Summer 2010

St. Cloud Area Quarterly Business Report, Vol. 12, No. 3

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 3 • SUMMER 2010

SLOW, UNEVEN RECOVERY CONTINUES

LOCAL CONDITIONS REMAIN WEAKER THAN NORMAL

Executive Summary

Uneven growth in the local economy continues as the area slowly recovers from recession. Within the private sector, some pockets of the area economy are experiencing improved conditions leading to a cautious expansion in economic activity.

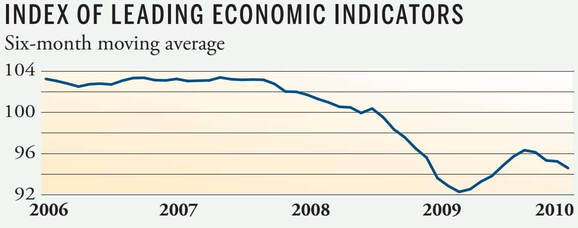
Total private employment increased at a 0.5 percent rate over the 12 months ending July 2010. This is a marked improvement over last quarter's report, when year-over-year area private employment declined by 0.4 percent. Still, area private employment growth remains well below its long-term average of 1.1 percent. It is also clear that some sectors of the local economy are performing better than others. For example, the goods-producing sectors of manufacturing and construction continue to shed workers, while retail and wholesale trade, professional and business services, education and health, and leisure and hospitality sectors are adding employees. In all, six of the 11 sectors of the private economy that we include in the report experienced job gains, while the other five indicated job loss. Over the same period last year, private employment declined by 3 percent and nine of 11 sectors were shedding jobs.

Government employment continues to rise locally. The public sector added jobs at a 3.8 percent rate over the year ending July 2010 — with large increases in state and federal employment. Local government employment declined by 1.1 percent over this period. Government employment is likely to make a smaller overall contribution to area employment in coming quarters as the federal stimulus program winds down, so continued recovery of the private sector is more important than ever.

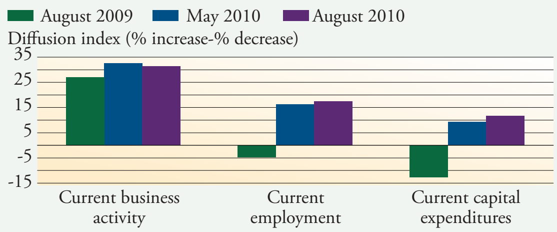
The four components of the St. Cloud Index of Leading Economic Indicators were split with two up and two down. Overall the index rose in the past quarter. But our probability of recession index rose to a reading of 87 percent (meaning there is an 87 percent chance of being in recession in the next four to six months.) This measure is adding uncertainty to our outlook.

Only 14 percent of surveyed firms report a decrease in economic activity in the past three months. One year ago, the corresponding number was 18 percent. Employment conditions are markedly improved from one year ago. In August 2009, the employment index was -4.6. This index increased to 17.4 in this year's summer survey. These conditions — while still below what would normally be expected in August — reinforce some of the other labor market measures found elsewhere in this report (such as increased help wanted linage, reduced unemployment, falling initial jobless claims, etc.). Capital expenditures continue to slowly tick upward, and there appears to be little

INDEX OF LEADING ECONOMIC INDICATORS



KEY RESULTS OF SURVEY



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
Director,
Center for Economic Education
320-308-4797

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

inflationary pressure coming from prices received or wages paid by area firms.

The outlook for surveyed companies is improved from one year ago. Forty-four percent of the 86 area firms that responded to this quarter's survey expect conditions to improve six months from now, while 19 percent expect a decline in future business activity. Last year at this time, only 39 percent of area firms expected improved conditions and 21 percent expected decreased activity. It should be noted that many firms expect declining future activity as a normal seasonal pattern. With that noted, the labor market outlook remains cloudy. On balance, area workers can expect to experience reduced work hours and only a modest increase in compensation in the first part of 2011. Firms do expect a modest increase in difficulty attracting qualified workers.

