Spring 2010

St. Cloud Area Quarterly Business Report, Vol. 12, No. 2

King Banaian
St. Cloud State University, kbanaian@stcloudstate.edu

Richard A. MacDonald
St. Cloud State University, macdonald@stcloudstate.edu

St. Cloud Area
Quarterly Business Report
VOL. 12, ISSUE 2 • SPRING 2010

LOCAL GROWTH RETURNS

IMPROVEMENT IN LABOR MARKET SIGNALS END OF AREA RECESSION

Executive Summary

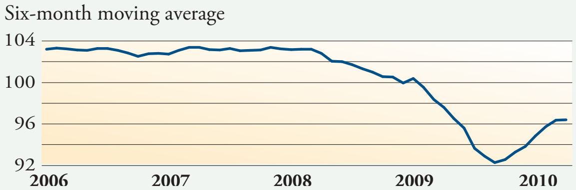
Improvement in the labor market and cautious growth in key sectors of the local economy appear to signal the end of the area recession. While some sectors of the area economy continue to struggle through cyclical and structural adjustments, the outlook for the remainder of the year is much brighter than it was one year ago.

April employment data for the St. Cloud area show growth in local employment. Annualized job growth of 0.5 percent, while below the long-term trend rate of growth, is a considerable improvement over April 2009, when year-over-year employment declined by 1.3 percent. St. Cloud's employment situation is substantially better than conditions felt statewide. For example, state employment fell 0.8 percent over the year ending April 2010. The Twin Cities fared worse — its employment fell 1.7 percent over the same period.

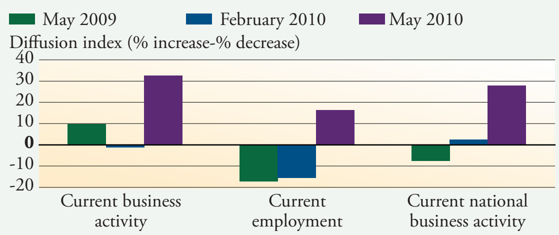
Much of the reported job growth can be attributed to disproportionate gains in area government employment. Year-over-year growth in local jobs in the government sector was 4.7 percent. Job growth occurred in local, state and federal government sectors. Without these jobs, area employment would have declined — the private sector shed jobs at a rate of 0.5 percent over the year ending April 2010. No other major metropolitan area in Minnesota has been more dependent on government employment in the recovery of its labor market. It remains to be seen if job growth in the public sector is sustainable.

INDEX OF LEADING ECONOMIC INDICATORS

Six-month moving average



KEY RESULTS OF SURVEY



The two local statistical indicators we use give a little pause to this optimism. The Index of Leading Economic Indicators has fallen in the past quarter but has grown more than 2 percent since April 2009. The Probability of Recession Index shows a 55 percent chance of recession in late summer. But data on local area employment, corrected for seasonal factors, point to robust growth since last September.

Fifty-four percent of surveyed firms report an increase in economic activity in the past three months, while 21 percent report a decrease. While this is, in part, a normal seasonal pattern, it is a considerable improvement over the survey from one year ago, when only 42 percent of firms experienced an increase in current activity and 32 percent reported weaker conditions. Survey responses designed to measure the health of the local labor market are also improved from one year ago. In May 2009, 32 percent reported decreased employment from the earlier quarter. This year, only 13 percent reported a reduction in payrolls. In addition, the employee compensation index is improved from last year. Its current value of 10.4 is a marked improvement from a -1.1 reading last year. Much of the explanation for improved current conditions can be attributed to better national business conditions. The index on current national business activity is 27.9, a dramatic improvement from last May,

COLLABORATING PUBLISHERS

St. Cloud State University
A tradition of excellence and opportunity
Center for Economic Education
Department of Economics
Social Science Research Institute

The Partnership
St. Cloud Area Economic Development Partnership
President: Tom Moore
320-656-3815

ABOUT THE AUTHORS

KING BANAIAN
Chairman
Economics Department,
St. Cloud State University
320-308-4797

RICH MACDONALD
Assistant Professor,
Department of Economics,
St. Cloud State University
320-308-4781

when it stood at -7.5.

The future outlook for surveyed companies is also improved. Sixty percent of the 86 area firms that responded to this quarter's survey expect conditions to improve six months from now, while 15 percent expect a decline in future business activity. Last year at this time, only 45 percent of area firms expected improved conditions. The outlook for employment and national business activity is also substantially improved from one year ago. Pricing pressures continue to be contained, as only 17 percent of surveyed firms expect to increase prices over the next six months and 14 percent expect to reduce prices.

In special questions, 53 percent of surveyed firms indicate an increase in costs associated with compliance requirements and regulatory burden. No firms report that these costs have decreased.

In a separate special question, 19 percent of firms expect the new health care overhaul law to substantially reduce their long-term profitability. Twenty-seven percent of firms expect a slight reduction in long-term profitability from the measure. It should be noted that 9 percent of firms expect a substantial increase in long-run profitability resulting from the health care overhaul.

