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ST. CLOUD AREA
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LOCAL RECESSION MAY HAVE BEGUN

EXECUTIVE SUMMARY

The performance of the St. Cloud area economy has weakened over the last several months as area firms continue to face a variety of challenges in adjusting to uneven and uncertain business conditions. While the area is experiencing overall positive employment growth, several key sectors — including construction, manufacturing, retail trade, financial activities and government — have seen a year-over-year decline in payrolls. Taken together, the area sectors that have seen declining employment account for nearly 53 percent of local payrolls, suggesting a few strong performing sectors are leading modest growth in St. Cloud.

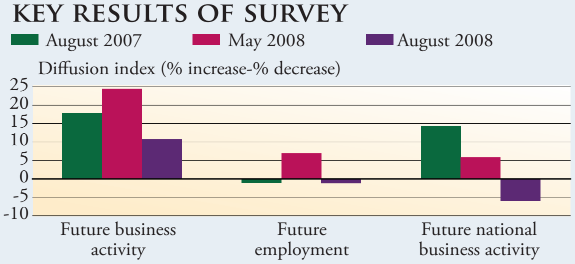
The St. Cloud economy continues to outperform the Twin Cities and the rest of the state in job growth. Year-over-year employment through July 2008 increased 0.7 percent in the local area. The Twin Cities saw 0.1 percent growth and employment was unchanged in the state of Minnesota. This modest local growth is, however, well below the long-term trend (annual local employment growth has averaged 2.1 percent over the past fifteen years). Combined with a host of factors (including continued high energy prices, financial market volatility and uncertain future monetary policy goals), the future outlook for the area economy is very clouded.

The St. Cloud Index of Leading Economic Indicators grew 1.9 percent in the last three months, almost entirely due to recent improvement in unemployment insurance claims. The probability of recession index swung sharply higher, indicating a 52.4 percent chance of a recession starting in August and a 64.9 percent chance for September.

Forty-one percent of surveyed firms report an increase in economic activity over the past three months, while 23 percent report a decrease. Only 17 percent of surveyed firms increased capital expenditures last quarter while 14 percent trimmed capital spending. This is the worst performance recorded on this item since 2002. All items from this quarter's current conditions index of the St. Cloud Area Business Outlook Survey are weaker than normally reported at this time of year.

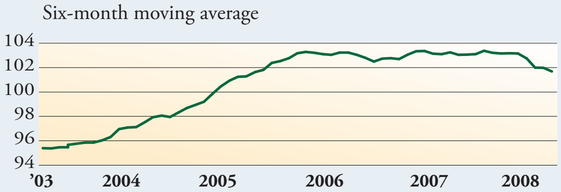
The future outlook is the weakest ever recorded in the survey. Only 41 percent of the 84 area firms that responded to this quarter's survey expect conditions to improve six months from now, while 30 percent expect a decline in future business activity. This relative pessimism is found in a variety of items in the future conditions index, where the indexes on future payroll employment, length of workweek, and national business activity are the lowest ever recorded in 9 ½ years of surveying local businesses. With few bright spots to point to, and a number of troubled sectors, the next six months could be very difficult for area businesses.

KEY RESULTS OF SURVEY



INDEX OF LEADING ECONOMIC INDICATORS

Six-month moving average



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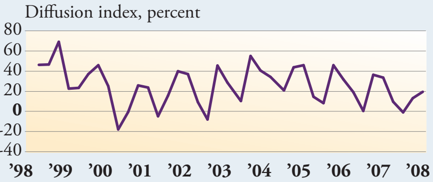
In special questions, half of surveyed firms expect inflation rates of 3-5 percent over the next 12 months—a range that is clearly outside of the Federal Reserve's comfort zone. Forty-three percent of surveyed business leaders expect John McCain to be elected president, while 39 percent think Barack Obama will be elected. Eighteen percent were unsure of the election outcome. Finally, area firms were surveyed on the extent to which they are involved in international trade. Relatively few local firms report being involved in exporting, importing, and input purchases and sales in other countries. Thirteen percent of firms report that they have either recently expanded or have plans to expand the international component of their business.

CURRENT ACTIVITY

Tables 1 and 2 report the most recent results of the business outlook survey. Responses are from 84 area businesses that returned the recent mailing in time to be included in the report. Participating firms are representative of the diverse collection of businesses in the St. Cloud area. They include retail, manufacturing, construction, financial, health services, 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.

Survey responses suggest that over the past three months the St. Cloud area continued to experience economic conditions that are weaker than normal for this time of year. The current activity diffusion index (representing the percentage of respondents indicating an increase minus the percentage indicating a decrease in any given quarter) is 17.9 in this quarter's survey, which is much lower than was reported one year ago (when it was 32.2), but is somewhat above the reading of 11.6 three months ago. Readers will note that this is essentially precisely what was written about this survey item three months ago; little has changed with regard to current conditions.

