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St. Cloud Area Quarterly Business Report, Vol. 5, No. 1

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St. Cloud Area Quarterly Business Report

Winter 2003

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Central Minnesota Economy Survives 2002 Brighter Future Ahead

Volume 5, Number 1

Executive Summary

The most recent quarter found the St. Cloud area economy continuing to be mired in the weakness that has endured since late 2001. Overall employment in the St. Cloud area fell, with job losses heavily concentrated in retail and service sectors. Economic performance improved in very few sectors of the economy as Central Minnesota continued to work through the aftereffects of the Fingerhut closing. Despite this, results from the **St. Cloud Index of Leading Economic Indicators** and the **St. Cloud Area Business Outlook Survey** indicate that a brighter economic future is on the horizon. Economic conditions now exist which make an area economic recovery beginning in the late spring or early summer of 2003 extremely likely. Both instruments are designed to forecast economic conditions over the next four to six months.

Area employment fell by 1.6 percent over the year ending November 2002, making the St. Cloud economy the worst performer of all neighboring metropolitan areas. It now appears, however, that area economic performance is close to bottoming out. The adverse spillover effects from the Fingerhut closing will soon die out and Fingerhut's net impact should turn positive with its new ownership and organization. In addition, predictions of the **St. Cloud Index of Leading Economic Indicators** remain encouraging. The local index is currently being bolstered by continued strength in new residential electrical hookups, an increase in the number of local business start-ups, and improvements in the U.S. Index of Leading Economic Indicators. A recent reduction in the length of the average workweek of area manufacturing production workers has offset some of the gains in the local index.

Sixty-seven percent of the fifty-one firms responding to the **St. Cloud Area Business Outlook Survey** anticipate an increase in the level of business activity for their company over the next six months compared to only 10 percent who expect conditions to worsen. This anticipated future growth is equivalent to the gains that were routinely expected to occur in the late 1990s and early 2000, when area growth peaked. Indeed, a larger percentage of surveyed firms plan to increase capital expenditures over the next six months than at any time since December 1999. However, business conditions at surveyed firms were relatively weak over the last quarter of 2002. Overall business activity, employment gains, length of the workweek, capital expenditures, employee compensation, and prices received were all significantly weaker than the results from last quarter's current conditions survey. In addition, area businesses became very pessimistic about national economic conditions over the past three months.

A special question in the December 2002 **St. Cloud Area Business Outlook Survey** asked area businesses to identify when they feel a sustained recovery of the area economy will begin. Sixty-three percent of responding firms indicate they expect the local recovery will begin in the second or third quarter of 2003. This is highly consistent with results found in other parts of the quarterly survey as well as the predictions of the **St. Cloud Index of Leading Economic Indicators**. A second special question asked area businesses to assess the extent to which the performance of their company is affected by the economic health of Central Minnesota rural communities. The surprising results to this question indicate that 63 percent of those firms questioned believe their company is either "moderately impacted" or "largely impacted" by

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the economic health of surrounding rural communities. It thus appears that area employers are quite deeply impacted by rural economic conditions in Central Minnesota.

St. Cloud Index of Leading Economic Indicators

The November 2002 **St. Cloud Index of Leading Economic Indicators** projects that the St. Cloud area economy will be in a full-fledged recovery by late Spring 2003.

The index is designed to forecast local economic activity four to six months in the future. Figure 1 shows that the index has increased for five consecutive months at a reasonably rapid clip. The local index has been boosted by steady increases in the number of new St. Cloud area residential electric hookups and in the number of new local business start-ups as suggested by new registrants with the Minnesota Office of the Secretary

Full-fledged recovery should begin by late Spring.

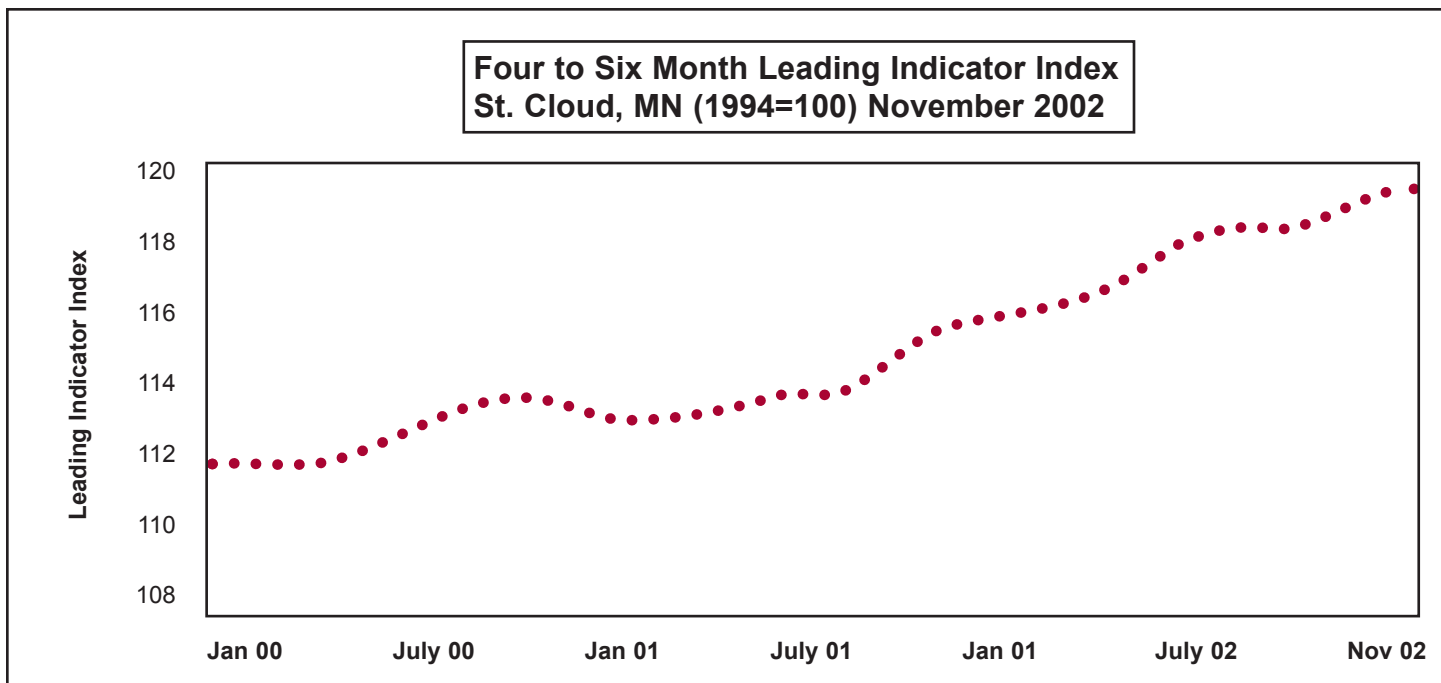
of State. Recent increases in the U.S. Index of Leading Economic Indicators have also given the local index a lift. A recent decline in the area average manufacturing work-week is the only factor that has adversely impacted the local index. Readers are once again reminded that the economic shock of the 2002 Fingerhut shutdown challenges the predictive capabilities of the statistical model used to derive the index. Forecasting models use past trends to help predict future events and they are less reliable when one-time events (such as the Fingerhut shutdown or the events surrounding 9-11 at the national level) affect the economy. Nevertheless, it is heartening that many local residents are confident enough to begin new businesses, while the additional residential electric hookups suggest people continue to move into the St. Cloud area. As a rule of thumb, three consecutive positive changes in the **St. Cloud Index of Leading Economic Indicators** suggest an expanding economy, while three consecutive decreases suggest a contracting economy and/or a slowing of economic growth.