Finally, area firms were asked to discuss the extent to which they have made structural adjustments in the most recent recession. Many firms report this recession has been different from those experienced in the past — and that many efficiency measures implemented during the recession will remain in place permanently.

Current Activity

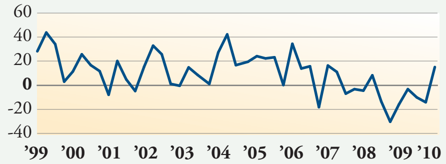
Tables 1 and 2 report the most recent results of the business outlook survey. Responses are from 86 area businesses that returned the recent mailing in time to be included in the report. Participating firms are representative of the diverse collection of St. Cloud-area companies. They include retail, manufacturing, construction, financial, health services and government enterprises small and large. Survey responses are strictly confidential. Written and oral comments have not been attributed to individual firms.

In the past six months, we have reported increasing optimism that recovery was on its way. We have also noted the survey was ahead of the data in indicating near-term recovery. This quarter's survey continues to demonstrate improvement in area economic conditions, and we now have enough confirmation from other data to be reasonably confident in declaring the end of the local recession. To be sure, this remains a slow and uneven recovery, and some indicators are not yet confirming the end of the recession. But there is sufficient evidence in the survey to believe growth will continue in coming quarters.

Survey responses from Table 1 are much improved from the same time last year. All eight survey items measuring current economic performance are considerably better than one year ago. The diffusion index — representing the percentage of respondents indicating an increase minus the percentage indicating a decrease in any given quarter — on current activity is 32.6. That's much higher than its 9.6 value one year ago.

CURRENT EMPLOYMENT

Diffusion index, percent



Consistent with the employment and unemployment data presented elsewhere in this report, area labor market conditions are greatly improved from a year ago. For example, the index on employment stands at 16, whereas one year ago it was -17. In addition, the length of workweek index stood at -6.4 in May 2009. It is now 11.6. Employee compensation is also slowly improving. Last year at this time, more firms were cutting back on employee compensation than were increasing it. Fifteen percent of surveyed firms now report increased worker compensation, and only 5 percent are

TABLE 1-CURRENT BUSINESS CONDITIONS

	May 2010 vs. Three months ago				February 2010
	Decrease (%)	No Change (%)	Increase (%)	Diffusion Index[3]	Diffusion Index[3]
What is your evaluation of:					
Level of business activity for your company	20.9	25.6	53.5	32.6	-1.2
Number of employees on your company's payroll	12.8	58.1	29.1	16.3	-15.5
Length of the workweek for your employees	10.5	66.3	22.1	11.6	-20.3
Capital expenditures (equipment, machinery, structures, etc.) by your company	7.0	75.6	16.3	9.3	7.2
Employee compensation (wages and benefits) by your company	4.7	80.2	15.1	10.4	11.9
Prices received for your company's products	16.3	65.1	17.4	1.1	-9.5
National business activity	7.0	47.7	34.9	27.9	2.4
Your company's difficulty attracting qualified workers	10.5	81.4	4.7	-5.8	-10.0

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.

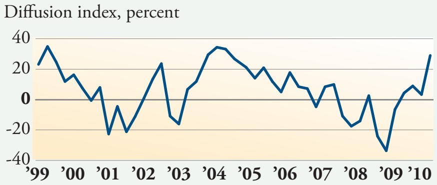
Source: St. Cloud State University Center for Economic Education, Social Science Research Institute and Department of Economics decreasing wages. These numbers remain far below what is expected for this time of year, but they are further evidence of a rebound in the area labor market. Finally, the index on difficulty attracting qualified workers is much higher than its -23.7 value last year. It is, however, still negative at -5.8 — a reminder that it will be some time before the labor market returns to normal.

The prices received index remains flat. However, one year ago it stood at -21.5 when nearly one-third of surveyed businesses reported decreasing prices received. In addition, the index on capital expenditures indicates strengthening local activity. The capital expenditures index of 9.3 is much higher than its -12.9 value one year ago. The local recovery appears to be closely correlated with national economic improvement. Last year at this time, the national business activity index had a value of -7.5. This year it is much higher, at 27.9.

As always, firms were asked to report any factors affecting their business.

CURRENT NATIONAL BUSINESS ACTIVITY

Diffusion index, percent



These comments include:

• "We are trying to sell 25 percent of our yearly sales in one month. Cannot say NO when the opportunity comes back."

• "Currently we are performing at a higher level than the past two years."

• "Residential (construction) is getting busier. Commercial is slow and will continue to be slow for one to two years."

• "Health care reform."

• "Currently our business partner has had some (challenges) ... that have been no good for public relations. Hopefully this will go away soon."

• "Everybody wants to (provide their own services) or 'water it down' to very short time periods. It compromises (the services) employees are receiving."

• "Rising cost of fuel."

• "Uncertainty over full impact of health reform legislation and loss/reduction of funding for state-sponsored programs."

• "Our accounts receivable are leveling off and improving. We're seeing a slight increase in ag sector spending. Residential construction/housing starts continues to be weak to nonexistent."