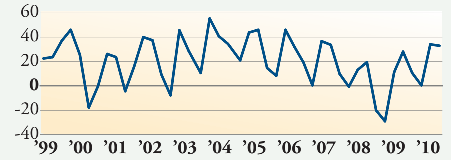
In special questions, 24 percent of surveyed firms believe current local conditions are much weaker than normal. Thirty-six percent of firms believe these conditions are mildly weaker than normal. These numbers compare unfavorably to the same question asked in May 2007. Economic uncertainty accounts for much of the concern of area firms. Fifty-five percent of firms indicate that there is more uncertainty than normal regarding the performance of the local economy. In May 2007, 50 percent of survey respondents thought there was more uncertainty than normal.

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 businesses in the St. Cloud area. 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.

Survey responses from Table 1 continue to highlight improvements in current conditions that are below normal but markedly better than one year ago. For example, last year's August survey of current business conditions found five survey items with a negative diffusion index. In this quarter's survey, only one item has a negative value. Note, however, that with a value of -4.7, the current prices received item is measurably improved from a -17.2 reading one year ago. A diffusion index represents the percentage of respondents indicating an increase minus the percentage indicating a decrease in any given quarter. For any given item, a positive index usually indicates expanding activity, while a negative index implies declining conditions.

CURRENT BUSINESS ACTIVITY



Consistent with local labor market data presented elsewhere in this report, area employment conditions are greatly improved from a year ago. For example, the index on employment stands at 17, whereas one year ago it was -5. In addition, the length of workweek index stood at -1.1 in August 2009. It is now 12.8. Employee compensation is also slowly improving. Last year at this time, the same number of firms cut back on employee compensation as were increasing it (and 79 percent of firms reported no change in wages and salaries). Nineteen percent of surveyed firms now report increased worker compensation and only 6 percent are decreasing wages (76 percent of firms still report no change in employee compensation). As reported last quarter, these numbers remain far below what is expected for this time of year, but they are further evidence of a slowly improving area labor market.

Finally, the index on difficulty

TABLE 1-CURRENT BUSINESS CONDITIONS

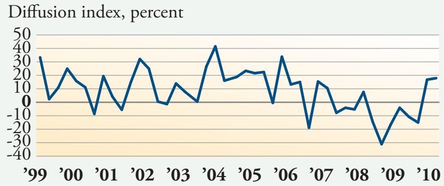
	August 2010 vs. Three months ago				May 2010
	Decrease (%)	No Change (%)	Increase (%)	Diffusion Index[3]	Diffusion Index[3]
What is your evaluation of:					
Level of business activity for your company	14.0	40.7	45.3	31.3	32.6
Number of employees on your company's payroll	12.8	57.0	30.2	17.4	16.3
Length of the workweek for your employees	8.1	70.9	20.9	12.8	11.6
Capital expenditures (equipment, machinery, structures, etc.) by your company	8.1	70.9	19.8	11.7	9.3
Employee compensation (wages and benefits) by your company	5.8	75.6	18.6	12.8	10.4
Prices received for your company's products	19.8	64.0	15.1	-4.7	1.1
National business activity	14.0	45.3	30.2	16.2	27.9
Your company's difficulty attracting qualified workers	4.7	82.6	9.3	4.6	-5.8

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: St. Cloud State University Center for Economic Education, Social Science Research Institute and Department of Economics attracting qualified workers continues to slowly improve. It has turned positive for the first time since the local recession began in August 2008. As we have noted in previous editions of the St. Cloud Area Quarterly Business Report, this series seems to track the path of the local economy fairly closely as a coincident indicator of economic performance.

CURRENT EMPLOYMENT

Diffusion index, percent



The index on capital expenditures indicates slowly strengthening local activity. The capital expenditures index of 11.7 is much higher than its -12.6 value one year ago. The national business activity item in Table 1 also shows improvement over last year, although its decline from last quarter is worth watching.

