US Middle Market Business Index questions

- What are your expectations regarding the general economy?
- What are your expectations regarding your organization's gross revenues?
- How would you describe the level of your organization's most recent quarter net earnings results?
- What are your expectations regarding your organization's aggregate capital expenditures or investments?
- What are your expectations regarding your organization's overall hiring levels?
- How would you describe your organization's current employee compensation level on average?
- How would you describe current access to credit?
- What are your expectations regarding your organization's planned borrowing?
- How would you describe the current general level of prices received?
- What are your expectations regarding your organization's planned inventory levels?

A VOICE FOR THE MIDDLE MARKET

CELEBRATING FIVE YEARS OF THE RSM US MIDDLE MARKET BUSINESS INDEX

Five years ago we saw an opportunity to bring deeper insight and knowledge to our clients, policymakers, media and others about the broader middle market economy. The question we wanted to answer: How could we give a much-needed voice to this important segment, which accounts for more than a third of U.S. employment and 40% of our gross domestic product? Enter the RSM US Middle Market Business Index.

Learn more about the MMBI's origin, the evolution and the direction it's heading in this video and article.

For more information on RSM, please visit **www.rsmus.com**.

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For more information on the U.S. Chamber of Commerce, please visit **www.uschamber.com**.

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The U.S. Chamber of Commerce is the world's largest business federation representing the interests of more than 3 million businesses of all sizes, sectors, and regions, as well as state and local chambers and industry associations.

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