• "We are entering our slower season in the summer, which is normal. The volcano in Iceland has (disrupted our business.)"

• "Commercial land and building owners are setting up for three-year tax appeals on real estate. Unpaid real estate tax levels will increase in 2010 and 2011."

• "The State of Minnesota is sending the jobs that we used to do to be done by a lab in Kentucky."

• "Continuing real estate slump has caused longer-term changes."

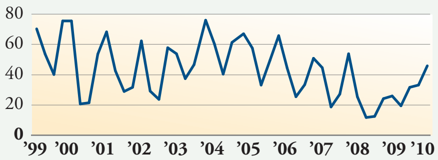
Future Outlook

Table 2 reports the future outlook for area businesses. With the exception of the index numbers for length of workweek, the survey numbers found in Table 2 are improved from one year ago.

As we have noted in prior issues of the QBR, it is not a surprise firms plan to reduce the length of the workweek in coming months. It is normal for firms to expand hiring and reduce work hours for existing employees when they are convinced a recovery is sustainable.

FUTURE BUSINESS ACTIVITY

Diffusion index, percent



The future business activity index is 44.9, which is much higher than its 24.8 value a year ago. Indeed, this is the highest May reading of the future business activity index since 2005 — a time when local

TABLE 2-FUTURE BUSINESS CONDITIONS

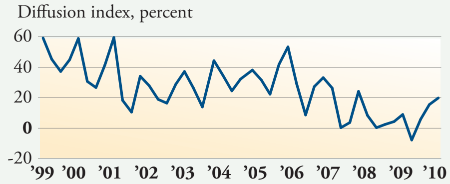
	Six months from now vs. May 2010				February 2010
	Decrease (%)	No Change (%)	Increase (%)	Diffusion Index[3]	Diffusion Index[3]
What is your evaluation of:					
Level of business activity for your company	15.1	25.6	60.0	44.9	32.1
Number of employees on your company's payroll	9.3	58.1	27.9	18.6	14.3
Length of the workweek for your employees	12.8	62.8	20.9	8.1	11.9
Capital expenditures (equipment, machinery, structures, etc.) by your company	5.8	68.6	20.9	15.1	17.8
Employee compensation (wages and benefits) by your company	2.3	70.9	24.4	22.1	13.1
Prices received for your company's products	14.0	65.1	17.4	3.4	8.3
National business activity	8.1	43.0	34.9	26.8	18.8
Your company's difficulty attracting qualified workers	4.7	81.4	8.1	3.4	2.3

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: St. Cloud State University Center for Economic Education, Social Science Research Institute and Department of Economics activity was approaching its most rapid growth phase. The total employment index is also higher than one year ago. The biggest difference between then and now is 28 percent of firms expect to increase hiring in the next six months. One year ago, only 19 percent were planning to expand employment. One reason firms are able to increase new hires is wage pressures remain low. With a value of 22.1, the index on employee compensation is only slightly higher than its 19.8 value one year ago. As we have noted before, this recession has had the characteristic of holding down wage growth (and in many cases actually reducing employee compensation). Many firms report in Special Question 3 below that this recession has caused them to trim labor costs in all kinds of creative ways.

FUTURE EMPLOYMENT

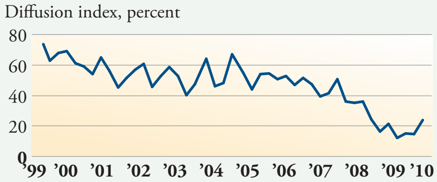
Diffusion index, percent



While firms are hesitant to increase capital spending, fewer of them say they are cutting back on these expenditures. Sixty-nine percent of firms expect no change on purchases of equipment, machinery and structures in the next six months. Of course, one form of capital spending is on commercial construction, and firms have repeatedly reminded us of the ongoing weakness in that sector. Firms also see little opportunity to increase prices in the next six months. The index on prices received is little changed from one year ago and is actually lower than last quarter's survey. Finally, expected improvements in national business activity are helping drive the improved outlook of local firms. While recent weeks have seen a return to financial market volatility and some uncertainties about economic performance in Europe, our firms appear to think this will not slow the pace of the national economy. With a value of 26.8, the index for this item is the highest it has been since February 2005.

FUTURE EMPLOYEE COMPENSATION

Diffusion index, percent

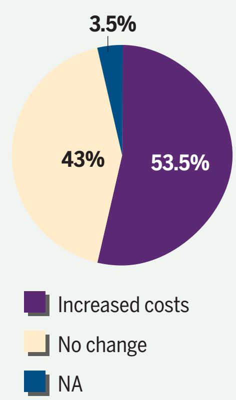


Special Questions

We have heard concerns about the expansion of compliance requirements and the regulatory burden faced by local firms; these concerns appear to relate to regulations found at all levels of government. There are, of course, some highly visible national legislative items that appear to expand to the set of compliance requirements faced by many area firms. For example, the health care overhaul and the current debate on a new set of financial regulations are two sweeping initiatives coming out of Washington. Government regulation presumably seeks to provide benefits society values. These regulations, however, can be costly. Economists often model the effects of regulation in the same way we treat adverse supply shocks — everything else equal, they tend to reduce output and increase prices (both of which are unfavorable for an economy). With that noted, we thought we would give area firms a chance to tell us if these regulatory costs were increasing, decreasing or unchanged.

