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NATIONAL CENTER FOR
THE MIDDLE MARKET

Middle Market Manufacturing

Partnering with the National Center for the Middle Market, Chubb surveyed 1,000 executives from middle market companies in December 2022. This report highlights the key general business trends and evolving risks affecting the manufacturing segment of the middle market.

Executive Summary

Middle Market Manufacturers Project Continued Strong Performance; Acknowledge the Importance of Managing Current and Future Risks

Key indicators point to a thriving middle market manufacturing segment. Companies have sustained double-digit year-over-year revenue and employment growth since the close of 2021. Overall, more than three-quarters of manufacturers (76%) say performance has improved compared to one year ago. Most leaders project strong growth continuing for 2023 and appear ready to invest in their businesses.

However, manufacturers face no shortage of current and future challenges. Supply chain issues, inflation, skills shortages, and threat of recession are the top four current concerns for manufacturing leaders. Cost and the economy are expected to be the major challenges this year. As manufacturers continue to explore solutions to attract and retain skilled talent to keep up with their growth projections, they will also be focused on managing and mitigating risks and will lean on their insurance partners for support.

KEY FINDINGS

01 Reshoring and a post-COVID boom are fueling strong growth and ongoing opportunity for manufacturers

U.S. middle market manufacturers have sustained historically high rates of year-over-year revenue growth since the second half of 2021. Between December 2021 and December 2022, 86% of companies increased year-over-year revenues with 54% reporting growth of 10% or more.

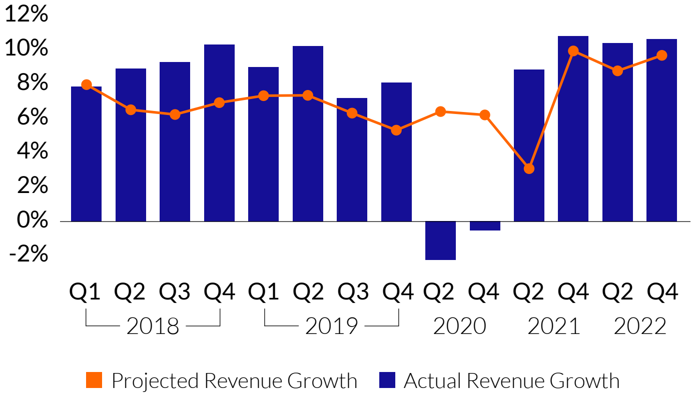
This strong performance may be partially attributed to ongoing recovery from the tumultuous events of 2020 and an inflationary impact driving higher prices of goods and services. However, organic growth is clearly a factor as well. Recent trends in reshoring are likely contributing to growth in the sector. Among middle market companies across all industries, approximately half of businesses have increased the amount of manufacturing they do in the United States, either within their own facilities or with another U.S.-based company or contractor, or both. Manufacturers are thus likely benefiting from new business opportunities with new customers as well as from bringing more of their own workload home. Expansion is driving new revenues as well. Over the past 12 months, a majority of manufacturers have introduced new products and services, and many have entered new domestic and/or international markets. With supply chain pressures easing, companies have more opportunities to serve international customers and middle market manufacturers report 10.9% total growth in international revenues for 2022, outpacing the previous year.

Manufacturing leaders see continued opportunity on the horizon with growth projections remaining strong for 2023. Overall, 65% of middle market manufacturers project year-over-year revenue growth for the year ahead compared to just 58% of middle market companies across all industry segments. While the rate of growth is expected to slow moderately in the sector, manufacturing leaders appear more confident in the economy than their peers and more likely to invest an extra dollar immediately than hold it as cash or for future investments. This sentiment translates into healthy expansionary plans for the sector for the year ahead.

The data behind the findings

ROBUST REVENUE GROWTH CONTINUES

Projected and actual revenue growth rates for U.S. middle market manufacturers



% of middle market manufacturers reporting/projecting year-over-year revenue growth

Increased year-over-year revenues

Expect revenue growth in 2023

RESHORING TRENDS ARE STRONG ACROSS MIDDLE MARKET BUSINESSES IN ALL INDUSTRIES

Change in U.S. manufacturing in the past 12 months

49% Yes, manufacturing more in the U.S. in-house

41% Yes, manufacturing more in the U.S. with another company/ contractor

22% No changes to how we manufacture

11% Already fully manufacture in the U.S.

