Moderate economic recovery expected to continue

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The moderate pace of economic growth and job increases observed since the end of the recession in June 2009 is expected to continue over the next 12 to 18 months, according to the Minneapolis Fed's regional forecasting models and midyear survey of business leaders. Overall, the district economic recovery has performed better than the national recovery. However, both the district and national economies were buffeted somewhat by events abroad and at home this spring.

During the economic recovery, the agriculture sector has been strong, manufacturing gained some traction and overall employment and consumer spending have increased, albeit at a measured pace. However, the impact of global events, falling home prices and a sour construction sector has kept a foot on the brake. Nevertheless, the Minneapolis Fed's forecasting models predict that employment will continue to expand and that personal income will increase over the next 18 months.

Recent slowing in recovery

Data released during the spring raised concerns that the pace of the recovery might be turning south. Nationally, the economy grew 1.9 percent during the first quarter of 2011, slower than the almost 3 percent growth during 2010. Furthermore, the May employment report showed that only 56,000 jobs were gained, less than half of what many economists were predicting.

Spring included a number of events that likely dragged on economic growth. Unrest in the Middle East and stronger global demand contributed to gains in oil prices and eventually gas prices at the pump. After dipping below $40 per barrel during the recession, oil prices climbed above $100 per barrel by March. In Minnesota, gasoline prices reached over $4 per gallon, but were down to $3.71 per gallon at the end of May. Still, this was $1.13 per gallon more than a year ago.

The earthquake and tsunami in Japan disrupted supply chains, which slowed operations for a number of U.S. manufacturers. Domestically, home prices have continued to fall, reducing household wealth and increasing risks for foreclosure. The S&P/Case-Shiller Home Price Index indicated that home prices fell more than 5 percent during the first quarter compared with a year earlier, reaching levels last seen during 2002.

While these developments are cause for concern, there are signs of optimism for the national and district economies. Global economic conditions have been relatively strong, playing a role in boosting exports (see related story on page 14). Furthermore, corporate profits have continued to grow, putting businesses in a position to expand once investment prospects find more sure footing.

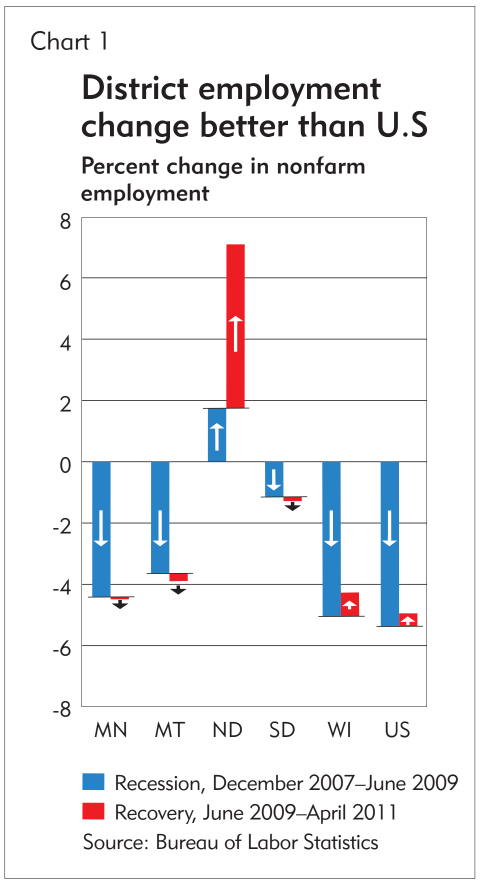
District employment growth holding its own

On the whole, the district economy has been more robust than the national economy during the recession and recovery in part due to positive developments in agriculture, mining and oil drilling. During the recession, district employment losses were smaller than in the United States; employment even grew in North Dakota (see Chart 1). Elsewhere, the *fedgazette* investigates the differences in employment changes between district states and the nation (see page 18).

Recovery employment gains have been modest in district states and the United States, except in North Dakota, where employment has grown 5.4 percent since the recession ended. North Dakota has enjoyed robust oil drilling activity; in April, 160 oil rigs were active in the state, up from 96 a year earlier.