CURRENT BUSINESS ACTIVITY



The employment diffusion index moved into positive territory from its negative reading three months ago, though it is well below what is normally expected in the summer survey. For example, the current value of the index is 7.1, which compares unfavorably to the value recorded in August 2005, when the index was at 21.1. Recent media reports have noted declining average hours worked as another sign of labor market weakness. This is found in the local survey, where the index value of 2.4 on length of workweek is the lowest ever recorded in a summer survey. Most businesses have experienced no change in attracting qualified workers and 12 percent note it is less difficult finding qualified workers. Overall, it is a difficult time for area workers, who are coping with declining labor demand in several area sectors (highlighted by layoffs at Grede Foundries, Park Industries, Times Media, Crystal-Pierz Marine and some area restaurants) during a period in which the cost of living is increasing.

Wage pressures appear to be restrained at this time. The diffusion index on current worker compensation is 25.5, which is below normal index values and appears to show no signs of the type of cost driven inflation that has concerned some economists in recent months. Likewise, prices received appear to be normal for this time of year, which may be a concern for some area firms that are experiencing an acceleration in nonlabor input costs (particularly en-

TABLE 1-CURRENT BUSINESS CONDITIONS

	August 2008 vs. Three months ago				August 2008
	Decrease (%)	No Change (%)	Increase (%)	Diffusion Index[3]	Diffusion Index[3]
What is your evaluation of:					
Level of business activity for your company	22.6	36.9	40.5	17.9	11.6
Number of employees on your company's payroll	15.5	61.9	22.6	7.1	-5.8
Length of the workweek for your employees	10.7	76.2	13.1	2.4	5.8
Capital expenditures (equipment, machinery, structures, etc.) by your company	14.3	67.9	16.7	2.4	9.3
Employee compensation (wages and benefits) by your company	5.5	65.5	31.0	25.5	13.9
Prices received for your company's products	14.3	54.8	27.4	13.1	10.4
National business activity	22.6	45.2	23.8	1.6	-15.1
Your company's difficulty attracting qualified workers	11.9	73.3	11.9	0.0	7.0

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

WHAT IS AFFECTING YOUR COMPANY?

Comments to this question include:

• "We do mostly seasonal work. Winter is our slow time of the year."

• "Subprime mortgage fallout and high gas prices (are adversely affecting us). Poor consumer confidence in the economy. A lot of people are uncertain."

• "Right now, farm land is the hottest part of the real estate industry, followed by apartments. Commercial is slow but steady. Single family (housing) has been well chronicled."

• "We are in the housing sector. There is no good news on the horizon in this industry—not in banking, not in construction, and not in foreclosure abatements. It's very, very difficult to keep deals going in the right direction."

• "We are a construction-related business in the midst of our seasonal increase. Things are busier, but not as busy as they should be."

• "The agricultural and commercial (components of our business) have been good. Estate … work is consistent as is divorce … work."

• "With a poor economy, (our service) is not a priority. We're doing more customized (work) rather than our traditional (offerings)."

• "The reluctance of cities and other government bodies to move projects forward has a bad impact on our workload and staffing."

• "We are going to see substantial food price inflation due to our biofuels policy, which uses 1/3 of the corn crop for ethanol."

• "High fuel (prices) … (and) no housing (and) building is affecting us."

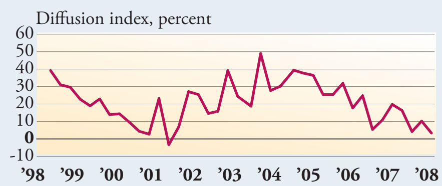
• "Political fundraising activities (are benefiting us). Busy through the election, then expect a slowdown."

• "Instead of being cautious during this period of economic slowdown, I became aggressive, expanded my capital expenditures and product offerings. It is working."

ergy and materials prices). After recording negative values for the past three quarters, the current national business activity index item moved into positive territory this quarter. Perhaps this is related to the fiscal stimulus of the past few months, although these effects are certain to be temporary and likely to be minor. In addition, the future outlook for national business conditions (see Table 2 below) is a concern.

Finally, in many ways the survey item that is most troubling is the reading on current capital expenditures. Among other things, capital expenditures serve as an indicator of business planning for the future. Firms that feel existing capacity is satisfactory to meet future demand will likely abstain from capital spending commitments until business is expected to improve. For the capital expenditures diffusion index in Table 1 to record its lowest number since 2002 (at a time when the future business conditions index reported in Table 2 is very weak) should be a sign of concern for local companies. During normal times, the value of this index is about 35, so a reading of 2.4 is worrisome.