The St. Cloud Area Overall Outlook

Table 1 shows nonfarm employment data for the St. Cloud Metropolitan Area (MSA), Minneapolis-St. Paul (MSA), and Minnesota. In a continuation of a negative trend that began in July 2001, St. Cloud MSA employment fell by 1.6 percent in the year ending November 2002. Despite this, there is some modestly good news in the overall employment figures. The robust 1990s expansion in area jobs ended in January 2000 with the initial large-scale layoffs at Fingerhut. While total St. Cloud MSA nonfarm employment grew a sizzling 5.5 percent over the year ending December 1999, the corresponding growth rate fell to 1.6 percent in December 2000 and was a negative 1.4 percent in December 2001. By July 2002, the annualized employment growth rate further fell to -1.9 percent, so there is evidence that job growth will soon head in the right direction.

St. Cloud's 1.6 percent employment decline in the year ending November 2002 is harsher than the corresponding -0.3 percent and -0.1 percent change in state and

Figure 1--St. Cloud Index of Leading Economic Indicators (November 2002)



Source: SCSU Center for Economic Education, Social Science Research Inst., R. MacDonald, M. Partridge

national employment. Likewise, the Duluth, Minneapolis-St. Paul, and Rochester MSAs all experienced better job growth (respectively, 0.7%, -0.1%, and 0.1%), again illustrating the severity of St. Cloud's current downturn. Indeed, among seven neighboring-state MSAs near the Minnesota border (Eau Claire, La Crosse, Des Moines, Sioux City, Sioux Falls, Fargo-Moorhead, and Grand Forks), U.S. Bureau of Labor Statistics data show that only Fargo experienced negative growth in the year ending November

Area job growth will soon head in the right direction.

2002 (-0.4%). In fact, La Crosse experienced solid 2.4 percent growth. The St. Cloud area's recent job growth rate remains 4.0 percentage points below its 2.4 percent 1988-2002 long-term trend annual job growth rate. All available evidence confirms that the St. Cloud recession which began in late summer 2001 lingered through Fall 2002. It should also be noted that Minnesota appears to be lagging other upper Midwest states in economic growth, although there are signs that the state economy is on the verge of recovery. Nonetheless, given the sharp blows the local economy has endured over the last three years, it is noteworthy that the local recession has not been more severe, although it has dragged on for at least 16 months.

National economic weakness continues.

The continued sluggishness of the national economy is a clear hindrance to the beginning of a sustained local expansion. Even with the well publicized Fingerhut shut down, the local economy would have likely started to emerge from recession if the national economy had expanded at the rate national forecasters predicted one year ago. Although there remains little likelihood that the national economy will dip back into recession, most analysts continue to forecast a jobless recovery through the first-half of 2003. The return of rapid national growth is being further delayed by

side-way movements in the stock market and oil prices remaining around \$30 per barrel. The continued uncertainty regarding a possible war with Iraq and any resulting aftermath also cloud the national outlook. These concerns are further compounded by tensions with North Korea. While businesses nationwide continue to be reluctant to invest in new capital, the good news is that consumer spending held up remarkably well in 2001 and 2002. Low interest rates have helped spur two strong years in the national housing and consumer durable goods markets. Most experts believe interest rates will remain near their current level as long as inflation remains tame. Sooner or later, these favorable rates, along with an improved business climate, will make business investment look more attractive. With continued impressive gains in productivity, it seems reasonable to expect the national economy to take off when capital spending finally begins to accelerate.

Along with the surprisingly weak performance of the national economy, the other key factor that has delayed St. Cloud's recovery is the slow-paced and cautious resumption of Fingerhut operations. The new owners did not buy the company's assets to watch them sit idle, so we remain optimistic that a reinvigorated Fingerhut operation is on the horizon. Yet, it will likely be considerably smaller than its pre-2002 size for the foreseeable future. But even a modestly sized Fingerhut operation will remove what has been a major drag on the local economy over the 2000-2002 period as the firm wound down its local operations from a peak employment level of approximately 4,500 in December 1999. Recent announced layoffs at International Paper and SPX Valves also contribute to local economic uncertainty, but the magnitude of job loss pales in comparison to that experienced in the Fingerhut shut down. Nevertheless, the average wage and benefits scale for these recently furloughed employees was likely higher than was the case for Fingerhut employees, so the impact of these job losses should not be overlooked.

Notwithstanding any possible large layoffs, the St. Cloud economy will likely stabilize

in early 2003, with a sustained local recovery beginning in the Spring or the early Summer. This conclusion is supported by the responses of area business leaders to a special question of the December 2002 **St. Cloud Area Business Outlook Survey**. Table 5 shows that sixty-three percent of responding businesses believe that the local economy will begin a sustained recovery in the second or third quarter of 2003. Needless to say, all bets are off if a prolonged U.S. war with Iraq drives up energy prices or sets off a wave of terrorist attacks.

