

SOUTH DAKOTA



Cash for guzzlers

Maybe South Dakota never got the memo.

The federal “cash for clunkers” program offered up to \$4,500 to drivers to upgrade their vehicles to more fuel-efficient models. But according to an investigation by the *Argus Leader*, state residents there used the program as an opportunity to simply trade in their vehicle for a discounted new one, with little net gain in fuel efficiency.

The program’s two best sellers in the state were the Ford F-150 and Chevy Silverado, both of which get about 16 miles to the gallon. For 90 percent of these purchases, the average trade-in improved net gas mileage by about three miles per gallon, the newspaper found. Average gas mileage for all new vehicles sold nationwide was 24.9, compared with 23.5 in South Dakota—a 6 percent difference—mostly the result of higher truck sales.

In all, the cash for clunkers program in South Dakota snagged \$10.3 million in federal incentives for about 2,500 trade-ins, according to federal databases, or about \$4,200 per vehicle.

The sound of hammer silence

Despite the fact that the state unemployment rate, at about 5 percent, is low compared to most states, the construction sector in the state has been taking its lumps during the recession.

Associated General Contractors of America, an industry trade group, said total employment in the sector dropped by about 1,400, or about 6 percent, during the 12 months ending this past September. If accurate, that would represent more than one-fifth of the net drop in employment statewide during this period, according to state figures. Sioux Falls saw the single largest drop of any city, from about 8,500 to 8,000 construction jobs.

The good news for the state and its largest metro is that it fared much better than most. The loss rate of construction jobs in Sioux Falls, for example, was lower than in 80 percent of metros nationwide.

There also might be work around the corner for some hammers. According to a November report by Moody’s, South Dakota was one of 11 states (which also included Montana and North Dakota) emerging from the recession, based on employment rates, home prices, residential construction and manufacturing.

—Ronald A. Wirtz

Looks like another slow year

By TOBIAS MADDEN
Regional Economist

Business leaders predict very sluggish growth in the U.S. economy in 2010, according to the November *fedgazette* business outlook poll. This was evident across district states as well as across economic sectors. Leaders remain pessimistic for their own businesses and communities. Tight credit conditions are still a concern for about a third of the respondents. The overall economic outlook is somewhat better than a year ago, and modest inflation is expected.

Respondents across the Ninth District believed their local economies would contract in 2010. Sentiment regarding business investment, employment, consumer spending and housing starts all remains pessimistic. Respondents see a rebound in sales revenues and anticipate flat prices for their products. However, they anticipate slight cuts in employees and capital investment. Leaders are not very concerned about finding good people, but are very concerned with government regulation.

Sluggish national growth

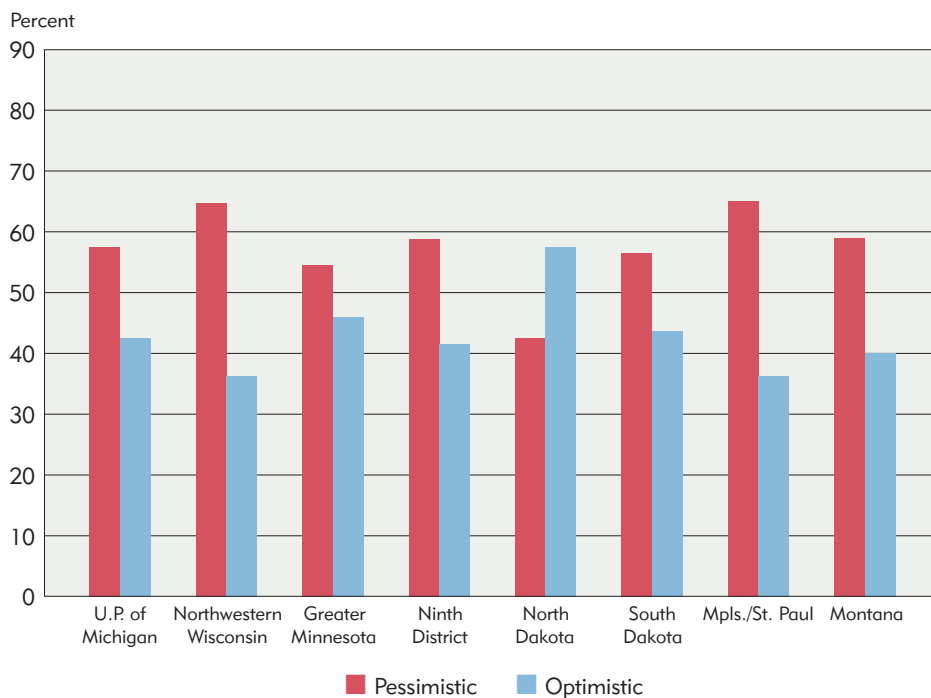
“There is going to be very slow growth,” commented a Minnesota manufacturer. About two-thirds of the respondents expect growth in U.S. GDP of 1 percent to 2 percent, and one quarter expect a recession in 2010. Responses were consistent across the district, with a slightly higher proportion of U.P. respondents expecting the recession to continue. Meanwhile, more respondents from the agriculture and construction industries expect a continued recession compared with those from the manufacturing industry. “Our general contracting business has no backlog and our real estate company has no clients,” said a U.P. construction company respondent.