CURRENT CAPITAL EXPENDITURES



FUTURE OUTLOOK

Table 2 reports the future outlook for area businesses. With four of the survey items in this table reaching their lowest values ever recorded, it is safe to say that the local outlook is highly unfavorable. There are very few bright spots to which to point.

TABLE 2-FUTURE BUSINESS CONDITIONS

	Six months from now vs. August 2008				
	Decrease (%)	No Change (%)	Increase (%)	Diffusion Index[3]	May 2008 Diffusion Index[3]
What is your evaluation of:					
Level of business activity for your company	29.8	29.8	40.5	10.7	24.4
Number of employees on your company's payroll	21.4	58.3	20.2	-1.2	6.9
Length of the workweek for your employees	21.4	69.0	8.3	-13.1	1.2
Capital expenditures (equipment, machinery, structures, etc.) by your company	9.5	65.5	23.8	14.3	12.8
Employee compensation (wages and benefits) by your company	0.0	65.5	34.5	34.5	33.7
Prices received for your company's products	10.7	51.2	33.3	22.6	30.3
National business activity	25.0	46.4	19.0	-6.0	5.8
Your company's difficulty attracting qualified workers	8.3	78.6	10.7	2.4	12.8

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

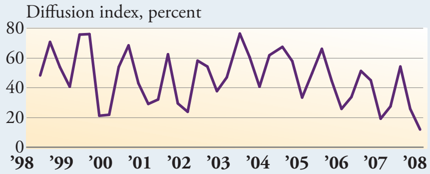
Well-publicized layoffs, business closures, rising prices, declining sectors, an uncertain future policy mix, volatile financial markets, and a highly visible national election makes it very challenging for the area economy to hold its course.

In recent issues of the St. Cloud Area Quarterly Business Report we have noted how difficult economic forecasting has been over the last several months. We have been particularly committed to carefully scrutinizing economic data — international, national, state, regional, local — for clear signs of a cyclical turning point. It is possible that the local economy has reached a peak, though we cannot pinpoint the date with precision. But the results of this quarter's future business conditions survey ... suggest the balance of this year and the first quarter of 2009 could be a challenging period for area businesses.

While conflicting signals remain — the second quarter GDP report, in which the export-driven economy is gauged to have grown at a 3.3 percent annualized rate makes it very difficult to utter terms like recession — if the survey results from Table 2 play out, the next six months could be a tough time in the St. Cloud area.

FUTURE BUSINESS ACTIVITY

Diffusion index, percent

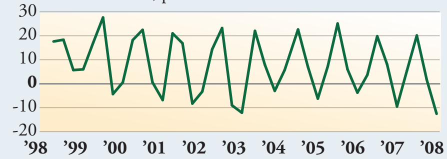


As shown in the accompanying chart, the diffusion index on future business activity, at a value of 10.7, has never been lower. In addition, the index on expected future employment is negative for only the second time (the first time was one year ago). Furthermore, the -13.1 value on the future length of workweek item (see chart) is the lowest ever recorded. Area workers can expect very difficult times at the beginning of the new year.

Area capital expenditures are not expected to rebound over the next several months. Only 24 percent of firms expect to increase capital expenditures over the next several months, while 10 percent plan to cut back on capital spending. This is

FUTURE LENGTH OF WORKWEEK

Diffusion index, percent



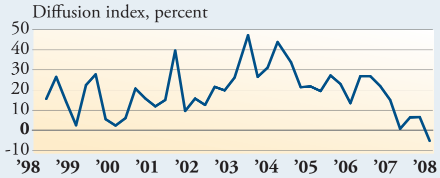
well below what is normally expected and is not the type of bounce that one would expect to observe from the period of current weakness in this series. Surveyed firms expect to keep employee compensation in control over the next six months—indeed, the 34.5 value of the index is below what is normally expected. The prices received index is also within its normal range, so pricing pressures appear to remain restrained.

National business conditions at the beginning of 2009 are expected to be the worst ever recorded in the survey. This index has never before been negative, but it has now registered a recording of -6.0, where 25 percent of firms expect a decline in national business activity and only 19 percent expect national conditions to improve. This is worth keeping an eye on, since there is a very limited scope of public policy alternatives that can help counteract this expected weakness. Fiscal stimulus has already been used in the last few months and monetary policy is limited by concerns over future inflation. Fed policymakers have already indicated that their next interest rate move is just as likely to be an increase in interest rate targets as a decrease (and no one really believes that a 2 percent funds rate target is sustainable when inflation rates are 3 percent or higher and the relative price of oil and other commodities has increased).

So, we could be in for a tough stretch — one in which public policy may be ineffective in cushioning expected economic weakness.