The St. Cloud Area Sectoral Outlook

Table 1 shows sectoral employment performance. The fall in local employment over the year ending November 2002 is widespread across most sectors. The sharp 7.7 percent decline in retail employment is primarily related to the fallout at Fingerhut. Not shown is a 5.9% decline in large general merchandise store employment which is a classic aftereffect of an economic shock such as that experienced in the Fingerhut closing. By comparison, Minnesota retail employment declined by only 0.1 percent over the year ending in November. Aside from Fingerhut's woes, the local retail sector has been in the doldrums for the past few years. Indeed, November's local retail employment is off more than 3,400 from the November 1999 figure (out of total St. Cloud MSA employment of about 95,000). Unless and until this course is reversed, a sustained local recovery will have difficulty gaining any real footing.

Government employment is down 1.6 percent over the year ending in November, but these estimates for the St. Cloud MSA are volatile on a monthly basis. Regardless, the state budgetary crisis will likely lead to further declines in government sector employment in 2003. Weakness is also found in the service sector (not service producing), which includes health, business, personal, legal, and accounting services, among others. Over the year ending November 2002, service sector employment was down 0.6 percent, which is well below the rapid 4.3 percent 1988-2002 long-term trend rate. This also marks a rather dramatic decline from the 4.9 per-

Retail sector has weakened.

cent annual increase in 2001. Over the 1989-2001 period, growth in this sector was never below 2.6 percent. The only bright spot in the service sector is a recent surge in health services employment, which is up 2.4 percent for the year ending in November.

Employment in the local construction sector has remained essentially flat over the

twelve month period ending in November 2002. However, the construction figures may be somewhat misleading in that 2000 and 2001 were amazingly robust, especially in the residential home sector. For example, U.S. Department of Commerce data suggest that the year-total valuation of local residential building permits through November 2002 ran 3-5 percent below the corresponding period in 2000 and 2001. Yet, these recent numbers are about one-fourth above the corresponding rate in 1999 and about two-thirds above that of 1998. Low interest rates should continue to support the local residential construc-

tion sector and the expected beginning of a local economic recovery in spring or early summer of 2003 should lift the local commercial building sector as well. Along with retail, a sustained recovery in the local construction sector would be a clear indication that the worst is over.

Local pockets of economic strength can be found in finance, insurance, and real estate (FIRE) and manufacturing, as job growth in the year ending November 2002 respectively equaled 4.6 percent and 1.4 percent. For FIRE, this reflects a takeoff that began in early 2001 that is likely caused by sev-

Table 1--Employment Trends

	St. Cloud Employment Trends			Minnesota Employment Trends			Twin Cities Employment Trends		
	in Percent			in Percent			in Percent		
	Long Term Trend Growth Rate	Nov 01- Nov 02 Growth Rate	Nov 2002 Employment Share	Long Term Trend Growth Rate	Nov 01- Nov 02 Growth Rate	Nov 2002 Employment Share	Long Term Trend Growth Rate	Nov 01- Nov 02 Growth Rate	Nov 2002 Employment Share
Total Nonagricultural 1988-2002	2.4%	-1.6%	100.0%	1.8%	-0.3%	100.0%	1.8%	-0.1%	100.0%
Total Nonagricultural 1992-2002	2.0%	-1.6%	100.0%	1.8%	-0.3%	100.0%	2.0%	-0.1%	100.0%
GOODS PRODUCING 1992-2002	2.4%	1.1%	22.7%	0.8%	-2.4%	19.9%	0.9%	-0.9%	19.5%
Construction & Mining 1992-2002	2.3%	-0.3%	4.6%	3.9%	-1.7%	4.8%	5.2%	1.5%	4.8%
Manufacturing 1988-2002	2.5%	1.4%	18.1%	0.1%	-2.6%	15.1%	-0.2%	-1.4%	14.7%
Durable goods 1992-2002	2.9%	1.3%	9.9%	0.3%	-2.9%	8.8%	0.2%	-1.9%	8.9%
Nondurable goods 1992-2002	2.0%	1.6%	8.2%	-0.4%	-2.2%	6.2%	-0.7%	-0.6%	5.8%
SERVICE PRODUCING 1992-2002	1.9%	-2.3%	77.3%	2.1%	0.2%	80.1%	2.3%	0.1%	80.5%
Transportation & Public Utilities 1988-2002	2.4%	0.4%	3.8%	1.3%	-3.7%	4.7%	1.4%	-1.8%	5.1%
Trade 1988-2002	1.1%	-5.8%	26.2%	1.5%	-0.5%	23.9%	1.5%	-1.4%	23.5%
Wholesale Trade 1988-2002	3.9%	2.0%	5.6%	1.4%	-1.7%	5.7%	1.3%	-1.9%	5.8%
Retail Trade 1988-2002	0.5%	-7.7%	20.6%	1.6%	-0.1%	18.2%	1.5%	-1.3%	17.7%
Finance, Insurance, & Real Estate 1988-2002	4.3%	4.6%	4.0%	2.3%	0.5%	6.2%	2.5%	0.9%	7.6%
Services 1988-2002	4.3%	-0.6%	28.7%	3.2%	0.8%	29.7%	3.0%	0.3%	30.1%
Health Services 1992-2002	3.5%	2.4%	8.5%	2.8%	3.0%	8.9%	2.2%	2.0%	7.4%
Educational Services 1992-2002	2.6%	-3.1%	4.2%	3.7%	3.9%	1.9%	4.0%	2.0%	1.6%
Other Services 1992-2002	4.3%	-1.4%	15.9%	2.7%	-0.5%	18.9%	2.9%	-0.4%	21.1%
Government 1988-2002	1.2%	-1.6%	14.7%	1.6%	1.2%	15.7%	2.1%	2.7%	14.2%
Federal 1992-2002	-0.2%	-3.8%	1.6%	0.2%	1.2%	1.3%	0.4%	1.1%	1.3%
State 1992-2002	0.4%	-5.3%	4.3%	0.6%	0.8%	3.5%	1.6%	2.0%	3.8%
Local 1992-2002	1.1%	0.7%	8.7%	2.0%	1.3%	10.9%	2.5%	3.1%	9.1%

Note: Long term trend growth rate is the compounded average employment growth rate in the specified period. St. Cloud and Twin Cities represent the St. Cloud and Minneapolis-St. Paul MSAs, respectively.