QUESTION 1

To what extent is your company experiencing a change in costs associated with compliance requirements and regulatory burden from local, state and/or federal governments?



Fifty-four percent of the 86 responding firms reported an increase in costs from compliance and regulations. Forty-three percent indicated no change in these costs. No firms reported these costs have decreased. It would appear that one way to improve the long-run performance of the local economy would be to re-evaluate the regulatory burden faced by businesses.

Written comments include:

- "EPA has come out with new lead-safe work practices and testing."
- "DOT compliance."
- "Wind load requirements. Lead abatement requirements on replacements."
- "These increased costs come out of our pocket. There is no way to pass these costs on to our customers right now."
- "Regulation always has a cost attached to it. Sometimes that cost is worth the regulation; however lawmakers and regulators rarely see all impacts regulation has. There seems to be a lot of regulation that has no science behind it."
- "Medical imaging regulations continue to increase, however, do not see any benefit other than more work for staff."
- "Will not hire some needed staff until Washington quits trying to regulate every way a business operates before the 2010 elections."
- "More regulations — more forms to complete and more legal worries."
- "Increased mandates and assessments and fees are impacting our costs of doing business."
- "New lead paint rules increase license costs, more city fees."
- "More paperwork — costs and time to process applications."
- "EPA — Federal license, equipment, procedure costs. All construction license and permit fees."
- "Ridiculous building permit fees from City of St. Cloud. Also, new elevator fee from state for no reason. $100 fee per elevator per year. $500 per year just for our location. This is unnecessary. Also had to spend thousands for fire code and want us to sprinkle an outside trash bin area for over $25,000. This is a cement area. I agree with Mayor (Dave) Kleis — need to reduce police and fire wasteful spending. How many full-time firefighters? Get the fire marshals something to do besides hanging around inspecting — too many full-time people with nothing to do but harass."
- "Trustwave security compliance. Property taxes. Health insurance increases."
- "Compliance costs have and will continue to increase in our industry."
- "Can't quantify it, but any time the government regulates it 'always' costs money! It's as sure as death."
- "Our industry is seeing significant cost both now and additional cost proposed in both state and federal legislation sessions."
- "Radon compliance ... increases the price

of housing $1,500-$2,000 per house (average of 1,200-1,400-square-foot house.)

• “New RESPA changes dictated changes to software, advertising, computer programming, training, seminars.”

• “Federal — big time costs.”

• “OSHA has stepped it up!”

• “Additional stormwater run-off requirement by MN PCA.”

• “More regulation requires more work hours to complete and comply. Federal ‘simplification’ went from one page to four pages.”

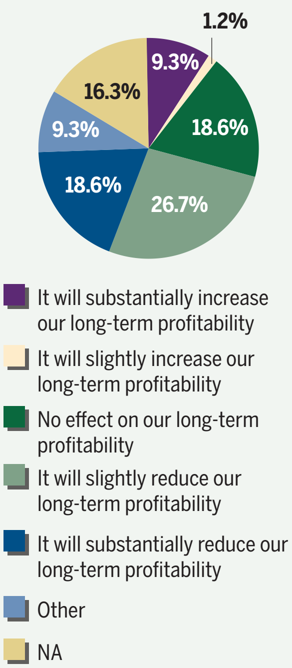
• “Increased oversight by banking regulators and cost of FDIC insurance.”

• “Compliance has become a larger and larger burden that we have had to deal with.”

Over the years, we have probably asked more questions about health care topics than any other special item in the survey. Recent months have seen the passage of landmark federal legislation that will mandate many businesses to provide health care for their employees in the future. A detailed discussion of the new health care law will have to wait until another issue of the Quarterly Business Report. For now, we simply wanted to know about the extent to which area firms were concerned that the health care law will affect their long-term profitability. We asked:

QUESTION 2

How do you expect the recently enacted health care reform law will impact the long-term profitability of your company?



Twenty-seven percent of firms think this will slightly reduce their long-term profitability, and 19 percent expect a substantial reduction in profitability. Nine percent of firms think it will substantially increase long-run profitability (presumably by unburdening firms from what they perceive to be unsustainable current health care costs). Nineteen percent of firms expect no effect on their profitability.

What is most notable about firms’ response to this question is in their written responses. Numerous firms report that they don’t know enough about the new law to make any reasoned judgments about how this will affect their company. Nearly one-quarter of the firms we surveyed indicated they were unsure of the effect this will have — many of these firms don’t understand the law. One firm made a wise suggestion — perhaps there is a market opportunity for someone to organize local informational sessions on what the new law will mean for local companies.

Written comments include:

• “Still do not know what total effect will be. We already provide extensive health insurance coverage for employees.”

• “I can’t see how increased cost will increase profitability.”

• “More employees to insure will cost more for insurance.”

