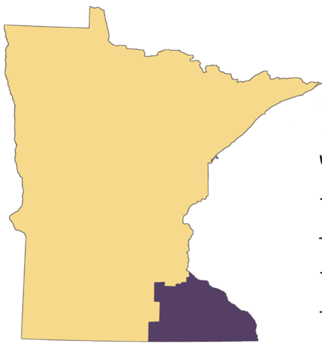

Southeast Minnesota
Economic and Business Conditions Report
Fourth Quarter 2016

This issue is part of a series for the six planning areas of Minnesota –
Central, Northeast, Northwest, Southeast, Southwest, and Twin Cities.
The Southeast Minnesota Planning Area consists of 11 counties:
Dodge, Fillmore, Freeborn, Goodhue, Houston, Mower, Olmsted, Rice, Steele, Wabasha, and Winona.

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Executive Summary

Continued strong economic growth in Southeast Minnesota is expected over the next several months according to the most recent prediction of the Southeast Minnesota Index of Leading Economic Indicators (LEI). After a quarter in which the LEI experienced a 2.34 point increase, the Southeast Minnesota leading index rose another 4.04 points in the fourth quarter of 2016. Three components of the LEI had positive readings in the current quarter. A decrease in initial claims for unemployment benefits, improvement in the Minnesota Business Conditions Index (which serves as a general measure of state business conditions) and stronger consumer sentiment helped lift this quarter's index. A smaller number of residential building permits in Rochester as well as weaker new filings of incorporation and LLC in the Southeast Minnesota planning area were the only negative components of this quarter's LEI.

There were 798 new business filings with the Office of the Minnesota Secretary of State in Southeast Minnesota in the fourth quarter of 2016 — representing a 7.8 percent increase from one year ago. There were 65 new regional business incorporations in the fourth quarter, a 6.6 percent improvement from prior year levels. At a level of 493, fourth quarter new limited liability company (LLC) filings in Southeast Minnesota were 17.4 percent higher than the fourth quarter of 2015. With 205 filings, new assumed name activity was 7.2 percent lower than the same quarter in 2015. There were 35 new filings for Southeast Minnesota non-profits over the three months ending December 2016—three fewer filings than one year earlier.