SOURCE: MN Workforce Center

eral factors including the expansion of ING Direct's local operations and a catch-up effect from long-running growth in the residential home market for realtors and bankers. The current 4.6 percent annual rate even exceeds its 4.3 percent 1988-2002 long-term trend growth rate. Yet, we caution that there are signs that FIRE's rapid expansion is starting to slow.

St. Cloud area manufacturers continue to fare amazingly well in a very difficult environment. Employment is up about 1.4 percent over the year ending in November. While this is below the 2.5 percent 1988-2002 long-term annual trend, St. Cloud area manufacturers have fared much better than their counterparts elsewhere. For example, state and national manufacturing employment during the same period respectively declined 2.6 percent and 3.5 percent (national data are from the U.S. Bureau of Labor Statistics at www.bls.gov). Moreover, the success of local manufacturers is not a recent phenomenon. Between November 1997 and November 2002, in the midst of being bombarded by the Asian crisis, a strong dollar, and the more recent U.S. downturn, national manufacturers shed 12.1 percent of their employees, while St. Cloud manufacturers actually **added** 9.6 percent more workers. Since manufacturing can occur virtually anywhere in the world, the continued growth of this sector is noteworthy. Nonetheless, the local economy remains vulnerable to large scale layoffs from any of the areas largest manufacturing concerns, so the relative success of this local sector should not be cause for observers to be excessively sanguine about the future of local manufacturing. Indeed, recent declines in the average manufacturing workweek could suggest that not all local manufacturers are on solid footing. On the bright side, the U.S. dollar weakened in 2002, helping manufacturers regain their competitiveness in world markets. A further decline in the dollar would be applauded by most local exporters.

St. Cloud Area Labor Market Conditions

The general weakness of the labor market is further demonstrated in Table 2. The November St. Cloud MSA unemployment

rate was 3.6 percent, well above the 3.1 percent rate recorded one year earlier. The slow 0.2 percent growth in the local labor force again suggests that many recently laid off workers or discouraged job seekers have dropped out of the labor force. The November seasonally unadjusted Minnesota unemployment rate was also 3.6 percent, which is unchanged from November 2001. While 3.6 percent may seem low compared to a 6 percent national unemployment rate, the unemployment rate is a poor indicator of a local economy's health. In the Northern Plains, the unemployment rate is always well below the national rate, meaning that today's relatively low rate is not unusual. To take an extreme example, North Dakota always has one of the lowest unemployment rates in the country even though its strong negative net-migration rates illustrate persistent weakness in the North Dakota economy (among other factors). Probably the best signal the local economy is beginning to stabilize is that new St. Cloud area unemployment insurance claims are finally starting to decline, reversing a two year-plus trend of accelerating claims. Table 2 shows that average monthly claims over the three months ending November 2002 were almost 8 percent below the corresponding period one year earlier. Indeed, new Minnesota unemployment insurance claims declined 17.5 percent during this period. While August to November St. Cloud area unemployment insurance claims are about the same as the similar period in 2000, they are still up 76 percent from the corresponding period in 1999. Help-wanted ad lineage in the *St. Cloud Times* continues to decline. During the three-month period ending in November, help-wanted ad lineage declined by 16 percent compared to the same period in 2001. Again, some of the decline reflects a general migration to other venues (such as the internet) for job postings. Yet, it is striking how little local retailers advertised for holiday-season workers.

Firms responding to the **St. Cloud Area Business Outlook Survey** agree that work-force availability will not be a general concern in the foreseeable future. Twenty-two percent of surveyed firms indi-

cate it was easier to find qualified workers in December 2002 than it was three months earlier (only 10% found it more difficult to find qualified workers over the same period). In addition, eighteen percent of survey respondents think it will be less difficult to find qualified workers six months from now. It should be noted that this is partially offset by 16% of firms who expect increased difficulty attracting qualified workers by May 2003. Overall, the survey of area business leaders suggests a continuation of the soft labor market conditions that have been experienced locally since March 2001.

St. Cloud Area Business Outlook Survey

The **St. Cloud Area Business Outlook Survey** is a survey of current business conditions and area firms' future outlook. It is administered quarterly with the cooperation of the St. Cloud Area Economic Development Partnership. Survey results reported in Tables 3 through 6 reflect the responses of fifty-one area business firms who returned the recent mailing. Participating firms are representative of the collection of diverse business interests in the St. Cloud area. They include retail, manufacturing, construction, financial, and government enterprises of sizes ranging from small to large. Survey responses are strictly confidential. Written and oral comments have not been attributed to individual firms.

Table 3 reports survey results of area business leaders' evaluation of business conditions for their company in December 2002 versus three months earlier. Results from Table 3 are universally less favorable than those that were reported in the September 2002 survey. It appears many area firms experienced weaker business activity over the past three months. For

Health services employment has expanded.

Area manufacturers have fared better than their counterparts elsewhere.

Area new unemployment insurance claims are falling.

example, the diffusion index (representing the percentage of respondents indicating an increase minus the percentage indicating a decrease in any given category) for

the level of business activity decreased from 35.8 to 7.8 in the current period. This represents a major decline in this index which is now at its lowest point since the December 2001 survey. Thirty-five percent of surveyed firms report an increase in business activity in this most recent quarter while 28% note a decrease. Several firms report (both favorable and unfavorable) seasonal effects and many note the impact interest rates are having on their business. For example, one area firm notes “new housing starts remain strong due to low interest rates” while another firm indicates “low rates improve mortgage refinance activity.” But one area firm is not entirely upbeat about the regional real estate market. This firm reports that “lakeshore sales (are) still slow especially (in the) upper bracket even though the rest of the market is strong.” Another firm

notes that “our business is affected by volume—we can create volume by going to outside sources...” and that its product line is “still being generated during slow times in the economy.” One firm writes “considering 9/11 we have been very pleased with how well we have done in sales.” Finally, a St. Cloud firm remarks that “the one-half percent sales tax might decrease sales, but not enough to cause a problem.”