Employment growth over the past year (April compared with a year earlier) was 0.5 percent in the district and 1.1 percent nationally (see Chart 2). Industries with the strongest employment gains in the district include natural resources and mining (+22 percent), manufacturing (+2.8 percent), professional and business services (+1.9 percent), and education and health services (+1.7 percent). While the gains in natural resources and mining are impressive, the sector represents only 0.5 percent of district employment. Industries with job losses were led by an almost 11 percent drop in construction employment. Meanwhile, government, information and financial activities, and leisure and hospitality had job losses of less than 1 percent.

The Minneapolis Fed's forecasting models indicate that employment growth will pick up somewhat in 2011 and 2012 after slow growth during the recovery (see page 19). Meanwhile, 30 percent of respondents to the Minneapolis Fed's midyear outlook poll expect to hire additional full-time workers over the next 12 months, while only 7 percent expect to reduce their full-time employment (go to minneapolisfed.org).

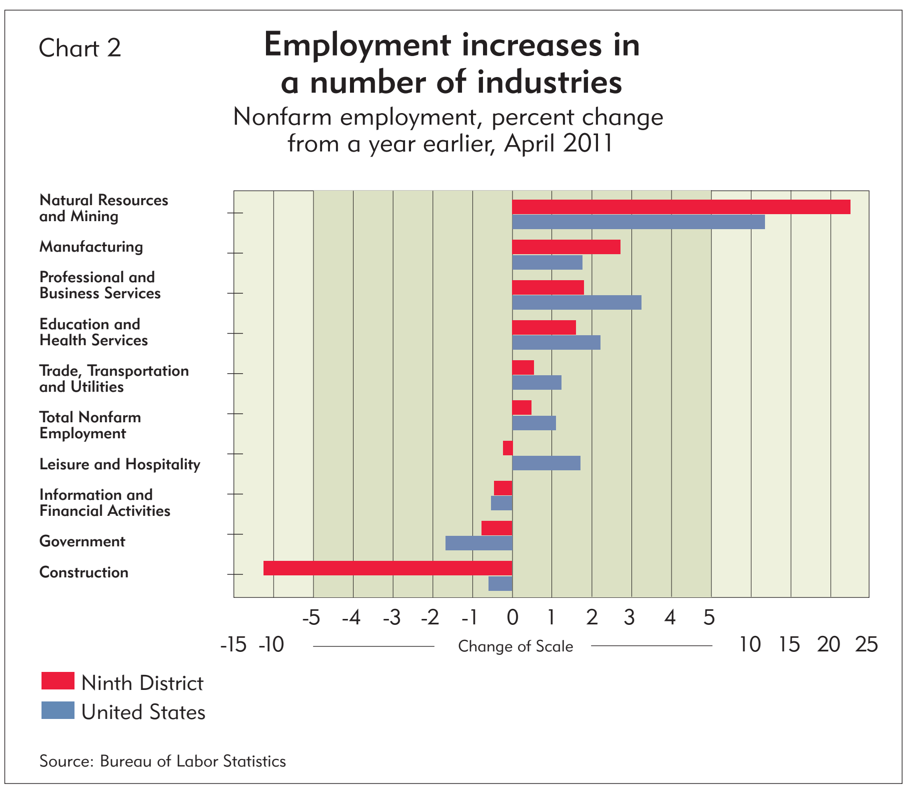


During the recession, the unemployment rate increased more in the nation than in district states, except in Wisconsin, where it increased 4.7 percentage points (see Chart 3). During the recovery, unemployment rates decreased more than the U.S. rate in Minnesota, North Dakota and Wisconsin, had a smaller decrease in South Dakota and continued to increase in Montana. Nevertheless, Montana, like all other district states, had a lower April unemployment rate than the United States. The Minneapolis Fed's forecasting models predict that unemployment rates will continue to step down through 2012, but will generally remain above historical averages.

Manufacturing strong, construction weak

While supply disruptions caused by the Japanese earthquake challenged manufacturers recently, the district manufacturing sector continues to grow. As manufacturing employment expanded over the past year, a June survey of purchasing managers by Creighton University (Omaha, Neb.) showed that manufacturing activity in Minnesota and the Dakotas increased every month during 2011.

While manufacturing has been on the rise, construction continues to falter. Not only has construction employ-



ment decreased over the past year, district housing units authorized were down 20 percent for the first four months of 2011 compared with a year earlier. On an optimistic note, the Minneapolis Fed's forecasting models point to increases in housing authorizations by year-end 2012.