FUTURE NATIONAL BUSINESS ACTIVITY

Diffusion index, percent



SPECIAL QUESTIONS

For the first time in many years, some economists are voicing concern about inflationary expectations. Recent months have seen the all-items consumer price index grow at an annualized rate in excess of 5 percent. While this has been isolated to a few select months and doesn't utilize the preferred measure of Fed policymakers, inflation rates like this have not been seen in a quarter century. For the first half of 2008, the all-items CPI grew at an annualized rate of 4.2 percent — much higher than the 2007 rate of 2.8 percent (which was itself outside of the Fed's likely comfort range of 1.5 – 2 percent). To be sure, monetary policymakers tend to focus on more comprehensive inflation measures — and they tend to follow core rates of inflation (a measurement that excludes food and energy costs from the price index) to observe underlying inflationary forces. While there is no evidence yet that accelerating food and fuel prices have systematically impacted core prices, it is noteworthy that a modest increase from core CPI rates of 2.3 percent for the first half of 2008 could easily find this series in the 3 percent range. Of course, to many people, adjusting the impact of food and energy costs out of the targeted inflation measures is a questionable practice. As Fed Chairman Ben Bernanke has noted: "We drive; we eat; we understand that inflation involves all prices, not just those that are not volatile."

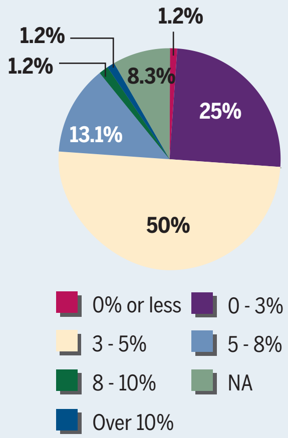
And, Fed policy has been quite expansionary in recent months, as monetary policymakers have focused on both stimulating the economy and ensuring there is adequate liquidity in financial markets. A persistent increase in the average level of prices can only come from excessive money growth. So the alarm bells are in place to alert policymakers and the public about increasing inflationary pressures.

We decided to see what area businesses expect with regard to the inflation rate over the next 12 months. While we aren't able to report an estimate for the expected inflation rate, we are able to use survey responses to get a sense of the range of inflation rates that businesses expect. It would appear that area businesses are slightly more concerned about inflationary pressures than U.S. markets. One-half of surveyed businesses expect inflation rates in the 3-5 percent range over the next 12 months. By comparison, the expected future inflation rate implied from the U.S. Treasury Inflation Protected Securities market is less than 3 percent.

One-quarter of survey participants expect an inflation rate between 0 and 3 percent and 13 percent of businesses expect inflation in the 5-8 percent range. Several businesses were unsure and didn't respond.

Business leaders were asked:

QUESTION 1
Within which of the following ranges does your business expect the U.S. inflation rate to be over the next 12 months?



*Numbers may not add up to 100 due to rounding.

Responses to Special Question 1:

• "I wish I could circle the 0-3% (option), but unfortunately the oil crisis will not subside, driving inflation to a 5-7 percent level."

• "Depends on oil prices. This affects everything."

• "Inflation is understated — replace all the economists with housewives for a more accurate measure."

• "(3-5 percent), per higher (industry) price index."

• "Rising energy, food, and steel prices will push inflation higher."

• "It looks like the corn and soybean crops will exceed expectations. This should keep food costs down."

• "If gasoline prices continue to increase, this impacts the cost of food, clothes, etc."

• "Food inflation will increase faster (6-8 percent) due to biofuels policy."

• "Over 10 percent due to raw material price increases."

• "The economy seems volatile and will take a while to stabilize."

• "Our industry — 'construction' — is experiencing more material cost increases than the norm!"

• "With increased cost of energy, an increase (in average inflation rates) is probable."

• "We try to keep positive — huge impact on our business."

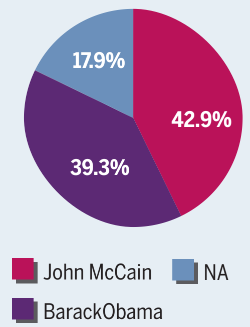
• "Has to level off or we are in a lot of trouble."

• "Prices are increasing faster than we are able to pass them on to our customers."

• "I would expect the government will keep a close eye on inflation."

The U.S. presidential election is the headline event of the fall months, and there is no shortage of predictions, polls, surveys, and markets that attempt to forecast the outcome of the election. We thought it would be fun to ask area business leaders who they expect will win the election. We made a point of noting that this was not a request of who they planned to vote for—instead, we simply wanted to know who they thought would win. The results were very close. McCain is cited by 42.9 percent of respondents, while 39.3 percent of the survey participants predicted Obama and 17.9 percent of respondents either didn't respond or didn't know. Given the number of people who didn't respond, there isn't much that can be said about these percentages. But let's suppose this 17.9 percent was evenly split between the two candidates. This would give McCain about 52 percent and Obama a little more than 48 percent. Interesting given the Iowa Electronic Markets —where futures contracts for the U.S. presidential election are traded— have the democratic candidate trading at a 59 percent vote share and the republican candidate at 41 percent. We make no claims about the scientific validity of our survey results, but area business leaders have been very accurate in predicting economic events over the past nine and a half years.