• “As a smaller business, we’ll need to make decisions in the long run of how this affects other employee benefits.”

• “Increased taxes will affect profitability. These costs will be shared by employees.”

• “Instead of taking a focused look at where cuts are needed, they implement global cuts which hurt those that actually save health care dollars by being less expensive options in the first place. Poor management of system.”

• “It will not allow us to hire one or two additional workers. It’s a job killer.”

• “As of today, I don’t believe there will be an impact.”

• “No longer able to provide (health care) to my employees.”

• “Unknown. Seems likely that as written it would reduce profits from health care operations and as an employer offering health coverage. However, we expect substantial change will be forthcoming.”

• “Businesses don’t pay health care or taxes. Customers do. The health bill, although I dislike it, will level the playing field. It would have been a good bill if it would have reduced overall health care costs by limiting excessive procedures or rationing care based on variable premium rates.”

• “Long term I expect government price controls to shift costs on to employers still offering this benefit.”

• “Will not be able to pay for health care costs or need to control costs not add government as a provider. Just adds costs when government gets involved.”

• “We’re all in similar situation — price will go up to cover any new costs we incur.”

• “There is not a soul alive that knows how this is going to affect anything down the road.”

• “Since I don’t really know what is in this bill, I can’t assess profit impact. I do believe taxes must be increased to pay for this huge entitlement plan. Ridiculous legislation!”

• “We believe it is too early to tell, but the impact on a small business does not look favorable.”

• “Income taxes will be increased to cover illegal immigrants in this country and the federal government is completely out of touch with business and the illegal immigrant population.”

• “We feel when business improves, health care costs will take a portion of potential profits.”

• “For small businesses, this is disastrous legislation. We couldn’t afford health insurance before and now we are forced to provide it, at increased costs (per the health care industry itself), or pay fines. Where is the freedom to run a business any longer? Now we face government mandates to the point where you sacrifice employees to pay the expense.”

• “Government mandates always turn out bad (and costly)!”

• “Government will be paying to cover the gap in coverage, then being it is government by the people, people will cover the shortages.”

• “We are just beginning to determine the impact. Largest impact may come from adding coverage for children up to age 26.”

• “We do currently have a health insurance program. I’m not sure what, if any, change will need to be made.”

• “It is our feeling that the health care will cause individuals and businesses to ‘pick up the tab.’ We expect our business to be impacted negatively.”

The Great Recession is now over — but it felt different from the past couple of recessions. The numbers seem to bear this out; this appears to have been the weakest period of local economic performance since the Great Depression. We have heard many comments from area business leaders of the extraordinary measures they have taken in the past couple of years. It has seemed to us that a silver lining of this recession has been the new business practices it engendered locally. This recession has forced area companies to become leaner and more competitive — and it appears to have helped them find efficiency gains that will permanently benefit them. We asked the following open-ended question:

QUESTION 3

During the recent recession, in what ways, if at all, has your company made structural adjustments in the way you do business that you expect will remain in place well after the recession has ended? Has your company's response to this recession been markedly different from prior recessions?

The response to this question was extraordinary. Sixty-seven companies took the time to write comments on this item. This is undoubtedly the most written responses we have received on a special question in the more than 11 years of writing the QBR. There is little we can add to this rich set of comments.

They include:

- "Continue to work on improving productivity. Our response has not been different."
- "We have had to decrease our expenditures on equipment. We now work to maintain equipment for longer use."
- "Reduced administrative staff that will remain in place."
- "Yes, different from prior recessions. We look for value in purchasing all supplies and office equipment."
- "More focused on efficiency and productivity. Invested heavily in technology to minimize labor."
- "After the downturn in the economy in 2009, we reduced our staffing levels and have maintained that level. We've hired a contingent/temporary work force for our busiest time of the year."
- "We have streamlined hiring of temp. workers so we can react to opportunities. No, we are a job shop so each event has specific needs we need to meet."
- "We adjusted our expenses in payroll, promotional marketing capital, and increased pressure to increase individual productivity."
- "Reduced expenses and limited bad debt."
- "We'll remain cost conscious — anywhere from garbage pick-up to capital expenditures. Also, we've become better cross sellers to our other divisions."
- "We remodeled our store front and sales floor to attract homeowners directly."
- "It's unknown how much of cuts will be long lasting. We have taken more aggressive cost-cutting measures compared to past recessions."
- "Lasted much longer than expected, could not ride it out without changes. Much smaller projects with short deadlines and no projects lined up when the last is finished requires a smaller more nimble/flexible and more independently capable staff."
- "Wages and benefits have been cut and will not be restored until we know the economy is on the upswing."
- "More work has been outsourced. Not sure if that will last long term."
- "No structural adjustments. Just continually finding ways to be more efficient."
- "Find new customers. Looking for low-priced product, mostly of lesser value."
- "Monitor accounts receivable more closely."
- "Reduced staff, increased use of technology, eliminated marginal services that had little customer value yet high effort to fulfill.