Consumer spending growing moderately

Since the end of the recession, consumer spending has made moderate gains. During the first part of 2011, consumers continued to increase their spending, but have been facing headwinds in the form of higher food and energy prices and continued declines in home values. Inflation as measured by the consumer price index increased 3.2 percent in April compared with a year ago. Rising food and energy prices played a primary role in this increase. Once they are removed, the core rate of inflation increased only 1.3 percent.

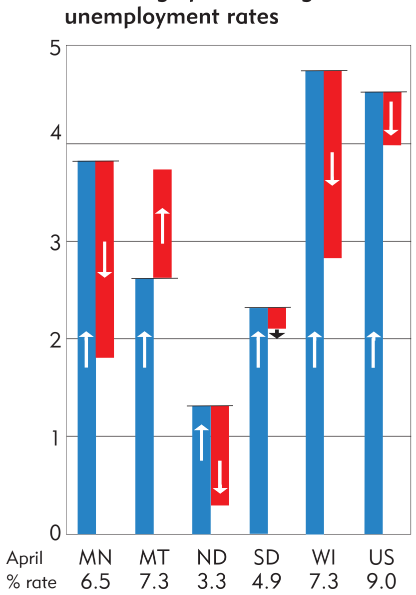
While price increases in food and energy have pinched consumers' pocketbooks, these expenditures on average represent far less than half of consumers' total expenditures. Nationally, consumers at the median level of income use 27 percent of their total out-of-pocket expenditures for food and energy. For low-income families, the impact of these price increases is larger; consumers at the lowest quintile of income use 32 percent of their expenditures for food and energy.

Consumer spending in the district will be buoyed by increases in personal income. The Minneapolis Fed's forecasting models predict that personal income will rise over the next 18 months, with growth rates during 2011 the fastest since before the recession began.

Chart 3

District unemployment rate change also beat U.S.

Percentage point change in unemployment rates



Recession, December 2007–June 2009
Recovery, June 2009–April 2011
Source: Bureau of Labor Statistics

Farmers get a late start in 2011

In addition to large harvests, prices for district agricultural commodities in 2010 returned to levels near their previous peak in 2008. These two factors led to strong farm incomes. However, the first half of 2011 has seen higher input costs and delays in planting. Farmers and ranchers are still bolstered by high output prices, and the outlook is for more of the same. Land prices continue to increase.

According to the Minneapolis Fed's first-quarter (April 2011) agricultural credit conditions survey, 2010 was a strong year for agricultural income, with 83 percent of respondents reporting increased income (go to minneapolisfed.org). Agricultural lenders are somewhat optimistic for farm profits in the second quarter of 2011, with 57 percent of survey respondents expecting increased income and only 3 percent expecting decreased income.

Farmers are concerned about the start of 2011. Due to wet, cool weather in most parts of the district as well as flooding, planting was delayed, and corn, wheat and soybean crop progress is slow. Emergence rates for these crops were well behind the five-year averages as of early June, which likely will have a negative effect on yields. On the upside, nearly all of the district is free from drought conditions.

For farmers, the outlook for prices is strong. Corn, soybean and wheat prices have continued to increase in 2011 from already high levels in 2010, and this trend is expected to continue into 2012 (see table). The outlook for revenues is mixed, as higher prices may be offset somewhat by lower yields. Profits may not be as large as in 2010 due to potentially lower yields and increased input costs, including fuel and fertilizer.

For animal producers, the outlook is strong. Prices for hogs and cattle are at historic highs. However, profits are being squeezed a little by higher input costs, particularly for feed and fuel. Once again, increased demand by bioenergy producers has driven feed costs up for those producers who don't live near an ethanol plant and have no access to the feed byproducts produced from ethanol. Dairy prices have also increased sharply, although they are expected to moderate somewhat in 2012. f

Crop, meat and dairy prices rise

Average farm prices

	2008/2009	2009/2010	Estimated 2010/2011	Projected 2011/2012
(Current $ per bushel)				
Corn	4.06	3.55	5.20-5.50	6.00-7.00
Soybean	9.97	9.59	11.40	13.00-15.00
Wheat	6.78	4.87	5.70	7.00-8.40
	2009	**2010**	**Estimated 2011**	**Projected 2012**
(Current $ per cwt)				
All Milk	12.83	16.29	19.65-20.05	17.75-18.75
Choice Steers	83.25	95.38	110.00-114.00	111.00-120.00
Barrows & Gilts	41.24	55.06	62.00-65.00	61.00-66.00

Source: U.S. Department of Agriculture, estimates as of June 2011