QUESTION 2
Which candidate do you expect will be elected president? Please note that this is not asking you for whom you plan to vote.



*Numbers may not add up to 100 due to rounding.

Responses to Special Question 2:

• "The Obama fascination is subsiding and McCain will win in a close race."

• "I think people will come to their senses and realize the flashy talk of Obama is just that."

• "Thinking most want a change—Obama is vastly different than Bush."

• "(Obama). He's confident, charismatic and a change from Bush."

• "(McCain)…might be a long shot, but better be a Republican or we're doomed."

• "It seems that Obama's experience is being questioned more and more."

• "No idea. I'm already tired of the campaign ads."

• "(Obama). People are angry at the current direction of the country."

• "Folks will vote for McCain because, as a person (who is) 72 years old, he will not be concerned about re-election and will be more willing to make the right decisions for the good of all U.S. citizens."

• "(McCain). Obama says a lot — with no facts — where is all the money coming from? How much more in taxes can Americans afford?"

• "(Obama). This country has suffered from lack of leadership for many years and this election offers nothing different."

• "(Obama). People will think Democrats will change things."

SCSU's economics department (of which the two authors are members) is cooperating with the dean's office in the Herberger College of Business at SCSU to explore the extent to which area businesses take advantage of international opportunities. Among other things, a variety of valuable resources are available from SCSU to assist area firms with their work in foreign countries. Therefore, we decided to use some simple background questions to explore area businesses' current involvement in international markets. We asked businesses:

QUESTION 3
We are interested in the international component of your business. Does your company engage in any of the following activities?
a. Exports
b. Imports
c. Input purchases
d. Input sales
Do any of the international components referenced above account for more than 25 percent of your company's total operations?

The results speak for themselves. Only

12% of surveyed businesses are engaged in export activities, 16 percent import items from other countries, 16 percent purchase inputs directly from other countries, and only 6 percent sell inputs to other countries. To be sure, many service-providing firms do not have a scale of operations or a scope of business to have an international component, but several businesses that might be expected to benefit from active participation in international markets have not yet pursued these opportunities. This will be the subject of further questions in upcoming business surveys.

Responses to Special Question 3:

- "(Imports of) lumber (from) Canada."
- "We do not directly purchase imports, but our purchasing group does. This amount has been going down lately."
- "…we purchase many products from Canada."
- "Since we are a service firm, we do not operate internationally."
- "25% of our product comes from Japan."
- "Equipment was all built in the USA—now all (of it is) done in China."
- "We participate and support many businesses with international trade."

Our final question was correlated with special question 3. We asked area firms if they had either attempted to expand or planned to expand their international component. The results were similar to the pri-

EMPLOYMENT DURING RECESSIONS

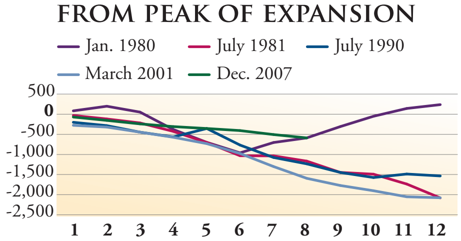
BY NOW YOU HAVE PROBABLY HEARD THAT ECONOMISTS DO NOT DEFINE RECESSIONS as "two consecutive quarters of GDP decreasing." They use a group of five indicators, the two most important of which are payroll employment and personal income.

For the last eight months, payroll employment has declined nationally. In the post-World War II period, there has never been eight consecutive months of employment decline without there being a recession, although the start of the decline has not always marked the start of the recession. What has made this period different has been the relatively mild decline in employment.

The graph below shows the decline in employment following the peaks of business cycle expansions as determined by the National Bureau of Economic Research (NBER). We then include the decline in employment that has happened so far from the peak of that series in December 2007. (We note that NBER has not set a date for the peak of the expansion, meaning they have not yet determined that a recession has begun.)

Each line measures how much employment has declined or increased in each month after the business cycle peak. In all cases except the January 1980 recession, the decline in employment lasted more than 12 months. And compared to those recessions, with an average cumulative job loss of more than a million workers, the decline in employment since December 2007 has been 463,000. If this has been a recession, it has been the mildest one in memory.