Respondents believed inflation would be modest in 2010. Concerns about near-term inflation are generally muted: Nearly a quarter of respondents predicted inflation of only around 1 percent, and 42 percent about 2 percent; however, 19 percent predicted inflation of 4 percent or higher, the highest percentage of which come from Montana and northwestern Wisconsin. Several leaders indicated that they are very concerned about higher inflation hitting in a few years. “Expect CPI to have a slow change over the next 12 months, but faster than average in inflation in 24 to 36 months,” a Montana respondent said.

Pessimism

Almost 60 percent of respondents are pessimistic about their community’s economic performance in 2010 (see Chart 1). The pessimism is strongest in the Minneapolis/St. Paul area and north-

CHART 1 Overall, what is your outlook for your community’s economy in the next 12 months?



Source: Federal Reserve Bank of Minneapolis business outlook poll

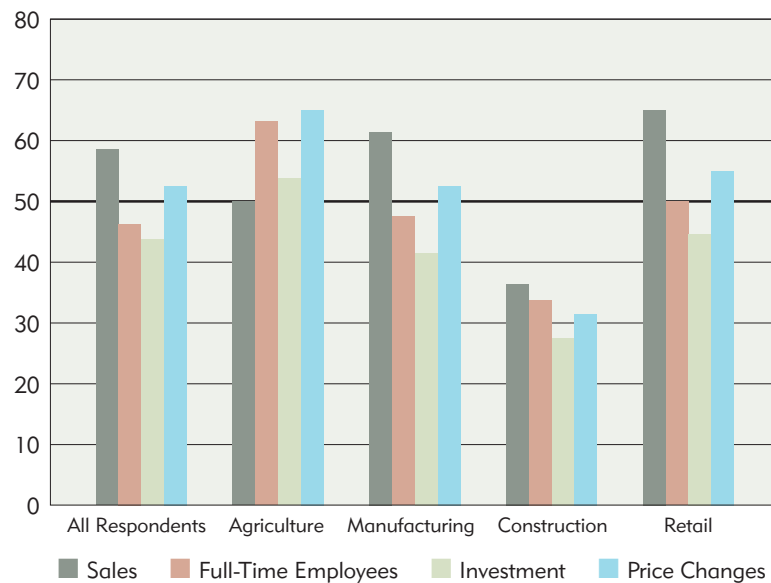
western Wisconsin. In contrast, North Dakota respondents were optimistic.

Respondents across the district and economic sectors expect large declines in employment in their community’s economy. Anticipated wage increases are very soft, as nearly two-thirds expect 0 percent to 1 percent increases in 2010. No respondents expect wages in their community to rise more than 3 percent. Meanwhile, business investment is expected to fall in 2010. “There is little incentive to invest in any new business expansion with prospects for higher taxes, more regulation and depressed demand for services,” a Minnesota respondent said.

The decrease in employment and capital investment may be affected by the consumer spending outlook. Nearly half of the respondents believe consumers will spend less in their communities. The results are similar for respondents across states and sectors.

Nearly half of respondents also predict that housing starts will decline further in 2010. “There is no sign of recovery in housing,” commented a Minnesota manufacturer that supports the housing industry. Respondents from all district states and economic sectors expect an overall decline in housing starts in 2010.