18% Do not do any manufacturing

ECONOMIC CONFIDENCE IS HIGH

% of middle market manufacturing leaders expressing confidence in the global, national, and local economies

Global
71%

National
80%

Local
89%

CAPITAL INVESTMENT APPETITES ARE STRONG IN MANUFACTURING

% of middle market executives that would invest an extra dollar immediately

Manufacturers
69%

Total MM
55%

EXPANSIONARY ACTIVITY IS HEALTHY

% of middle market manufacturers engaging in expansion activities over the past 12 months/planning expansion over the next 12 months

Introduce a new product or service
62% Past 12 months → 74% Next 12 months

Enter new domestic markets
44% Past 12 months → 63% Next 12 months

Expand into new international markets
26% Past 12 months → 53% Next 12 months

KEY FINDINGS

02 Finding talent to fuel growth remains a significant challenge

U.S. middle market manufacturers have needed and will continue to need more people to enable sustained growth and performance and to take advantage of new opportunities from reshoring as well as international growth. In 2022, more than half of manufacturers increased the size of the workforce with 43% growing employment by 10+% compared to the previous year. The rate of year-over-year employment growth for the sector soared to an all-time high of 11.7%, edging the 11.1% employment growth for the total middle market.

Nevertheless, 22% of manufacturers say their workforce is currently insufficient for market conditions today. Furthermore, anticipated strong revenue growth and expansion for the industry in 2023 will create additional need for more people in the sector. Overall, over the next 12 months, 53% of middle market manufacturers expect to further increase the size of the workforce albeit at a less aggressive but still much-higher-than-average anticipated growth rate of 7.9%.

Finding people with the right skills for these jobs has not been easy and manufacturers fully expect ongoing challenges in this area. Indeed, workforce is currently one of the top three concerns for manufacturers with almost half (49%) of companies describing filling positions with qualified people as very to extremely challenging.

As a result, many companies are leaning more heavily on their existing people to work more hours. Around a quarter of businesses have turned to contractors to fill voids. Others have outsourced. Despite these measures, more than a quarter of manufacturers say talent shortages have negatively impacted productivity and sales. One in five have cut back on product lines or offerings.

The impact of the talent dilemma is easy to quantify in some areas, but it is taking a toll in other areas that may not be so obvious to spot. In the traditional manufacturing space, contractors, new employees, and overworked/tired employees may increase a company's risk profile. Errors and accidents caused by inexperience or fatigue as well as higher levels of turnover among these employees may significantly impact the bottom line, as well as workplace culture and morale. Moreover, companies utilizing subcontractors may have added risks related to protection of property as well as a degree of supply chain risk related to the subcontractor's ability to deliver products.

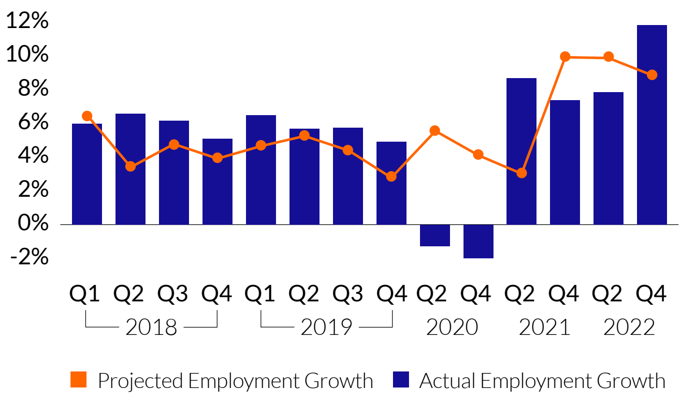
To address these complex issues, companies are taking a variety of actions to revamp recruiting, hiring, onboarding, and retention practices, including changing experience requirements for hiring and training, presumably to provide more on-the-job support for teaching the required skills for the job. Some companies have told us they are exploring apprenticeship programs and partnering with local community colleges to increase access to talent. However, many will continue to expect more overtime and output from the current workforce while filling positions and getting new hires up to speed, which may exacerbate some of the current workforce problems and further tax an already over-burdened team.

A third of manufacturers are looking at technology and automation as ways to reduce dependance on human resources. This approach also comes with its own set of related challenges including increased cybersecurity risk and the need for a workforce with a higher level of digital skills and sophistication. Companies will need to carefully explore all their options and find the right balance between risks and costs to ensure their ability to meet demand with the resources available.