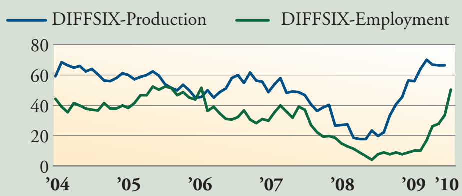
AT LAST, GOOD NEWS IN MANUFACTURING

In the past decade, St. Cloud manufacturing employment receded from 20 percent of the area work force in early 2000 to 14.8 percent in April 2010. This mirrored the national economy but was more pronounced here than elsewhere. The manufacturing base took several hits in the last recession as well, with several local plants consolidating in other parts of the U.S. or elsewhere in the world.

Almost no individual industry in the manufacturing sector was spared. As the data on diffusion of employment and production in manufacturing (right) show, in the U.S. in the worst parts of the recession in early 2009, five of six manufacturing industries were cutting production. More than 90 percent of them were cutting workers at this time.‡

DIFFUSION OF PRODUCTION AND EMPLOYMENT

Manufacturing sector, U.S.



As the recession wound down nationally in the third quarter of 2009, inventories for many parts of the economy ran at prerecession levels and manufacturing picked up. As the graph shows, many sectors started to rapidly expand, but employment did not pick up immediately. There may have been some labor hoarding that happened — or, workers who did tasks other than production during the depths of the recession, but who were turned back to producing quickly as demand picked up. But six months of continual increases in demand has led to a desire to hire, and as the graph shows, the share of manufacturers adding to payrolls rose to almost 45 percent in April 2010. Expanding the diffusion index for production further would make the economic expansion quite robust.

Bringing it down to St. Cloud, we focus on three key industries: Nonferrous metals, food processing and printing. These three industries represent 86 of 330 firms in the area and 42 percent of manufacturing employment (according to 2007 U.S. Census Bureau figures.). Most mineral manufacturing such as granite is used in commercial construction, an area still in serious decline, and currently slower than 2009. The printing business still shows declines in aggregate hours worked; it is still at 88 percent of its 2007 level. Food processing, while not expanding, is resistant to cyclical swings and is still above 95 percent of its 2007 peak year. Locally, we are a little behind what is going on in manufacturing, but there is some reason for optimism in these data.

‡ In this context, a diffusion index tells you the share of 141 manufacturing industries that are expanding employment or production. This is different from how the diffusion indexes in our survey are calculated.

Much more aggressive in changing business practices."

• "Office has gone virtual. Eliminating need for physical office space."

• "Reduced advertising budget. No overtime. Would rather add staff. Better inventory control to reduce floor plan interest expenses."

• "Lessons learned during the Great Recession will not be soon forgotten. We will not even go back to many of our old ways of operating."

• "Laid off or cut back on hours for employees — will not increase or re-hire or replace. Operate lean."

• "We consistently have to look at our prices and fees. There is very little 'loyalty' left today. People are usually focused on cost and a cheaper price."

• "Do less business with banks. Fund my own business."

• "Turnover of personnel has decreased from expected levels — has caused some 'right sizing' adjustments."

• "Reduced capital expenditures. Delayed expansion project. Since reinstated. Reduced select operating expenses."

• "The recession has forced us to focus on expense reduction, both in variable expenses and personnel. We have become too lean and need to back off a bit. It's interesting that government has not tried to do the same."

• "We have looked at how we provide value to our clients. We changed processes and procedures to become more efficient. We needed to provide more value to our clients with less resources."

• "We've added technology to reduce labor costs long term. We've also had to tighten our credit collection practices."

• "Recession depth has resulted in pending reorganization, expense reduction and employee adjustments."

• "More electronic usage, more website marketing."

• "Recession and lack of business is longer and greater this time around. Maintained staff but no replacement after attrition."

• "Laid off workers."

• "Increased investment in automation to increase productivity while not adding to payroll and health care costs."

• "Uncertain if some changes will remain in place (administrative structure)."

• "Similar to previous recessions — reducing payroll."

• "Very difficult. Most people were really scared to buy anything."

• "No dramatic changes in structure or how we approach business. This recession was/is deeper and longer than in the past. We have learned a lot, and it will impact how we manage going forward."

• "What changes we made will hopefully be reversed once the economy improves."

• "We have streamlined expenses and put into place new strategies to be more efficient."

• "Not different — continue to focus on efficiency improvements."

• "Much greater attention to controlling operating costs, and personally reaching out to past and potential clients."

• "We started cleaning our own offices which we will probably continue now that we are used to it. We worked harder to analyze our phone bills, etc. and found ways to cut lines and expenses. We also look harder for errors in billings — and found way too many!"

• "Change in travel policy."

• "Wage reductions will become permanent. Similar response — work on reducing costs."

• "More competition on ... projects. Travel greater distances for business."

• "We've always been a customer come first, customer service company. Watch our inventory closely and labor force."

• "Just became more cost driven."

• "Eliminated overtime."

• "Yes, more layoffs ..."

• "The duration and the dramatic effect on the housing component has tremendously impacted all real estate-driven companies, including ours."

• "Cut costs, this recession will last longer."