The diffusion index for number of payroll employees is also the lowest it has been all year. The index declined from 24.5 three months ago to 0 in December. Values for length of workweek and employee compensation are also sharply lower than last quarter’s survey. Area firms responding to the survey continue to indicate little difficulty attracting qualified workers over the past quarter. General worker shortages experienced in the late 1990s are no longer a problem for area businesses, although one area firm notes that it is “very difficult to find good trained people. [It] takes a long time to train from scratch.” Local capital spending weakened last quarter. Only twenty-six percent of responding firms increased capital expenditures last quarter while 12 percent cut back on capital pur-

chases. This is, of course, a strong indication that the local economic recovery has not yet begun.

Over the past quarter, surveyed firms were less successful passing on price increases to customers. The diffusion index in this category fell from 1.9 to -5.9 over the September to December period (the value of the index was 19.3 in the June 2002 survey), as more area firms received lower prices than received higher prices. Less than 10% of respondents indicated prices received were higher in December than three months earlier (by comparison, the corresponding number in June 2002 was 32%). To the extent that these numbers suggest a weakening of profit margins, this represents yet another challenge for area firms to overcome. One area firm reports “minor price changes for some materials” while another firm writes “in [30% of our business] well-made Chinese imports are lowering retail prices dramatically. Dock strikes hurt inventories this fall. In [the other 70% of our business], our domestic manufacturers keep lowering prices to prevent Chinese [firms] from gaining the foothold in the market that they have already gained in [other markets].” This

Table 2--Other Economic Indicators

	2002	2001	Percent Change
St. Cloud MSA Labor Force Nov (MN Workforce Center)	103,089	102,922	0.2%
St. Cloud MSA Civilian Employment# Nov (MN Workforce Center)	99,356	99,728	-0.4%
St. Cloud MSA Unemployment Rate* Nov (MN Workforce Center)	3.6%	3.1%	NA
Minnesota Unemployment Rate* Nov (MN Workforce Center)	3.6%	3.6%	NA
Mpls-St. Paul/MSA Unemployment Rate* Nov (MN Workforce Center)	3.5%	3.5%	NA
St. Cloud Area New Unemployment Insurance Claims Sept-Nov Average (MN Workforce Center)	460.7	499.7	-7.8%
St. Cloud Times Help Wanted Ad Linage Sept-Nov Average	3,846	4,574	-15.9%
St. Cloud MSA Residential Building Permit Valuation (\$1,000) Sept-Nov Average (U.S. Dept. of Commerce)	9,341	8,292	12.7%
St. Cloud Index of Leading Economic Indicators Nov (SCSU)	118.8	115.7	NA

- The employment numbers here are based on resident estimates, not the employer payroll estimate in Table 1.
 * - Not Seasonally Adjusted
 NA - Not Applicable

firm also remarks on the damage U.S. protectionist steel tariffs have done to its core business. Finally, over the past three months, local confidence in the national economy has slipped dramatically. The diffusion index on national business activity fell from 22.7 to -11.8, its lowest reading of the year. Only 8% of responding businesses felt the national economy improved last quarter, while 20% believed national business activity declined. Despite historically low interest rates, ongoing concerns about the possibility of a war with Iraq, prolonged weakness in financial markets, and persistent volatility of oil prices have all weighed heavily on area firms' perceptions of the health of the national economy.

Responses tallied in Table 4 paint a remarkably different picture. With one exception, these results are substantially more favorable than those reported in the similar table found in the September 2002 **St. Cloud Area Quarterly Business Report**. Summary results from questions related to survey respondents' expectations of business conditions six months from now versus December 2002 are reported in

this table. The diffusion index for the question that asks about the level of future business activity for area companies is 56.9 (up sharply from a value of 22.6 reported last quarter). Two-thirds of surveyed businesses expect improved business conditions over the next six months (this is sharply higher than three months ago when only half of responding firms expected stronger future economic activity). In addition, 28% of firms surveyed last quarter anticipated a future decrease in business activity. That number declined to less than ten percent in the most recent survey. One area firm writes "business (is expected to) dramatically pick up for us in the second quarter of 2003." A second firm notes "seasonal construction activity plus interest rates that are low will cause an increase in construction."

When compared to the results of the September 2002 survey, business respondents expect a stronger labor market over the next six months. For example, the index on the survey item which asks about anticipated payroll employment is up from 15.1 to 27.5. Forty-one percent of survey

respondents expect to increase hiring over the next six months (the corresponding number was 25% in June). The diffusion index on length of the workweek is also improved from -3.8 to 13.8 as 22% of responding firms anticipate the workweek to lengthen by May 2003. It should also be noted that 57 percent of surveyed firms expect to increase employee compensation over the next six months and only one firm expects compensation to decline. Area firms also continue to expect little trouble finding qualified workers. The diffusion index on this item is little changed from its September value. These are all indications that the area economy is poised for recovery by the late spring or early summer months of this year.

Perhaps the most optimistic leading indicator of area firms' improved future outlook is the survey item asking firms about their future capital spending plans. The value of the diffusion index on this item is 29.5, the highest it has been since December 1999 (when the local economy was growing at an extremely rapid pace)! Thirty-seven percent of surveyed firms

Figure 2-Diffusion Index for Question 8: Difficulty Attracting Qualified Workers
Percent Increase Minus Percent Decrease