The data behind the findings

EMPLOYMENT GROWTH RATE REACHES AN ALL-TIME HIGH

Projected and actual employment growth rates for U.S. middle market manufacturers



% of middle market manufacturers reporting/projecting year-over-year employment growth

Increased year-over-year employment growth

56%

Expect employment growth in 2023

53%

SKILLS GAPS RESULT IN MORE OVERTIME, MORE CONTRACTING, AND LESS PRODUCTIVITY

% of middle market manufacturers reporting impact of workforce issues

Employees working longer hours/more shifts

46%

Inflation driving reassessment of cost of living/merit increases

41%

Having to slow down on productivity/sales

28%

Having to outsource

28%

Having to bring in contractors

26%

Having to cut back on product lines/offerings

21%

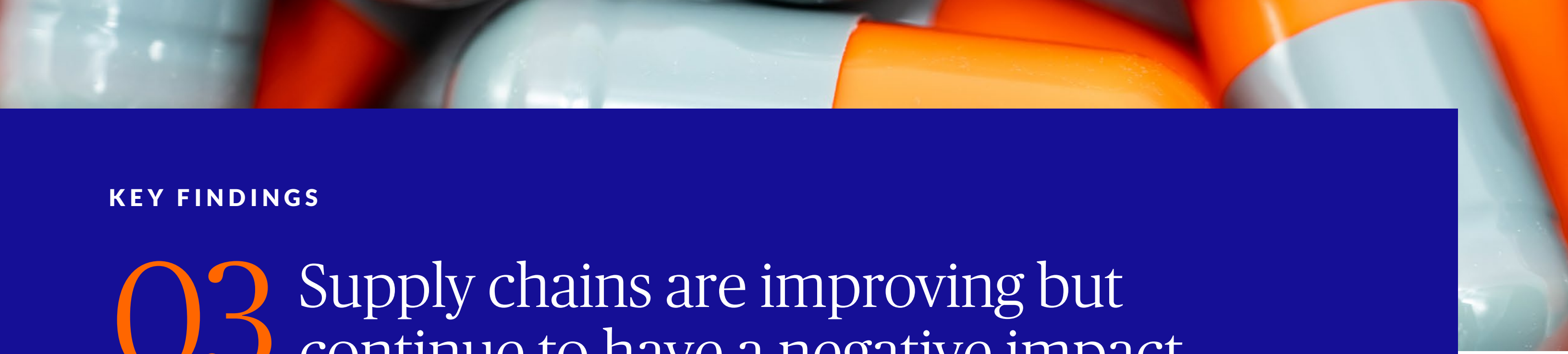
Having to bring in consultants

21%

CHANGES IN WORKFORCE PRACTICES AND APPROACHES ARE COMMON

% of middle market manufacturers reporting/planning action to address workforce issues

	Transitioning from employees to tech & automation alternatives	Changing experience requirements due to difficulty in finding good talent	Changing requirements in training of the workforce	Increase overtime/ hours/workload for current staff	Allow current staff to have flexible work hours from home or office schedule
Manufacturers doing so in the past 6-12 months	31%	33%	38%	47%	41%
Manufacturers to so over the next 6-12 months	33%	34%	46%	39%	37%



KEY FINDINGS

03 Supply chains are improving but continue to have a negative impact on manufacturers

Despite overall improvements to global supply chains and fewer companies reporting disruptions, supply chain issues remain the number one concern for middle market manufacturers today.

At the close of 2022, 41% of companies reported being affected by a supply chain disruption in the past six months, down from 59% in December 2021. However, nine out of 10 companies continue to report a negative impact on current revenue related to supply chain issues. Nearly as many believe the top line will continue to be affected in 2023.

These lingering consequences may be attributed to the fact that manufacturers view supply chain issues as one of their most difficult risks to manage with three out of five companies describing it as extremely or very challenging. Manufacturing leaders struggle with the growing complexity, size, scale, and globalization of their supply chains and cite negotiating terms and coping with service disruptions as some of their most challenging responsibilities.

To reduce the risk of disruption, many companies have worked to diversify their suppliers and reduce dependence on one company or one geographic region. Most are practicing reshoring to some degree—bringing overseas manufacturing back to their own U.S. based facilities and/or contracting the work to other U.S.-based companies. Many are increasing connectivity with suppliers to keep better tabs on the status of orders and learn about delays and disruptions in advance.

However, greater connectivity ushers in its own set of challenges: 52% of manufacturers express a high degree of concern related to being exposed to a ransomware attack due to connectivity with suppliers. Many companies have increased their IT budgets and invested in additional security to help mitigate this risk.