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

These comments include:

• "Concern that we can effectively negotiate our health benefit package without reducing coverage or increasing cost for employees and company."

• "Please don't let anybody fool you. This recession is NOT over, either locally or nationally. I suspect we have at least one more year."

• "Have a pending lease renewal — if (they) vacate instead of renewing, (it) will have a major impact."

• "We are seeing very little privately funded projects to bid on. All of our current work is either work in progress or publicly funded projects."

• "Raw materials prices have caused wholesale prices to rise, even in this time of lower demand."

• "I'm very concerned about the economy. I work extremely hard to keep our center full and staff employed."

• "Storm damage has created increased activity, however, it is too early to tell if this activity will create profitable results."

• "State of Minnesota awarded bid to a company in Kentucky for jobs we used to do."

• "I feel people are losing confidence in the government and its role in bailing us out of this economic mess. The positive I am beginning to see is that people themselves are seeing that they need to take action in their own lives (save more, cut to basics needed, tighten up to save the day). The government has spent us into oblivion. There's no help for small businesses."

• "Value of real estate needs to come back up before anything can happen in our industry."

• "Cautious optimism is what I hear from my clients."

• "The end of the home buyer tax credit has made the summer selling season considerably slower than usual. We are anticipating conditions to be normal this fall."

• "Uncertain about health care bill and its effect on our business."

• "July was slow."

• "We are a seasonal business. We are experiencing strong growth in most sectors."

• "I believe we're in for or already are in double dip recession. I haven't spoken with a business associate who's busy this summer."

• "Business remains steady, but still see apprehension of hiring full-time workers."

• "Commercial business is down 20 percent."

• "I hope that as we move toward 2011, the economy would turn around with more jobs and less depressing economic developments."

Future Outlook

Table 2 reports the future outlook for area businesses. It is a normal seasonal pattern for the index numbers on overall activity, employment and length of workweek to be weaker than three months earlier. This

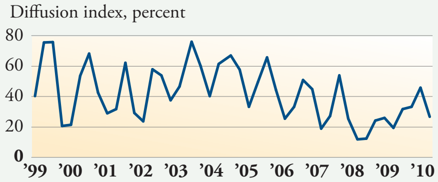
TABLE 2-FUTURE BUSINESS CONDITIONS

	Six months from now vs. August 2010				
	Decrease (%)	No Change (%)	Increase (%)	Diffusion Index[3]	May 2010 Diffusion Index[3]
What is your evaluation of:					
Level of business activity for your company	18.6	34.9	44.2	25.6	44.9
Number of employees on your company's payroll	19.8	58.1	18.6	-1.2	18.6
Length of the workweek for your employees	19.8	67.4	10.5	-9.3	8.1
Capital expenditures (equipment, machinery, structures, etc.) by your company	8.1	65.1	23.3	15.2	15.1
Employee compensation (wages and benefits) by your company	2.3	73.3	22.1	19.8	22.1
Prices received for your company's products	15.1	62.8	17.4	2.3	3.4
National business activity	7.0	52.3	27.9	20.9	26.8
Your company's difficulty attracting qualified workers	5.8	74.4	12.8	7.0	3.4

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 seasonal pattern is confirmed by Table 2. It is worth noting the indexes for business activity and employment are improved from the survey of last August. Indeed, with a value of 25.6, the future business activity index is the highest summer reading since the August 2005 survey. As can be seen from the accompanying chart, the future business activity index seems to be slowly trending upward after reaching its historical low point in August 2008. There has been abundant national discussion about a recovery that is losing steam — so far, this has not been seen in the local survey data, although we have not yet returned to normal growth.