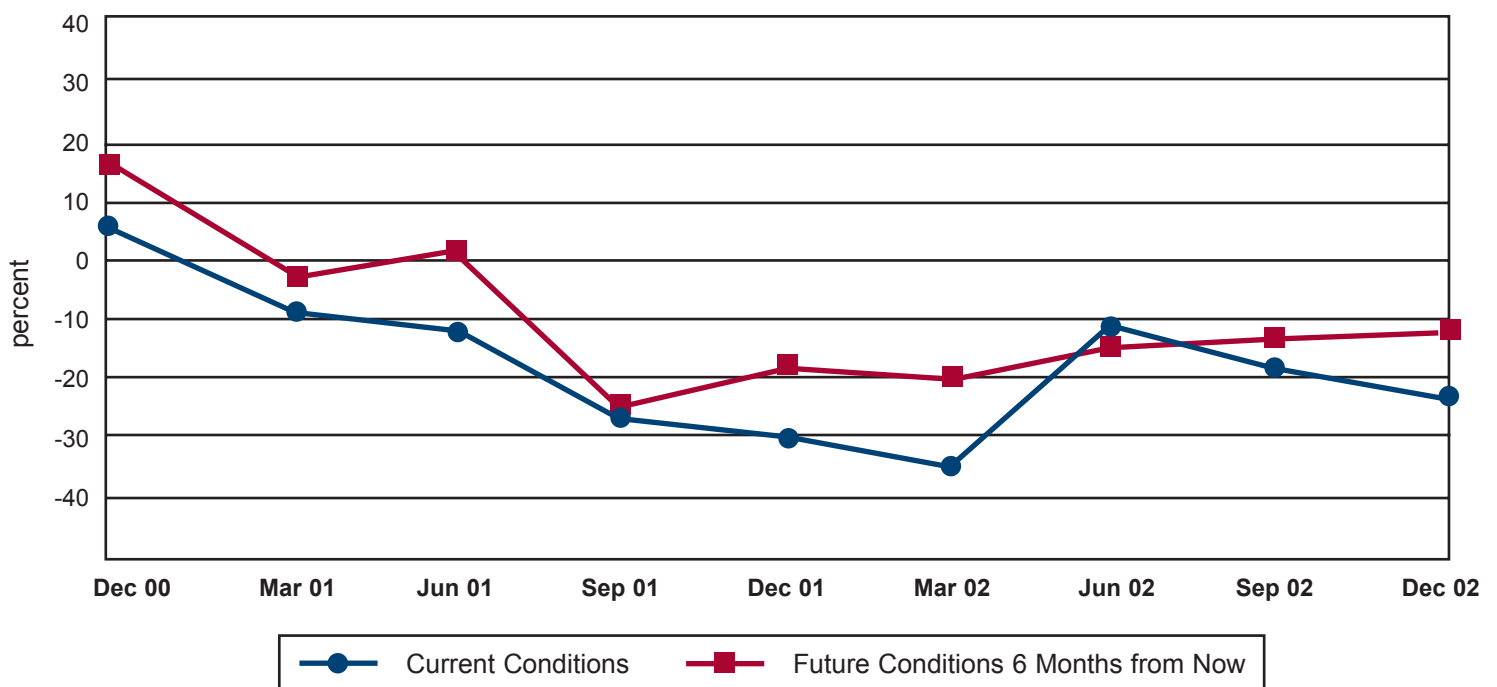


Table 3--Current Business Conditions*

ST. CLOUD AREA BUSINESS OUTLOOK SURVEY Summary Dec. 2002 <i>What is your evaluation of:</i>	December 2002 vs. Three Months Ago				September 2002 Diffusion Index ³
	Decrease (%)	No Change (%)	Increase (%)	Diffusion Index ³	
Level of business activity for your company	27.5	33.3	35.3	7.8	35.8
Number of employees on your company's payroll	19.6	58.8	19.6	0	24.5
Length of workweek for your employees	13.7	70.6	13.7	0	15.1
Capital expenditures (equipment, machinery, structures, etc.) by your company	11.8	60.8	25.5	13.7	24.6
Employee compensation (wages and benefits) by your company	0	74.5	23.5	23.5	32.1
Prices received for your company's products	15.7	70.6	9.8	-5.9	1.9
National business activity	19.6	56.9	7.8	-11.8	22.7
Your company's difficulty attracting qualified workers	21.6	66.7	9.8	-11.8	-7.6
Notes: (1) reported numbers are percentages of businesses surveyed. (2) rows may not sum to 100 because of "not applicable" and omitted responses. (3) diffusion indexes represent the percentage of respondents indicating an increase minus the percentage indicating a decrease. A positive diffusion index is generally consistent with economic expansion.					
* SOURCE: SCSU Center for Economic Education, Social Science Research Institute, and Department of Economics					

Table 4--Future Business Conditions*

ST. CLOUD AREA BUSINESS OUTLOOK SURVEY Summary Dec. 2002 <i>What is your evaluation of:</i>	Six Months from Now vs. December 2002				September 2002 Diffusion Index ³
	Decrease (%)	No Change (%)	Increase (%)	Diffusion Index ³	
Level of business activity for your company	9.8	19.6	66.7	56.9	22.6
Number of employees on your company's payroll	13.7	43.1	41.2	27.5	15.1
Length of workweek for your employees	7.8	68.6	21.6	13.8	-3.8
Capital expenditures (equipment, machinery, structures, etc.) by your company	7.8	52.9	37.3	29.5	24.5
Employee compensation (wages and benefits) by your company	2.0	37.3	58.8	56.8	50.9
Prices received for your company's products	7.8	49.0	35.3	27.5	18.9
National business activity	9.8	52.9	21.6	11.8	15.1
Your company's difficulty attracting qualified workers	17.6	64.7	15.7	-1.9	-3.8
Notes: (1) reported numbers are percentages of businesses surveyed. (2) rows may not sum to 100 because of "not applicable" and omitted responses. (3) diffusion indexes represent the percentage of respondents indicating an increase minus the percentage indicating a decrease. A positive diffusion index is generally consistent with economic expansion.					
* SOURCE: SCSU Center for Economic Education, Social Science Research Institute, and Department of Economics					

Local capital spending is expected to pick up.

expect to increase capital purchases over the next six months while only 8% expect to cut back on capital expenditures. As virtually all observers