NATIONAL EMPLOYMENT FROM PEAK OF EXPANSION



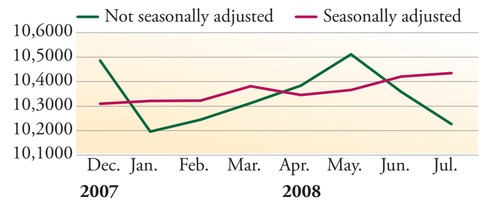
NOTE: Data through August 2008

Looking at the St. Cloud data for comparison is somewhat more difficult for two reasons. First, we only have data since 1988, and we do not have a monthly series of local area income through which we can better determine business cycle peaks. We have, however, tried to ascertain dates using only the employment series. The graph below shows the data for the St. Cloud metro area with the dates we determined for previous local business cycle peaks: October 1989, May 1996 and May 2001. We then use the same starting date as the current decline in national employment.

Second, local area employment data are highly seasonal, which makes data comparisons flawed unless adjusted. The data presented below has been adjusted by a simple procedure. The adjustment process can be seen in the graph below in which we show the unadjusted and adjusted employment data for December 2007 through July 2008. There are natural peaks in seasonal employment in the fall in the St. Cloud area, and troughs in January and summer (owing to holidays and closing schools, respectively.)

The result is striking. The adjusted data show that over the first seven months of 2008 the St. Cloud economy added jobs at a 2.1 percent seasonally adjusted annual rate. That growth rate is about the normal growth rate of employment in the St. Cloud area. This stands in stark contrast to our observation of the diffusion of rising and declining industries we note elsewhere in this report. The reason for this is that several of those declining industries are those which we would expect to decline in summer (like local government) and after holidays (retail sales, for example). The recent engines of employment in St. Cloud, such as education and health services or business services, have maintained vigorous growth over the last 12 months.

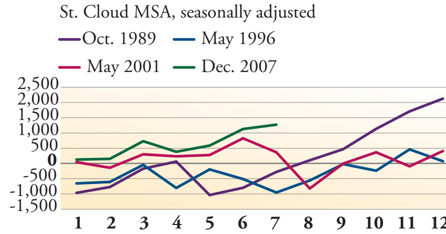
ST. CLOUD EMPLOYMENT

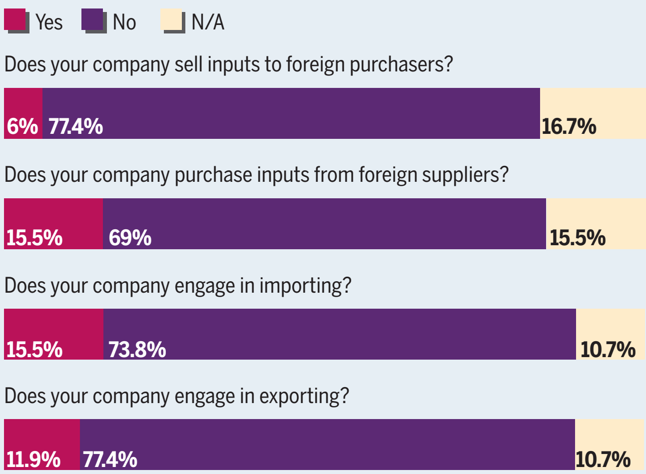


The current period and the May 2001 "recession" so far share similarities. In both cases, on a seasonally adjusted basis, local area employment grew at a lower-than-normal rate. But that recession was elongated by the closure of Fingerhut. We have seen smaller layoffs over the summer, but nothing so far of that magnitude.

EMPLOYMENT AFTER PEAKS

St. Cloud MSA, seasonally adjusted

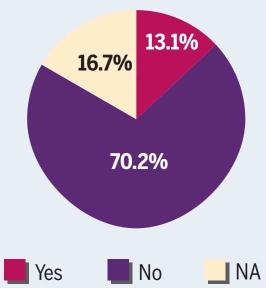




*Numbers may not add up to 100 due to rounding.

or question, with only 13 percent of firms answering yes. Written responses reveal the nature of some of these actions.

QUESTION 4
Has your company either attempted to expand its international component or have plans to expand its international component?



Responses to Special Question 4:

- "We would like to but are interested in who in the state or federal government that we need to contact."
- "No, but some of our clients indicate they are looking at 'reglobalizing' due to transportation cost increases."
- "There are some possibilities we are looking at."
- "Sales to Canada and Australia."
- "I'm in real estate, which is mostly a local activity."
- "Continually attempt to expand…opportunities (to our domestic and international customers)."
- "Canada sales efforts have increased. European inquiries have increased on their own."
- "(Yes, our) imports are increasing."

SECOND HALF RECESSION?