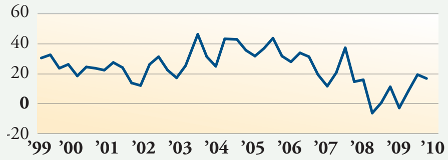
FUTURE BUSINESS ACTIVITY
Diffusion index, percent



The future capital equipment index has never followed an observable seasonal pattern, so the accompanying chart is a reminder that while planned purchases of equipment, machinery and structures have increased from their low point (experienced in November 2008, a -7.9 reading), there is a long way to go before we approach the readings of 40 and above that we experienced five years ago. Table 2 also confirms the moderating of pricing pressures and indicates only 20 percent of firms expect wage increases over the next six months. During the height of the local worker shortage of the late 1990s, the index on employee compensation was at 75.4, so labor costs seem to be stable, which is normal at this stage of the local recovery. Expected future national business activity slowed since the May survey. In a pattern that we also seem to be observing in the national media, area business leaders seem to have lost a little confidence in the future strength of the national economy. We discuss this in more detail below.

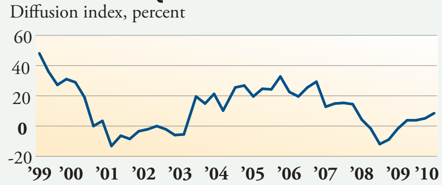
It has been a long time since area employers have had to be concerned with an area worker shortage. Well-qualified workers have been relatively easy to find for many years. To be sure, in 2005 and 2006, area

FUTURE CAPITAL EXPENDITURES
Diffusion index, percent



firms expressed modest concern about the difficulty of attracting qualified workers, but these concerns were mild compared with the late 1990s and 2000. Of course, the area still felt the hangover from the local recession of 2001-2003 (which included the structural shock of the shuttering of Fingerhut) into the mid-2000s. It seems we never quite returned to the days of persistent labor shortage experienced a decade ago. We bring this up because it turns out that the worker shortage responses have reasonably closely tracked the performance of the local economy over many years. It appears that when this index is negative, the area is in recession, and when it is positive, the area economy is growing. We realize, of course, that this may be a purely statistical artifact, but one can tell a story about labor shortages and the strength of economic performance. So we leave it to the reader to interpret the current pattern of this series. It turned positive in November 2009 and has slowly been rising since then … continued improvement in this series could be yet another indicator of local recovery.

FUTURE DIFFICULTY
ATTRACTING QUALIFIED WORKERS
Diffusion index, percent



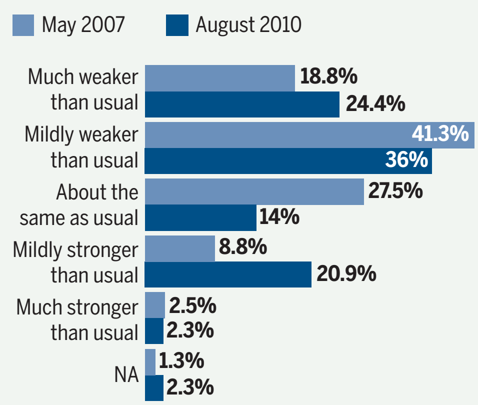
Special Questions

In the July 2007 St. Cloud Area Quarterly Business Report, we used the term "economic uncertainty abounds" to describe some of the comments we were hearing from area business leaders about the local economy. In particular, we wrote:

> For several months, there have been mixed readings on the performance of the local and national economies. While some sectors appear to be struggling, others seem to be experiencing strong growth. Survey questions typically ask area business leaders about the conditions at their own company and the national economy. But this quarter, we look into firms' perceptions of the current and future performance of the local economy.

We have been getting these same mixed readings over the past few months. While many area business leaders report that their companies are experiencing at least modest growth, there seems to be a pervasive attitude that the local economy is not doing so well. This attitude could come from many sources — personal observation, business contacts, media stories, etc. — and it could be contributing to local economic uncertainty. With this in mind we decided to ask area business leaders the exact same set of special questions that we asked in the uncertain times of the May 2007 survey. General results from this quarter's questions confirm that area business leaders do feel the area economy is (and will continue to be) weaker than normal. Results also indicate there is more economic uncertainty than normal. Compared with May 2007, these results are somewhat more pessimistic than during that earlier uncertain period. We asked:

QUESTION 1
Compared to normal economic conditions for this time of year, which of the following is your company's perception of current local conditions?