CHART 2 With regard to your own company, how do you see operations changing during the next year? (Above 50 indicates expansion; below 50 indicates contraction)



Source: Federal Reserve Bank of Minneapolis business outlook poll

Higher sales but less employment and investment

Sales revenue in 2010 is expected to increase from 2009 levels across the district except in Montana, where a sales decrease is anticipated (see Chart 2 on page 14). Meanwhile, sales gains are expected across all sectors except construction. “Forest products have been terrible for three and a half years with another year, at least, to go,” commented a Montana manufacturer that supports the construction industry.

Meanwhile, employment is projected to fall further. A quarter of the respondents expect to decrease employment in 2010, while 18 percent expect to increase jobs. Every sector and geographic area foresees decreased hiring. Most respondents reported that securing workers is not a challenge.

Access to credit may be affecting hiring and capital expenditure decisions. About a third of the respondents reported that access to bank credit has deteri-

orated over the past three months. As a result, 21 percent of respondents say it affected their hiring plans. “Businesses are struggling and, as they weaken, credit just gets tougher,” commented a Minnesota manufacturer. Another Minnesota manufacturer noted that “banks are pulling back on credit—they need to continue lending or small businesses like us will struggle and fail.” Tighter credit may be affecting capital expenditures, as nearly a third said the difficulty accessing credit has hurt planned capital expenditures. “They have added new restrictive reporting requirements and are not funding projects they would have funded in the past,” said a Minnesota agricultural producer.

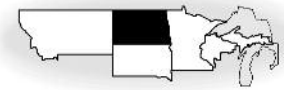
Investment in plant and equipment is expected to drop in 2010, with a third of respondents expecting decreased levels and 21 percent anticipating increased levels. The decrease is widespread across sectors and geography. Productivity was

sluggish in 2009: 44 percent of respondents reported level or decreased productivity.

Company pricing pressure is modest. A quarter of respondents expect to increase prices on their products and services, while 20 percent see price declines in 2010. Moderate price pressure is stable across district states but varies among sectors. Only 5 percent of construction firms expect to increase prices, while 40 percent expect to decrease prices. Meanwhile, 57 percent of agricultural producers expect higher prices for their products.

The biggest challenge facing businesses is complying with government regulation. Eighty-six percent of respondents reported that complying with government regulations will be a challenge in 2010. Said one Minnesota construction company, “Government regulation continues to add cost with little benefit realized.” ■

NORTH DAKOTA



Harvests good, but don't hold your breath

Things came up mostly green for North Dakota's farmers this year.

According to the U.S. Department of Agriculture, the state's soybean crop will be up 10 percent from a year ago, thanks to higher yields and an increase in harvested acres. The state is also a leader in pulse crops, which had banner years. The state's dry pea crop rose 46 percent, and the lentil harvest is expected to be more than triple the size of last year's crop because of significantly more harvested acres, which itself was driven by prices that are double those in 2006. The state's average sunflower yield is expected to approach its 2005 record.

Not everyone is having a spectacular year, however. Potato growers are facing blight for the first time in years and expect production to drop by 17 percent. The corn crop is down by one quarter, though mostly due to much lower harvested acres. The wheat harvest is only expected to match its five-year average.

State farmers also have been pioneers in getting paid for their carbon-capturing ability, but prices for so-called carbon offsets have crashed. In May 2008, carbon contracts were trading over \$7 per metric ton on the Chicago Climate Exchange. Prices dropped to about 60 cents by summer and to 15 cents in early December.

Exporting the wind

The burgeoning wind market in North Dakota is starting to find sales outlets in other states.

Recently, the Tennessee Valley Authority, which serves a seven-state region, agreed to purchase 200 megawatts of power annually from a wind farm being developed in Ashley, N.D., along with 250 megawatts from a wind farm in neighboring South Dakota.

The Western Area Power Administration has also signed a three-year deal to buy up to 50 megawatts annually from a wind farm owned by Basin Electric Power Cooperative. WAPA is a federal agency serving a 15-state region that markets hydroelectric power generated from rivers in 11 states. The agency is attempting to integrate water and wind power, and is also negotiating for 100 megawatts of wind power from an independent wind farm developer with holdings in both North Dakota and Minnesota.

—Ronald A. Wirtz

Manufacturing crashed in 2009; small bounce expected in 2010

By TOBIAS MADDEN
Regional Economist

Manufacturing activity declined significantly in 2009 across the Ninth District. Manufacturers' outlook for their operations in 2010 is for a small bounce back, but they expect the overall economy to fall further, according to the November survey of manufacturers conducted by the Federal Reserve Bank of Minneapolis and the Minnesota Department of Employment and Economic Development.