• "No changes were necessary."

• "Yes, more technology, less staff, 'do it better for less.' "

• "Due to 2009 layoffs, staff increases have been calculated and measured."

• "Eliminated employees will be replaced with technology advancements. We will rehire 10 percent of what we cut."

• "We went on a diet! Cut hours, cut workers. Management is taking up part of the workload."

• "Production shifts reorganized to eliminate overtime. This will remain in effect. Salaries reduced 10 percent across the company. Plan to reinstate if and when conditions permit."

• "Repositioned business strategy to be a leader in foreclosure sales of residential houses."

• "We have decreased the number of employees and space. We will continue to function leaner after the recession."

• "Restructuring to focus on credit quality and started a corporate wider initiative to increase ROE."

• "Fewer employees. Look at all costs. Reduce benefits. Review work procedures. Technology advantages."

• "We cut hours, looked for efficiencies — will continue to keep in place."

• "Developed process that allowed us to operate with less staff."

• "We have maintained a lean inventory. We will continue to watch our levels."

• "We have relied heavily on technology to replace personnel. We have realized that this is a cost-effective way to deliver our services, and we will think first about technology and second about hiring."

Data still mixed

As seen in Table 3, the private St. Cloud economy continues to lose employees but at a much slower rate than Minneapolis-St. Paul. Overall employment numbers are currently inflated by temporary hiring of census workers; these figures will unwind toward the end of summer. The manufacturing sector continues to contract (see the box on Page 34 in this report for more), but the service sector is expanding. Anecdotal evidence suggests larger retailers in the area are hiring, and the data support this. Gains were also found in information technology and in professional and business services. Financial services employment in the area was weak, and smaller losses were found in leisure and hospitality. Health and education employment was largely flat over the period.

Household employment in St. Cloud grew strongly in the past year, though the comparisons are made to a very weak first quarter of 2009. The labor force grew by 1.8

TABLE 3 - EMPLOYMENT TRENDS

	St. Cloud (Stearns and Benton)			13-county Twin Cities area			Minnesota		
	15-year trend rate of change	April '09-April '10 rate of change	April '10 employment share	15-year trend rate of change	April '09-April '10 rate of change	April '10 employment share	15-year trend rate of change	April '09-April '10 rate of change	April '10 employment share
Total nonagricultural	1.2%	0.5%	100.0%	0.6%	-1.7%	100.0%	0.7%	-0.8%	100.0%
Total private	1.1%	-0.4%	82.4%	0.6%	-1.7%	85.6%	0.8%	-1.0%	83.8%
Goods producing	0.1%	-3.3%	18.7%	-1.6%	-6.1%	13.0%	-1.3%	-4.7%	14.2%
Construction/natural resources	1.6%	-3.3%	3.9%	-0.7%	-19.0%	2.6%	0.0%	-11.2%	3.1%
Manufacturing	-0.2%	-3.3%	14.8%	-1.8%	-2.3%	10.4%	-1.6%	-2.7%	11.1%
Service providing	1.5%	1.4%	81.3%	1.0%	-1.0%	87.0%	1.1%	-0.2%	85.8%
Trade/transportation/utilities	-0.5%	1.4%	20.6%	-0.2%	-2.8%	17.9%	0.2%	-0.2%	18.7%
Wholesale trade	0.8%	0.1%	4.4%	0.3%	-1.6%	4.7%	0.7%	-0.1%	4.8%
Retail trade	-1.3%	2.9%	12.7%	0.2%	-0.2%	10.0%	0.2%	1.7%	10.7%
Trans./warehouse/utilities	1.7%	-2.4%	3.4%	-1.6%	-11.6%	3.2%	-0.6%	-6.2%	3.2%
Information	0.1%	4.9%	1.1%	-0.6%	-2.5%	2.3%	-0.6%	-1.3%	2.1%
Financial activities	3.0%	-1.4%	4.3%	0.9%	-3.1%	7.8%	1.1%	-2.2%	6.4%
Professional & business service	3.9%	3.1%	7.6%	1.0%	2.1%	14.9%	1.3%	1.5%	11.7%
Education & health	3.0%	-0.1%	17.8%	3.3%	-0.1%	16.0%	3.3%	0.8%	17.6%
Leisure & hospitality	1.8%	-0.6%	8.6%	1.3%	-10.4%	9.3%	1.0%	-1.2%	8.8%
Other services (excluding govt.)	0.8%	-2.7%	3.7%	1.3%	-1.8%	4.4%	0.7%	-3.8%	4.2%
Government	1.6%	4.7%	17.6%	0.6%	-1.5%	14.4%	0.5%	0.3%	16.2%
Federal government	2.3%	7.2%	2.3%	0.2%	1.1%	1.3%	0.3%	1.1%	1.3%
State government	2.4%	2.7%	5.6%	0.9%	-2.1%	4.2%	0.8%	-0.3%	3.9%
Local government	1.1%	5.3%	9.7%	0.6%	-1.7%	8.8%	0.4%	0.4%	11.0%

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.