Twenty-four percent of the 86 responding firms responded "much weaker than usual" and 36 percent indicated "mildly weaker than usual." In May 2007, about 60 percent of firms also indicated "weaker than usual," but there is a larger share of this quarter's respondents who answered "much weaker." Perhaps the biggest difference between the two earlier periods is that 23 percent of firms currently perceive local conditions that are either "mildly stronger" or "much stronger" than normal. The corresponding percentage in May 2007 was only 11 percent. In that earlier survey, a much larger percentage of respondents indicated "about the same as usual" than was found this quarter.

Written comments include:

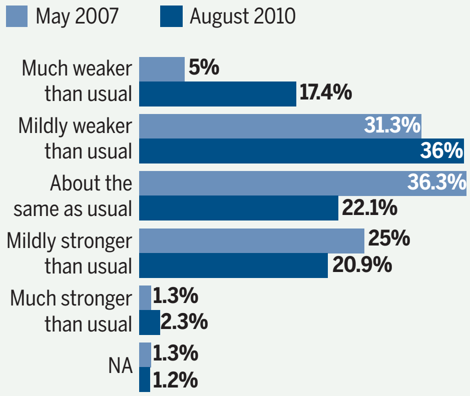
- "Government work is off."
- "City and county governments are not doing much work to improve and expand infrastructure — they don't want to spend."
- "Unusually weak. We don't know if the weakness is due to Highway 10 construction or to market factors."
- "We are a job shop and complement other corporations like ourselves. When they are slow, we see little work from them. But lately three St. Cloud firms have kept us busy."
- "Our customer base is so widespread, we don't notice local trends."
- "Seeing pockets of favorable results."
- "August 2010 will be best sales month ever."
- "Customers need way more money down now so it will take a while for them to build up savings to buy our products."
- "We have a spike in activity due to some local storms — construction related."

We also asked about firms' perception about future local conditions. We asked:

QUESTION 2

Compared to normal economic conditions expected six months from now, which of the following is your company's perception of expected future local conditions six months from now?

Seventeen percent of firms think local conditions will be "much weaker" and 36 percent expect them to be "mildly weaker" in six months' time. This is notably less optimistic than in the May 2007 survey, where only 5 percent expected "much weaker" conditions and 31 percent expected a "mildly weaker" local economy.



This is an important finding. Area firms do seem to expect weaker future conditions in the local economy and this could constrain their current decisions regarding employment, employee compensation, hours worked, capital expenditures, etc. It may well be that it is only after these expectations improve that we can expect a return to normal activity.

Written comments include:

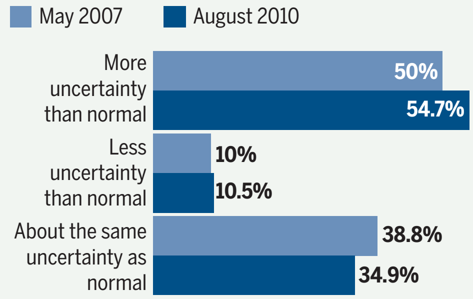
- "We expect the local economy to taper and sustain with small pockets of growth."
- "Government funded work will continue to spiral down especially depending on who wins the governors election."
- "I expect it to be at least a year before construction starts to pick up."
- "We expect a dip in sales before an extended upward swing."

Finally, firms' uncertain outlook for the local economy is one important factor that affects their economic uncertainty. Over the past few months, we have witnessed weak national jobs numbers, strong earnings reports for many large firms, a cloudy outlook for other countries, political debate over the need for another round of stimulus, etc. This all seems to be contributing to economic uncertainty that is hampering national economic growth. We asked area firms the following question:

QUESTION 3

In general, does your company feel there is currently more, less or about the same uncertainty as usually occurs regarding the performance of the local economy?