The data behind the findings

SUPPLY CHAIN DISRUPTIONS ARE DECLINING

% of middle market manufacturers reporting an impact from supply chain constraints/disruptions in the past 6 months

59%	45%	41%
December 2021	June 2022	December 2022

SUPPLY CHAIN ISSUES CONTINUE TO NEGATIVELY IMPACT REVENUES

% of middle market manufacturers reporting/projecting negative revenue impacts from supply chain disruptions

	Current revenue:	Revenue projections
Some negative impact	91%	86%
0-5% neg impact	52%	49%
5-10% neg impact	33%	34%
Over 10% neg impact	7%	3%

Mean negative impact: -4.6% (current revenue)

Mean negative impact: -4.4% (revenue projections)

59% of companies say it is extremely/ very challenging to manage supply chain risk

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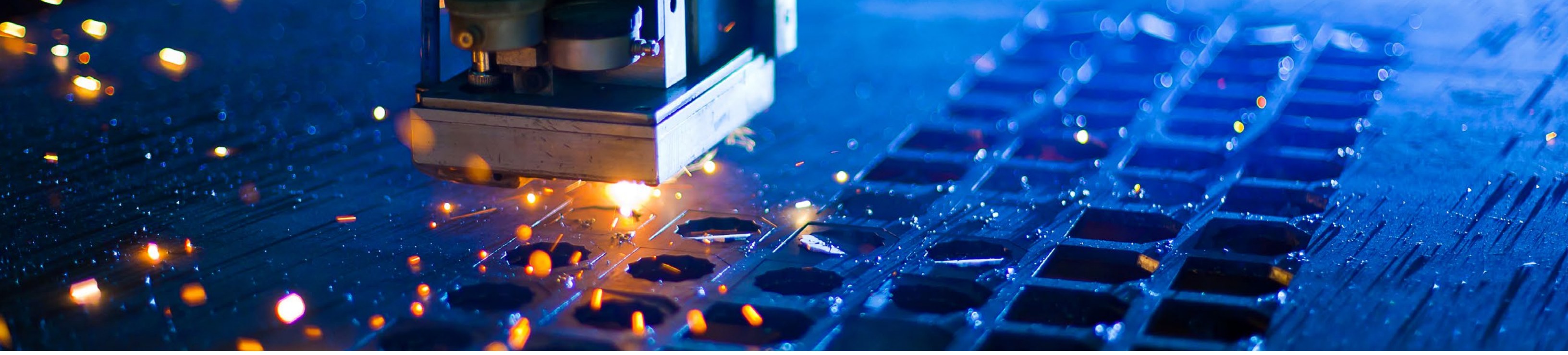


MANY ASPECTS OF SUPPLY CHAIN MANAGEMENT ARE HIGHLY CHALLENGING

% of middle market manufacturers reporting a high degree of challenge (Q 200)

Coping with service disruptions (e.g., port closures, natural disasters, union stoppages, etc.)
71%

The growing complexity of the supply chain
71%

Negotiating terms with customers
65%

The size and scale of the supply chain
65%

Globalization of the supply chain
64%

Complying with customer requirements
54%

Wage fluctuations
54%

Supplier due diligence/audit
54%

Competition
53%

Maintaining the confidentiality of digital assets
53%

Negotiating terms with suppliers
50%

Currency fluctuations
50%

SUPPLY CHAIN DIVERSIFICATION, RESHORING, AND SUPPLIER CONNECTIVITY AND OVERSIGHT HELP MITIGATE SUPPLY CHAIN RISK

42% find suppliers in multiple geographic regions

29% purchase from an alternative source

26% have a secondary “standby” source available

26% increase supplier/vendor oversight functions

58% of manufacturers have made changes for the purpose of bringing or doing more manufacturing in the U.S. in the past 12 months

48% have increased connectivity with suppliers in the past 12 months

52% are extremely/very concerned about being exposed to a ransomware attack due to connectivity with suppliers

49% have increased IT budgets; 47% invest in additional security

KEY FINDINGS

04 Inflation and recessionary fears are dark clouds on the horizon

Manufacturers cite the economy and costs as the two biggest external challenges they anticipate facing over the next 12 months.

Despite generally high levels of economic confidence, U.S. middle market manufacturing leaders acknowledge that they are in the midst of dealing with high inflation, and leaders continue to worry about a potential recession. These two issues present the most difficult risks for organizations to manage; only half of manufacturers believe they are fully prepared to respond to new disruptions arising from these economic circumstances.