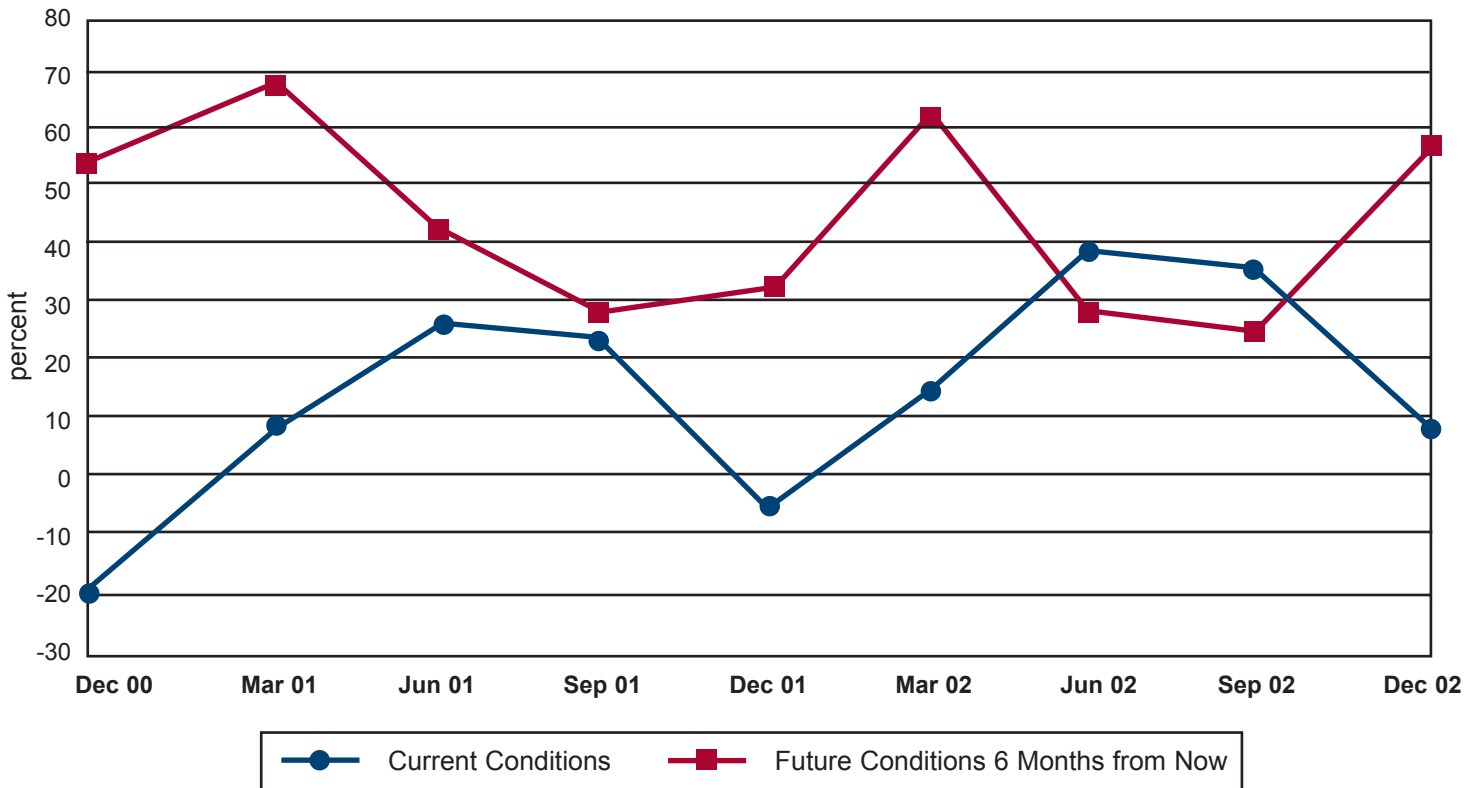
have remarked, any economic recovery is unlikely to be robust until capital spending picks up. Going forward, this is certain to be one of the bright spots for the area economy. Another uplifting local indicator is the expectation that firms will be able to pass on higher prices by mid-year. The diffusion index on prices received is up sharply from 18.9 in September 2002 to 27.5 in the current period.

The largest concern that survey respondents seem to have about the future of the St. Cloud area economy appears to be uneasiness about the pace of national business activity. The diffusion index on this survey item declined slightly to its lowest level in six months. Area firms could certainly benefit from less uncertainty about the health of the national economy.

An historical view of the evolution of the diffusion indexes on current and future business conditions over the past several quarters is presented in Figure 3. This shows an abrupt decline in the diffusion index on current business activity over the past three months. This index is now at 7.8 (its record high of 67.8 was recorded in June 1999, while its low of -19.3 occurred

in December 2000). This period's future business activity diffusion index indicates an equally sharp increase from last period's reported value. This index is well above its all-time low of 19.7 recorded in June 2000, and is only slightly below its value of 61.2 in March of last year. It should be noted that some of this represents a normal seasonal pattern of business activity that has now been observed over the four years that the survey has been conducted.

Figure 3-Diffusion Index for Question 1: Level of Business Activity
Percent Increase Minus Percent Decrease



Special Question #1: When Will a Sustained Recovery of the Local Economy Begin?

The St. Cloud area has experienced recessionary economic pressures since the summer of 2001. Last year’s Fingerhut closing and the associated spillover effects from this major shock to the Central Minnesota economy ensured that a recovery would not begin until after 2002. To be sure, not all area businesses have experienced weak economic conditions over the past 18 months. But many area firms (especially those in service industries and the retail sector) are looking for a return to the more vigorous business activity of the late 1990s. While the resilience of the area economy has allowed businesses to persevere during this trying period, firms in Central Minnesota must nevertheless be looking forward to a sustained economic recovery. Area business leaders were asked when they feel this recovery will begin. The results indicate that the majority of survey respondents feel the area economy has not yet bottomed out. Sixty-three percent of surveyed firms believe the recession will be over (and the recovery will begin) in the second or third quarter of this year. Besides being consistent with the **St. Cloud Index of Leading Economic Indicators**, these responses are generally consistent with many national observers’ view that the performance of the national economy will be improved around mid-year. Only 8% of responding firms think the recovery will begin later than the third quarter and a similar percentage think the current quarter is likely to be when the local economy emerges from its recent weakness. About 10% of surveyed businesses believe the recovery began in 2002.

Table 5--Special Question 1--WHEN WILL A SUSTAINED RECOVERY BEGIN?

Please indicate when you believe the local economy will begin a sustained recovery.*

Panel A: Survey Results

Began in Third Quarter	Began in Fourth Quarter	First Quarter 2003	Second Quarter 2003	Third Quarter 2003	Fourth Quarter 2003 or Beyond
5.9	3.9	9.8	39.2	23.5	7.8

* reported results are percent of surveyed businesses.