The numbers speak for themselves. Firms not only face uncertainty regarding the global, national and state outlooks, they also report more uncertainty than normal



in the local economy. Fifty-five percent of firms say there is more uncertainty than normal and only 11 percent think there is less uncertainty. These numbers represent an increase in economic uncertainty from when the same question was asked in May 2007.

Comments include:

- "With the economics of the last number of years, it is a little difficult to determine what 'normal' is for this question."
- "Obamacare and tax changes will leave much uncertainty."
- "City councils are sitting on their hands until they know what the state is going to do."
- "Elections, taxes, business environment, interpretation of regulation all create more uncertainty at this time."
- "Haven't seen enough positive signs to increase certainty!"
- "Companies are doing more with less. If fewer people are working, there is going to be slower growth."
- "We are looking to reach into other markets to pick up where there are losses."

OUTPUT, JOBS AND SALES — A LOOK AT THE DATA

Weak job growth, particularly in private sector jobs, dominates the data in Table 3. The local service sector grew jobs, led by the information, professional and business services, and leisure and hospitality sectors. Retail store employers continued to provide growth over the last year. The goods sector continues its contraction, with construction employment dropping below 5 percent of area employment. This trend is part of a national movement, and seems unlikely to turn around soon. Manufacturing employment has declined in St. Cloud, contrary to the trend in the rest of the state, but much of the decline came in the second half of 2009. There was a net gain of 700 jobs in manufacturing from January to July in the St. Cloud area.

Unemployment rates continued to recede in the area. Employment rose 1.3 percent, according to the household survey of the Bureau of Labor Statistics (versus 0.9 percent in its payroll survey). The unemployment rate fell as the area's labor force barely grew in the 12 months ending in July. Similar stories applied to Minneapolis/St. Paul and to the state, as seen in Table 4.

Area measures of the business cycle continue to show general strength, but much of this is due to easy comparisons to last July at the depths of the recession. New filings for unemployment insurance in the May-July period fell 31 percent compared with year-ago levels. Help-wanted linage in the St. Cloud Times and building permit valuations rose compared with last year, though the help-wanted figures showed weakness over the last three months.

The St. Cloud Area Index of Leading Economic Indicators was split, with positive readings for initial claims for unemployment insurance and business incorporations rising over the last quarter and help-wanted advertising and hours worked in manufacturing declining. The positives outweighed the negatives this quarter, so the index rose 1.57 percent. In general, over the past six to eight months the series has gone sideways after a substantial rise in the last four months of 2009.

However, including recent movements in the state economy (measured by the state economic indicators series produced

TABLE 4-OTHER ECONOMIC INDICATORS

	2009	2010	Percent change
St. Cloud MSA labor force July (Minnesota Workforce Center)	108,523	108,603	0.1%
St. Cloud MSA civilian employment # July (Minnesota Workforce Center)	100,006	101,313	1.3%
St. Cloud MSA unemployment rate* July (Minnesota Workforce Center)	7.8%	6.7%	NA
Minnesota unemployment rate* July (Minnesota Workforce Center)	8.0%	6.8%	NA
Minneapolis-St. Paul unemployment rate* July (Minnesota Workforce Center)	8.1%	6.8%	NA
St. Cloud-area new unemployment insurance claims May-July average (Minnesota Workforce Center)	1,471.0	1,015.0	-31.0%
St. Cloud Times help-wanted ad linage May-July average	1,281	1,514	18.2%
St. Cloud MSA residential building permit valuation In thousands, May-July average (U.S. Department of Commerce)	4,286.7	5,094.7	18.8%
St. Cloud index of leading economic indicators July (St. Cloud State University)**	91.8	93.9	2.3%