Table 3 shows the pattern of industries experiencing employment expansion and contraction over the last year. As measured by share of employment, almost an equal number of industries are expanding and contracting. Were it not for the education and health sectors, it is unlikely the economy would have experienced even the mild 0.7 percent employment growth we had over the last year. The 12-month change figures mask variation over that time period: There was more slowing of the economy in the latter half of 2007 and some growth in spring. Importantly, the St. Cloud area has done better over the year than has the state as a whole or as has the Twin Cities. Construction employment in the Twin Cities adjusted later than it did in the St. Cloud area, which is acting as a drag on employment there.

Noticeably in Table 4, the number of St. Cloud residents who were working in July 2008 was 0.8 percent below its July 2007 level. This would suggest that the increase in employment in St. Cloud is being accounted for more by workers who do not live in the area (recall that the St. Cloud "Metropolitan Statistical Area" or MSA includes Benton and Stearns counties, but not Sherburne.) With an increase in the labor force in the MSA, our unemployment rate leaped to 5.6 percent, above those in the state and

TABLE 3 - EMPLOYMENT TRENDS

	St. Cloud (Stearns and Benton)			13-county Twin Cities area			Minnesota		
	15-year trend growth rate	July '07-July '08 growth rate	July '08 employment share	15-year trend growth rate	July '07-July '08 growth rate	July '08 employment share	15-year trend growth rate	July '07-July '08 growth rate	July '08 employment share
Total nonagricultural	2.1%	0.7%	100.0%	1.5%	0.1%	100.0%	1.4%	0.0%	100.0%
Total private	2.2%	1.0%	87.2%	1.5%	-0.4%	87.2%	1.5%	-0.3%	85.8%
Goods producing	1.7%	-1.7%	22.5%	0.1%	-3.6%	15.3%	0.3%	-2.7%	17.0%
Construction/natural resources	2.6%	-1.8%	5.4%	2.3%	-6.5%	4.3%	2.2%	-3.9%	4.8%
Manufacturing	1.4%	-1.6%	17.1%	-0.6%	-2.4%	11.0%	-0.4%	-2.3%	12.2%
Service providing	2.2%	1.4%	77.5%	1.7%	0.7%	84.7%	1.7%	0.5%	83.0%
Trade/transportation/utilities	0.5%	0.1%	20.9%	0.9%	-0.6%	18.7%	1.0%	0.2%	19.0%
Wholesale trade	1.8%	0.5%	4.5%	1.2%	-1.8%	4.8%	1.3%	-0.1%	4.8%
Retail trade	-0.3%	-1.0%	13.0%	1.2%	-0.6%	10.3%	1.0%	0.1%	10.9%
Trans./warehouse/utilities	2.4%	3.7%	3.5%	0.0%	1.0%	3.6%	0.4%	0.7%	3.3%
Information	1.6%	-0.2%	1.2%	0.6%	0.7%	2.4%	0.3%	-0.2%	2.1%
Financial activities	3.9%	-0.5%	4.6%	1.5%	1.2%	8.0%	1.7%	0.7%	6.5%
Professional & business service	5.6%	4.5%	8.9%	2.0%	-1.1%	14.8%	2.3%	-0.6%	11.9%
Education & health	3.5%	2.5%	15.9%	3.4%	2.3%	14.2%	3.4%	1.9%	15.6%
Leisure & hospitality	2.6%	1.7%	9.1%	2.1%	0.9%	9.6%	1.8%	0.1%	9.5%
Other services (excluding govt.)	1.8%	8.5%	4.1%	1.6%	-0.6%	4.3%	1.1%	-1.0%	4.2%
Government	1.4%	-1.4%	12.8%	1.2%	3.3%	12.8%	0.9%	1.3%	14.2%
Federal government	0.6%	2.2%	1.7%	0.1%	0.6%	1.2%	-0.1%	0.5%	1.2%
State government	1.8%	0.1%	3.1%	2.0%	4.5%	3.8%	1.5%	1.9%	3.3%
Local government	1.4%	-2.7%	8.0%	1.0%	3.1%	7.8%	0.9%	1.2%	9.7%

Note: Long-term trend growth rate is the compounded average employment growth rate in the specified period.

Source: Minnesota Department of Employment and Economic Development and author calculations.

in the Twin Cities. All other indicators, from building permits to help-wanted linage to initial claims for unemployment insurance, registered weakness for the local economy between May and July, and the St. Cloud Index of Leading Economic Indicators declined sharply over the last year.

Nevertheless, the last quarter has had three of four leading indicators in positive territory, though two of those three just mildly so. After sharp increases in unemployment claims in the first third of this year, the last three months have seen a marked improvement in this indicator, accounting for most of the recent rebound in St. Cloud LEI. Hours worked continued to decline in this period, which bodes particularly poorly for the key manufacturing sector of the economy.