TABLE 4-OTHER ECONOMIC INDICATORS

	2009	2010	Percent change
St. Cloud MSA labor force April (Minnesota Workforce Center)	109,397	111,396	1.8%
St. Cloud MSA civilian employment # April (Minnesota Workforce Center)	100,362	103,737	3.4%
St. Cloud MSA unemployment rate* April (Minnesota Workforce Center)	8.3%	6.9%	NA
Minnesota unemployment rate* April (Minnesota Workforce Center)	8.3%	7.0%	NA
Minneapolis-St. Paul unemployment rate* April (Minnesota Workforce Center)	7.9%	6.8%	NA
St. Cloud-area new unemployment insurance claims February-April average (Minnesota Workforce Center)	2,071.0	1,360.0	-34.3%
St. Cloud Times help-wanted ad linage February-April average	1,287	1,733	34.7%
St. Cloud MSA residential building permit valuation In thousands, February-April average (U.S. Department of Commerce)	2,670.3	4,024.7	50.7%
St. Cloud index of leading economic indicators April (St. Cloud State University)**	92.1	94.1	2.1%

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

**- October 2001=100

NA - Not applicable

percent in the 12 months to April 2010, but employment grew by 3.4 percent. The differences in Tables 3 and 4 are that Table 3 reflects the employment reported by firms in the St. Cloud area, while the employment in Table 4 is an estimate of employment of workers living in St. Cloud households. Thus self-employment will be reported in Table 4 but not Table 3. We looked at data on assumed names and limited liability partnerships in the area to get additional information on new business formation but saw very little to indicate expansion there.

The decline in unemployment in St. Cloud mirrors what is happening elsewhere in the state. Local area new unemployment insurance claims fell by more than one-third, and help-wanted advertising rose by about the same amount. The value of building permits taken out in February through April 2010 is more than 50 percent larger than those taken out in the same period in 2009. Again, these comparisons are to the worst of the recession of 2008-09, but it nevertheless shows the worst parts of the recession appear behind us.

The gains to the St. Cloud Index of Leading Economic Indicators (LEI) in the previous quarter that we discussed in March were in part inflated by some large gains to help-wanted advertising. We expected this to subside and that a short decrease in LEI would occur this period. As seen in Table 5, the decrease in help-wanted advertising was the primary factor that drove LEI down in the last quarter. We would be quick to add that it is still up more than 2 percent over the past 12 months (see Table 4). Two of the four indicators are up, but the decrease in new business incorporations has played a significant role in the decrease of LEI in the past quarter. New business formation more generally (including individuals operating sole proprietorships under assumed names and partnerships forming as LLCs) has not risen as would be expected in an economic recovery. There are of course many possible reasons for this, but one could be the more difficult regulatory environment.

Undoubtedly LEI marked a bottom in September 2009 and currently stands 4 percent above that low. We would normally expect the recession to end four to six months after that date, which would put the end of the recession between December 2009 and February 2010. Our Probability of Recession Index (PRI), on the other hand, is still showing a 55 percent chance that the economy will be in recession in August. This is despite a fairly strong, expansionary indicator for the Minnesota economy from the Creighton University survey of Mid-American States. All seven components of its indicator turned positive by April 2010. It would not surprise us to see this indicator turn to expansion within the next month or two, but for now we must caution against too much optimism from this report.

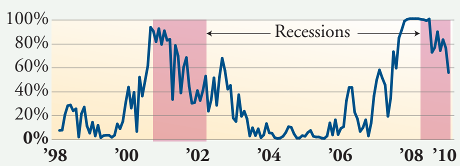
TABLE 5-ELEMENTS OF ST. CLOUD INDEX OF LEI

Changes from April to February 2010	Contribution to LEI
Help-wanted advertising in St. Cloud Times	-2.23%
Hours worked	0.02%
New business incorporations	-1.78%
New claims for unemployment insurance	0.21%
Total	-3.78%

To convince you (and us) that we should follow the more optimistic indicators rather than this last one, let's step back and look at the big picture for St. Cloud. We now have seven consecutive months of employment above the September 2009 trough when corrected for seasonality. On a seasonally adjusted basis, employment is 1,890 above that low, just less than 2 percent. This is a fairly robust growth rate, much faster than what has been the norm for the past decade.

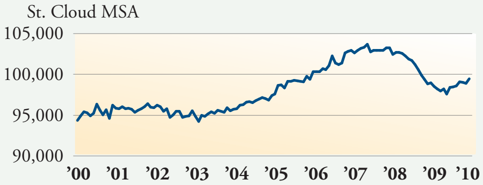
PROBABILITY OF A RECESSION

Four-six months ahead



SEASONALLY ADJUSTED EMPLOYMENT

St. Cloud MSA



A fast-growth rate after a fairly steep decline — referred to by many as a "V-shaped" recovery — is a real possibility for St. Cloud at this time. It is hard not to look past the statistical measures such as LEI and PRI and focus instead on that possibility.

IN THE NEXT QBR Participating businesses can look for the next survey in August and the St. Cloud Area Quarterly Business Report in the Oct.-Dec. 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.