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

TABLE 3 - EMPLOYMENT TRENDS

	St. Cloud (Stearns and Benton)			13-county Twin Cities area			Minnesota		
	15-year trend rate of change	July '09-July '10 rate of change	July '10 employment share	15-year trend rate of change	July '09-July '10 rate of change	July '10 employment share	15-year trend rate of change	July '09-July '10 rate of change	July '10 employment share
Total nonagricultural	1.2%	0.9%	100.0%	0.7%	0.5%	100.0%	0.8%	1.1%	100.0%
Total private	1.1%	0.5%	84.9%	0.7%	1.0%	86.9%	0.8%	1.5%	85.5%
Goods producing	0.2%	-2.3%	20.4%	-1.5%	-2.6%	13.6%	-1.2%	-0.9%	15.1%
Construction/natural resources	1.2%	-2.9%	4.9%	-0.6%	-12.0%	3.2%	-0.1%	-6.0%	3.8%
Manufacturing	-0.1%	-2.0%	15.5%	-1.8%	0.7%	10.4%	-1.5%	1.0%	11.3%
Service providing	1.5%	1.8%	79.6%	1.1%	1.0%	86.4%	1.2%	1.5%	84.9%
Trade/transportation/utilities	-0.5%	0.7%	20.9%	-0.2%	-1.8%	17.8%	0.2%	0.5%	18.6%
Wholesale trade	0.9%	0.4%	4.6%	0.2%	-1.7%	4.6%	0.7%	1.0%	4.8%
Retail trade	-1.5%	1.5%	12.9%	0.1%	0.0%	10.0%	0.2%	1.3%	10.6%
Trans./warehouse/utilities	1.9%	-2.0%	3.4%	-1.5%	-6.9%	3.2%	-0.5%	-2.6%	3.2%
Information	-0.3%	6.6%	1.2%	-0.6%	-1.6%	2.3%	-0.6%	0.3%	2.1%
Financial activities	2.9%	-1.5%	4.4%	0.9%	-0.5%	7.9%	1.1%	-0.9%	6.4%
Professional & business service	4.0%	3.7%	7.8%	1.0%	4.6%	15.0%	1.3%	3.6%	11.8%
Education & health	3.3%	1.2%	17.2%	3.4%	2.2%	15.6%	3.5%	3.2%	17.3%
Leisure & hospitality	2.2%	3.6%	9.1%	1.8%	7.1%	10.3%	1.4%	6.0%	10.0%
Other services (excluding govt.)	0.6%	-2.3%	3.8%	1.2%	-2.2%	4.4%	0.6%	-4.0%	4.2%
Government	1.8%	3.8%	15.1%	0.7%	-2.2%	13.1%	0.5%	-1.1%	14.5%
Federal government	2.5%	9.8%	2.4%	0.3%	2.8%	1.3%	0.3%	5.8%	1.3%
State government	2.5%	12.9%	3.9%	1.1%	-1.5%	3.8%	1.1%	-1.4%	3.4%
Local government	1.4%	-1.1%	8.9%	0.6%	-3.3%	8.0%	0.3%	-1.9%	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.

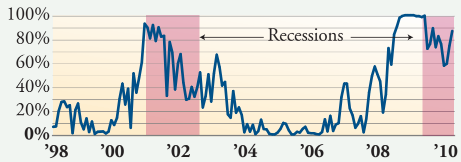
TABLE 5-ELEMENTS OF ST. CLOUD INDEX OF LEI

Changes from May to July 2010	Contribution to LEI
Help-wanted advertising in St. Cloud Times	-2.44%
Hours worked	-0.21%
New business incorporations	1.49%
New claims for unemployment insurance	2.73%
Total	1.57%

by Creighton University) in our probability-of-recession index shows an unpleasant return of high readings. At present the reading is for an 87 percent probability that the St. Cloud economy will be in recession at the end of 2010. We will need a few more months of data before this series turns in a reading below 30 percent, a point at which all our indicators would signal the end of the recession. (As we said last quarter, this one indicator has yet to declare the recession over.)