Compared to one year ago, three out of five manufacturers say they are paying higher wages today by an average increase of 5.1%. However, the greatest impacts of inflation are manifesting in the costs of goods, raw materials, shipping costs, and inventory. In response, a solid majority of manufacturers have raised their own prices, and this may be helping to drive positive outcomes for some companies. Indeed, nearly as many middle market manufacturers cite a positive overall impact of inflation over the last six months as those that cite a negative impact from inflation. Whether or not price increases can continue to offset costs, however, is questionable. Three out of five manufacturers point to extreme price sensitivity for their products. At some point, higher prices will negatively impact demand.

Going forward, inflation and global economic concerns may impact companies' performance in other ways. While manufacturers point to plants, equipment, and facilities as key areas for investment dollars to help fuel future growth, nearly half of companies say that ongoing inflation could delay these capital expenditures. International business could suffer, too. While international revenues were up in 2022, more than a quarter of manufacturers say the threat of recession and the volatility of the global economy have a major impact on their ability to do business overseas.

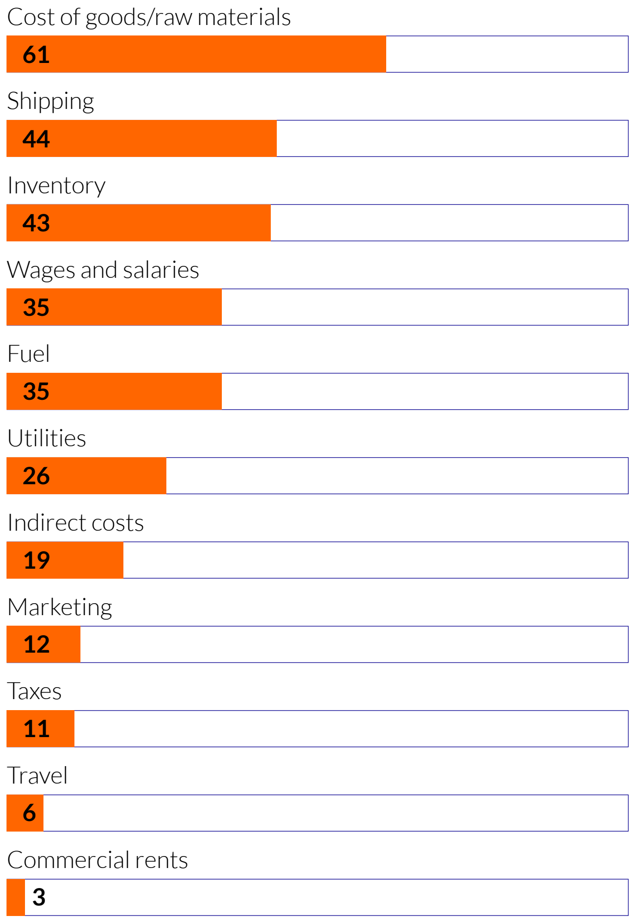
While the risks and concerns are real, most manufacturers gain peace of mind from partnering with insurance agents and brokers to manage risks and help cover losses due to different types of business disruptions. Of course, insurance is not immune to the effects of inflation. Most companies recognize that the replacement value of their covered assets has increased in the current economic situation and their ability to cover the costs of replacing assets with their current coverage may have changed. Many are considering evaluating policies and increasing coverage amounts.

The data behind the findings

62% of manufacturers report significant challenges managing inflation risk

60% of manufactures report significant challenges managing recession risk

AREAS WHERE MANUFACTURERS ARE MOST IMPACTED BY INFLATION



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OUTCOMES

69% of manufacturers have raised prices

48% say inflation could delay capex

28% say threat of recession and volatility of global economy have a major impact on ability to do business overseas

INSURANCE

57% of manufactures are extremely/very reliant on insurance agent/broker when it comes to managing risk

70% say replacement value of covered assets has increased due to inflation

48% say inflation has impacted ability to cover replacing assets with current insurance coverage

41% say inflation will lead to evaluating adequacy of insurance coverage or limits

68% will consider increasing coverage amounts to compensate for inflation

Middle market companies and their insurance partners can rely on us to provide specialized risk engineering services and helpful tools to evaluate and mitigate exposures.

We can also develop customized insurance coverages that offer essential protection.

More than ever, middle market companies need expert advice on how to manage evolving risks

Working with an insurance agent or broker is the best way to create tailored insurance strategies that help protect a company's operations and business performance.

For more information about these or other topics, visit chubb.com.

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