Panel B: Selected Survey Responses

Business leaders were asked to comment on when they thought a sustained recovery of the local economy would begin. These comments include:

- ◀ This is a qualified guess but, I believe that some of Fingerhut’s future being determined has helped start a recovery.
- ◀ Sustained [recovery] will occur when [the] public perceives the recovery is occurring.
- ◀ We have not seen a slow down in the past. We believe the local economy is relatively healthy.
- ◀ Indications are that the local economy has regained a positive attitude toward growth; and with the attractive loan rates make a sustained recovery on the horizon.
- ◀ Commercial customers in Central Minnesota are not seeing any increase in orders.
- ◀ Activity has increased.
- ◀ Too much negative world news-until the war begins people will be uneasy.
- ◀ Uncertain; if we go to war, I feel it will be a longer time before recovery begins.
- ◀ Based on discussions with local retailers, we anticipate 2nd quarter increases in our business.
- ◀ We are already seeing signs of a recovery because customers are asking for more services. However, I don’t believe we will see a sustained recovery until the 2nd or 3rd quarter of 2003.
- ◀ The bulk of our work is commercial. We will see an increase after residential work catches up.
- ◀ I think all companies will have made financial adjustments by [the 2nd quarter of 2003] due to the slower recovery of the stock market.
- ◀ We are seeing some signs of strengthening now but believe as many companies review 2002 success it will provide further impetus for a sustained recovery.

Special Question #2: The Extent to Which the Performance of Area Businesses is Affected by the Economic Health of Central Minnesota Rural Communities

A second special question asked area firms to consider the extent to which the economic health of neighboring rural Central Minnesota communities impacts their business. Citizens of rural communities make up a large customer base for many St. Cloud area businesses. In addition, area employers access a significant share of their work force in rural communities. The competitive challenges faced by rural retailers has been, of course, well documented. Equally challenging is the desire for the inhabitants of surrounding rural communities to enjoy high wage jobs while retaining the rural lifestyle to which they are accustomed. Results from this special question indicate that area firms are rather heavily impacted by the economic health of rural communities. Only 6% of those surveyed report that their business activities do not depend at all on economic conditions in surrounding rural areas. On the other hand, 16% of surveyed firms say this has a “large impact” on their business and 47% believe the economic well-being of rural areas is of moderate importance. Thus, 63% of the fifty-one firms surveyed indicate the economic health of rural communities is of moderate to large significance. The public-policy issues related to this pattern of responses are obvious. It is clear that the needs of neighboring rural communities cannot be ignored, and to a surprisingly large extent, the economic prosperity of St. Cloud area businesses depends on rural economic performance. Yet, with the ongoing decline in the relative importance of agriculture, healthy rural economies in the future will look considerably different than the traditional Central Minnesota stereotype. Results are reported in Table 6 and selected survey responses can be found below the table.

TABLE 6-Special Question 2 --THE EXTENT TO WHICH THE PERFORMANCE OF AREA BUSINESSES IS AFFECTED BY THE ECONOMIC HEALTH OF CENTRAL MINNESOTA RURAL COMMUNITIES

Some commentators have argued that the economic health of rural communities has profound spillover effects on urban areas. To what extent is the performance of your business affected by the economic health of Central Minnesota rural communities?*

Panel A: Survey Results

Not at all	Minor impact	Moderate impact	Large impact	Other	NA
5.9	27.5	47.1	15.7	0	3.9

* reported results are percent of surveyed businesses.

Panel B: Selected Survey Responses

Business leaders were asked to comment on their responses. These responses include:

- ◀ Our trade area is primarily Central Minnesota.
- ◀ Let’s face it. I always have believed keeping the farmers in profit keeps everything going.
- ◀ St. Cloud is somewhat sheltered because of its size and diversity.
- ◀ We have a significant number of clients in rural communities.
- ◀ Since most of our positions are tech, we don’t recruit much in rural areas.
- ◀ [Companies such as ours] do business more in accordance with interest rates than the economic health of rural areas.
- ◀ Many people from rural communities come to St. Cloud for shopping, medical, etc.
- ◀ Our business is not affected by rural communities to a large extent.
- ◀ Rural Minnesota economic health drives deposits and loan growth.
- ◀ 80% of the product [our company] produces is delivered within a radius of 75 miles.
- ◀ A significant amount of our sales are rural.

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Economic Outlook 2003 and the 41st Annual Winter Institute

The SCSU Center for Economic Education invites all readers of the St. Cloud Area Quarterly Business Report to attend the **9th Annual Economic Outlook** to be held at the St. Cloud Civic Center in downtown St. Cloud at 5 pm on Thursday, February 20, 2003. This year's panel consists of Dan Laufenberg, Chief Domestic Economist, American Express Financial Advisors, Tom Stinson, Minnesota State Economist, and Mark Partridge, SCSU Professor of Economics (and co-author of this report). The Economic Outlook program is held in coordination with the Minnesota Economic Development Center and is free to registered participants. For more information, contact the SCSU Center for Economic Education at 320-255-2157.

Readers are also invited to attend the **41st Annual Winter Institute** to be held at 8:45 am on February 21, 2003 at the Ritsche Auditorium on the SCSU campus. This year's keynote speaker is Federal Reserve Board Governor Ben Bernanke. As one of the seven members of the Federal Reserve Board, Governor Bernanke is one of the most influential economic policy-

makers in the U.S. The title of his talk is *Balance Sheets and the Recovery*. Harold Hodgkinson, co-director of the Center for Demographic Policy at the Institute for Educational Leadership, is this year's second speaker. Dr. Hodgkinson is a very entertaining speaker and is a renowned expert on demographic trends. The title of his talk is *Demographics is Destiny*. The Winter Institute program concludes with a regional experts panel who will address the *Regional Workforce of 2010*. This panel consists of U.S. Senator Norm Coleman, U.S. Congressional Representative Mark Kennedy, Teresa Bohnen, President St. Cloud Area Chamber of Commerce, John Frobenius, St. Cloud Hospital and CentraCare Health Systems and at least one other high profile area business leader. The Winter Institute is free and open to the general public. For more information, contact the SCSU Center for Economic Education at 320-255-2157.

We also want to thank Betty Schwarzkopf for her excellent help in producing this report for the last couple of years and wish her well in her new position. Participating businesses can look for the next survey at the beginning of March and the accompa-

nying **St. Cloud Area Quarterly Business Report** (including the **St. Cloud Index of Leading Economic Indicators** and the **St. Cloud Area Business Outlook Survey**) in late April. Area businesses who wish to participate in the quarterly survey can call the SCSU Center for Economic Education at 320-255-2157. All survey participants will receive a free copy of the **St. Cloud Area Quarterly Business Report** on a preferred basis.