PROBABILITY OF A RECESSION

Four-six months ahead



For the time being, we believe, any additional action from national policymakers to provide some lift to the economy is on hold. The Federal Reserve's deliberations over the summer led it to reverse its first attempt at exiting its "quantitative easing policy." Respondents in the latest policy survey of the National Association of Business Economists thought monetary and fiscal policy should be pointed toward growth rather than concerns about inflation or growing fiscal deficits. Seventy-five percent opposed an additional stimulus package. The survey probably reflects thinking in Washington as well as on Wall Street.

If there's to be a rebound and another leg up in the economy in 2010, it likely will not come from government policy. It likely will not come as well from overseas. While smaller economies may grow through exports — even places like Germany, not that small, has had a nice rebound in 2010 — it remains to be seen who will buy those goods. Savings rates in the United States have returned to 6 percent, levels not seen in the previous 25 years. As households recognize the hit to their portfolios from lost house equity as well as their 401(k)s, that rate may rise. It is unclear what the effect of the recent financial overhaul legislation signed into law will have on the mortgage market. Fannie Mae and Freddie Mac will be resolved someday — when and how is still anybody's guess. When they do, the impact on local housing markets and our moribund construction industry will be affected greatly. For now, they seem just to drift along, as does the rest of the St. Cloud economy.

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.

RECESSION MAY BE OVER, BUT RISKS STILL HIGH

We were pleased with the keen discussion of our last Quarterly Business Report regarding the end of St. Cloud's recession. There was a wide range of opinion on this question. We agree there is room for doubt about whether the recession has ended.

One confounding factor is the recent development of the national business cycle. Most economists believed in early summer that the 2007-2009 national recession had ended in late summer of 2009. As we had discussed previously, there was a divergence of opinion on the shape of the recovery — would it be "V"-shaped, or "U"-shaped or even a double-dipped "W"?

There is a split in the economic data. If you focus on the goods-producing sector, your viewpoint would be rather optimistic. Even as this summer progressed, indicators of manufacturing activity have largely shown a sharp rise. Some of this was due to an extraordinary sell-off in inventories in 2009; eventually those shelves needed to be restocked with new goods. Because St. Cloud is more dependent on manufacturing than the nation or state at large, this has been and continues to be a strong indicator for economic activity. (As noted above, more manufacturing output does not necessarily translate into more manufacturing jobs.)

Other data tell a different story. Another strong indicator has been sales of goods and services, but many of the goods we have been buying lately have been imported goods. After netting out the impact of inventories and imports, national economic activity has hovered around the 1-2 percent area in the past three quarters, and there is little sign of this improving. The rest of the world economy, particularly in Europe, appears to have little appetite for American goods. As long as this continues, it is likely that the GDP figures will continue to stay in the level they were in the second quarter, around 1.5 percent growth.

Does this portend a second recession? The national leading economic indicators series suggests not. However, in a recent economic letter from the Federal Reserve Bank of San Francisco, economists Travis Berge and Oscar Jorda showed leading indicators were greatly influenced by the unusual performance of estimates of credit market tightness. Because the Federal Reserve is operating a zero Federal Funds rate policy, the indicators of credit demand may be giving a false signal of strength. When that indicator is removed and the leading indicators series re-estimated, the probability of a second recession in 2011 rises to nearly 50 percent.[1]

Our own measures of future local economic activity discussed do not contain credit market measures. Thus our measures do not necessarily contradict the national scene. And respondents to our survey have also noted some slowing of the national economy. All forecasts should include the words "barring unforeseen circumstances," and at this juncture we can see at least a greater-than-usual amount of risk of the W-shaped business cycle. Still, we are reasonably confident that the local area has fared better than the national economy, and should continue to do so.

[1] Berge and Jorda, "Future Recession Risks." Federal Reserve Bank of San Fransicso **Economic Letter,** Aug. 8, 2010, online at www.frbsf.org/publications/economics/letter/2010/el2010-24.html