The St. Cloud area showed a probability of recession starting in August 2008 of 52.4 percent and in September of 64.9 percent. These are the highest values since May 2003, when the local economy was just completing the effects of the Fingerhut closing. While probabilities recede after this point, it is important to note it would take a few months' readings of below 20 percent before we would expect a signal of recovery. Evidence from previous local area recessions (as discussed in the box) shows that in two of the previous three recessions, employment did not pick up for a year after the peak of the expansion. The data therefore begin to cast a dark cloud on the first half of 2009, which is very consistent with the survey results reported earlier in this report.

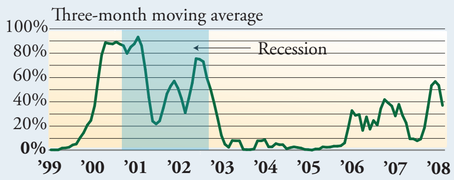
This notion of a recession having been delayed but not avoided has appeared in national surveys as well. The revision of GDP growth in the second quarter to a positive 3.3 percent annual rate reflected strong growth in exports and the effects of tax rebates. But that growth may have borrowed stimulus from the second half of this year. The Wall Street Journal survey of forecasters – as of this writing having last been taken before the GDP revision – showed expectations for GDP growth of 1.3 percent in the third quarter and 0.6 percent in the fourth. The probability of recession for the August 2008-August 2009 period was 63 percent. Only four of the 53 forecasters surveyed put the probability at 25 percent or less.

TABLE 4-OTHER ECONOMIC INDICATORS

	2007	2008	Percent change
St. Cloud MSA labor force July (Minnesota Workforce Center)	107,007	107,634	0.6%
St. Cloud MSA civilian employment # July (Minnesota Workforce Center)	102,491	101,644	-0.8%
St. Cloud MSA unemployment rate* July (Minnesota Workforce Center)	4.2%	5.6%	NA
Minnesota unemployment rate* July (Minnesota Workforce Center)	4.7%	4.9%	NA
Minneapolis-St. Paul unemployment rate* July (Minnesota Workforce Center)	4.2%	5.4%	NA
St. Cloud-area new unemployment insurance claims May-July average (Minnesota Workforce Center)	867.3	909.0	4.8%
St. Cloud Times help-wanted ad linage May-July average, in inches	5,589	4,587	-17.9%
St. Cloud MSA residential building permit valuation In thousands, May-April average (U.S. Department of Commerce)	11,754.3	8,999.3	-23.4%
St. Cloud index of leading economic indicators July (St. Cloud State University)**	103.4	101.1	-2.2%

MSA = St. Cloud Metropolitan Statistical Area, composed of Stearns and Benton counties.
# - The employment numbers here are based on household estimates, not the employer payroll estimate in Table 3.
* - Not seasonally adjusted
**- January-March 2001=100
NA - Not applicable

PROBABILITY OF A RECESSION



It is unlikely that either monetary or fiscal policy will provide any stimulus over the next few months as the elections take most of the political actors' focus away from economic concerns. The Federal Reserve is hemmed in by inflationary concerns as well, with there now being a slight bias in Federal funds futures forecasts toward the Fed raising interest rates. The weaker dollar has provided some stimulus to exports, but as European economies have begun to weaken, it is likely neither that the dollar will weaken further nor that exports will continue to improve.

A strengthening dollar may be helping with gasoline prices though, at least in the short run. The effects of Hurricane Gustav have largely been through disruption of oil tanker flows into the refineries in the Gulf Coast. As of this writing we have not seen major changes in oil prices, though OPEC production in August fell slightly. Congressional action on an energy plan could happen by the time this report is published. All these are adding to uncertainty over energy prices that area business leaders are experiencing.

Nationwide and globally, business confidence has slipped since the realization that the effects of the tax rebate checks have been exhausted, though the Moody's business confidence index for the U.S. is above where it was last winter when the subprime mortgage crisis had everybody's attention. We think this is consistent with a country waiting on those "changes" that both political parties promise us are coming after the election – buoyed by an almost-even divide between business leaders who think McCain or Obama will win. And it is consistent with a country wondering if the stimulus of spring will be enough. We have our doubts that it was, and whoever wins will have a full economic agenda facing him come January.

TABLE 5-ELEMENTS OF ST. CLOUD INDEX OF LEI

Changes from April to July 2008	Contribution to LEI
Help-wanted advertising in St. Cloud Times	0.42%
Hours worked	-1.03%
New business incorporations	0.05%
New claims for unemployment insurance	2.42%
Total	1.86%

IN THE NEXT QBR Participating businesses can look for the next survey in November and the St. Cloud Area Quarterly Business Report in the January-March edition of ROI. Area businesses that wish to participate in the survey can call the St. Cloud State University Center for Economic Education at (320) 308-2157.