Manufacturers were blown away in 2009. “The economy is terrible,” noted a small Minnesota manufacturer. A whopping 72 percent of respondents said orders were down in 2009 from 2008. Two-thirds sliced production, and 61 percent cut employment. Manufacturers also cut investment and product prices. Profits fell as well. “I've been in business for 33 years and now face losing it,” said another small Minnesota manufacturer. The dismal results were evident across states and sizes of firms. “We are struggling to survive and may not make it,” a small South Dakota producer said.

Many manufacturers are experiencing tighter credit: 28 percent reported that their access to bank credit deteriorated over the past three months, and only 9 percent said credit conditions improved. “We were dropped by our bank of 10 years even though we were never late on any payment. Our sales and profits are down, and we no longer ‘fit’ their risk tolerance, which they blame on tighter scrutiny by the Federal Reserve,” said a medium-sized Wisconsin firm.

Compared with 2009, manufacturers' outlook for orders and production are

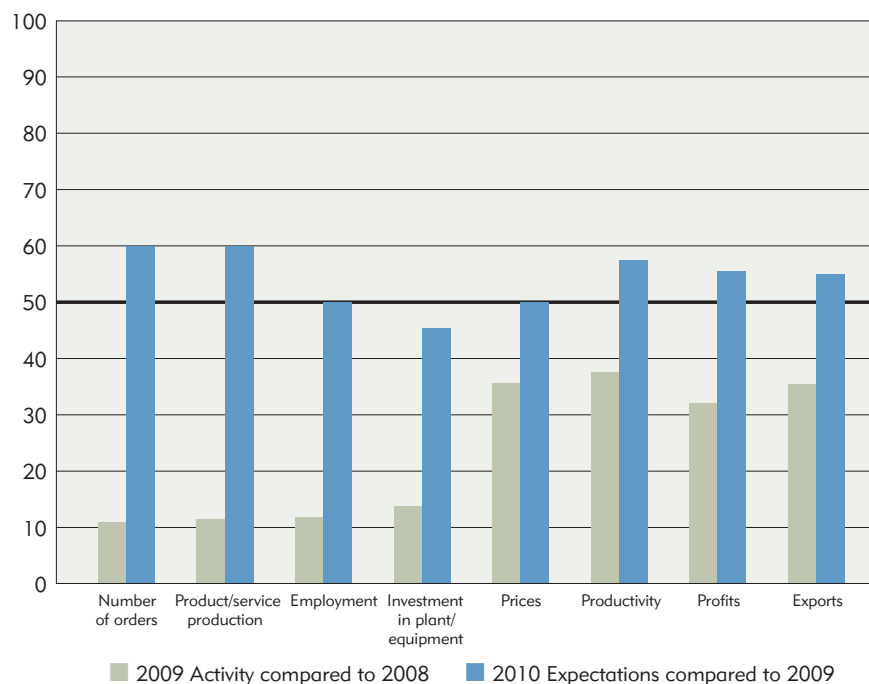
up (see chart). However, they expect to keep employment, investment and prices at 2009 levels. “We are keeping the door open and waiting for an upturn in the economy,” a Montana medium-sized producer said. Manufacturers expect productivity and profits to edge up in 2010 from 2009 levels. Meanwhile, after dropping in 2009, respondents believed exports will increase slightly in 2010, led by Minnesota and South Dakota exporters.

Even though respondents expect their own businesses to recover somewhat, they anticipate continued deterioration in

their state economies. “Hold on to your hat; this is gonna be a tough one coming!” said a small Montana manufacturer. Respondents anticipate downturns in business investment, employment, corporate profits and consumer spending, and they believe overall economic growth will be flat. Respondents from the Dakotas are the most optimistic, and those from the Upper Peninsula of Michigan are the most pessimistic for their state economies. Over half of respondents expect increased inflation levels in 2010 from the tepid inflation of 2009. ■

Manufacturing activity was way down in 2009 and should increase slightly in 2010

(Above 50 indicates expansion; below 50 indicates contraction)



Sources: Federal Reserve Bank of Minneapolis; Minnesota Department of Employment and Economic Development