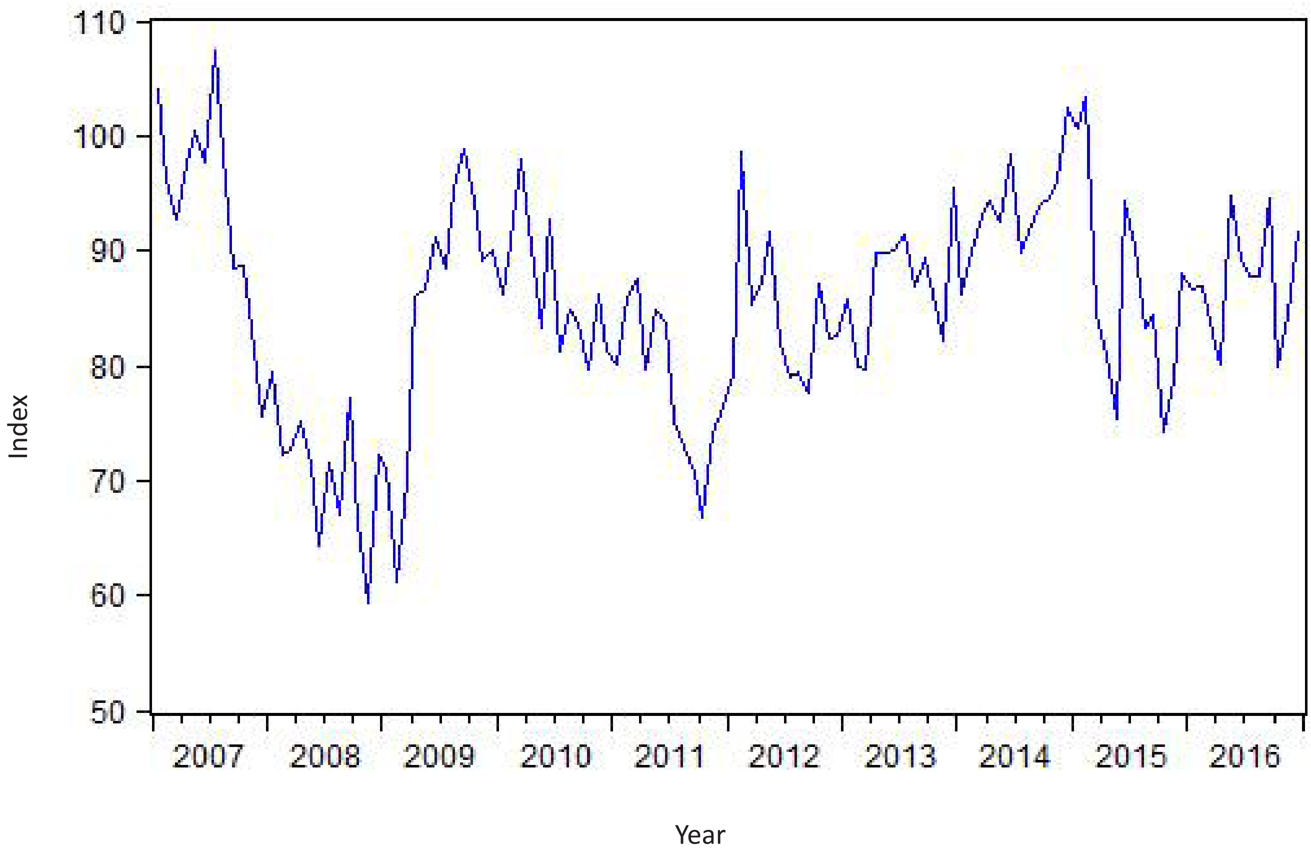
Using preliminary data, employment of Southeast Minnesota residents fell by 1.9 percent over the year ending December 2016. Compared to December 2015, 5,183 fewer residents of Southeast Minnesota now have jobs. The regional unemployment rate was 3.6 percent in December, higher than the 3.1 percent level recorded one year earlier. Initial claims for unemployment insurance in December 2016 were basically unchanged from one year earlier and the Southeast Minnesota labor force contracted by 1.5 percent. The average weekly wage in Southeast Minnesota rose to $872 in the most recent reporting period—an increase of 2.5 percent over year earlier numbers. The planning area's bankruptcies have begun to level out.

Data from the Rochester area—the largest market in Southeast Minnesota—were mixed, with an increase in overall employment (along with employment growth in the key health/education sector), higher new business filings, and a rise in the value of residential building permits having a positive impact on the outlook. On the negative side was a smaller labor force, a higher unemployment rate, increased initial jobless claims, and weaker manufacturing employment.

Southeast Minnesota Leading Economic Indicators Index

The SCSU Southeast Minnesota Leading Economic Indicators (LEI) index is designed to predict performance of the regional economy with a four-to-six month lead time. The LEI finished 4.04 points higher in the fourth quarter, and is now 4.3 percent above its level of one year earlier. As can be seen in the accompanying figure, the LEI has bounced around in recent quarters.

SCSU Southeast Minnesota Index of Leading Economic Indicators (December 1999 = 100)



Components of SCSU Southeast Minnesota Leading Economic Indicators Index

Component of Index	Contribution to LEI, 4th quarter 2016	Contribution to LEI, 3rd quarter 2016
Minnesota Business Conditions Index	2.79	-2.31
Southeast Minnesota initial claims for unemployment insurance	3.45	-1.73
Southeast Minnesota new filings of incorporation and LLCs	-2.46	2.96
Rochester MSA residential building permits	-4.12	4.89
Consumer Sentiment, University of Michigan	4.38	-1.47
TOTAL CHANGE	**4.04**	**2.34**

Three of five components of the LEI had a positive reading in the fourth quarter. Recent improvement in the Minnesota Business Conditions survey (conducted by Creighton University), which serves as a general measure of state business conditions, had a positive value in this quarter's index. Decisions to consume medical services depend in part on consumer choice, so consumer sentiment is used as a national-level indicator of Southeast Minnesota business activity. Consumer sentiment strengthened in the most recent quarter. Lower initial claims for unemployment insurance in recent months also helped boost the LEI in the fourth quarter. Weaker new filings of incorporation and LLC in the Southeast Minnesota planning area in the fourth quarter and lower Rochester metro area residential building permits were each declining components of this quarter's leading index.

SCSU Southeast Minnesota Leading Economic Indicators Index

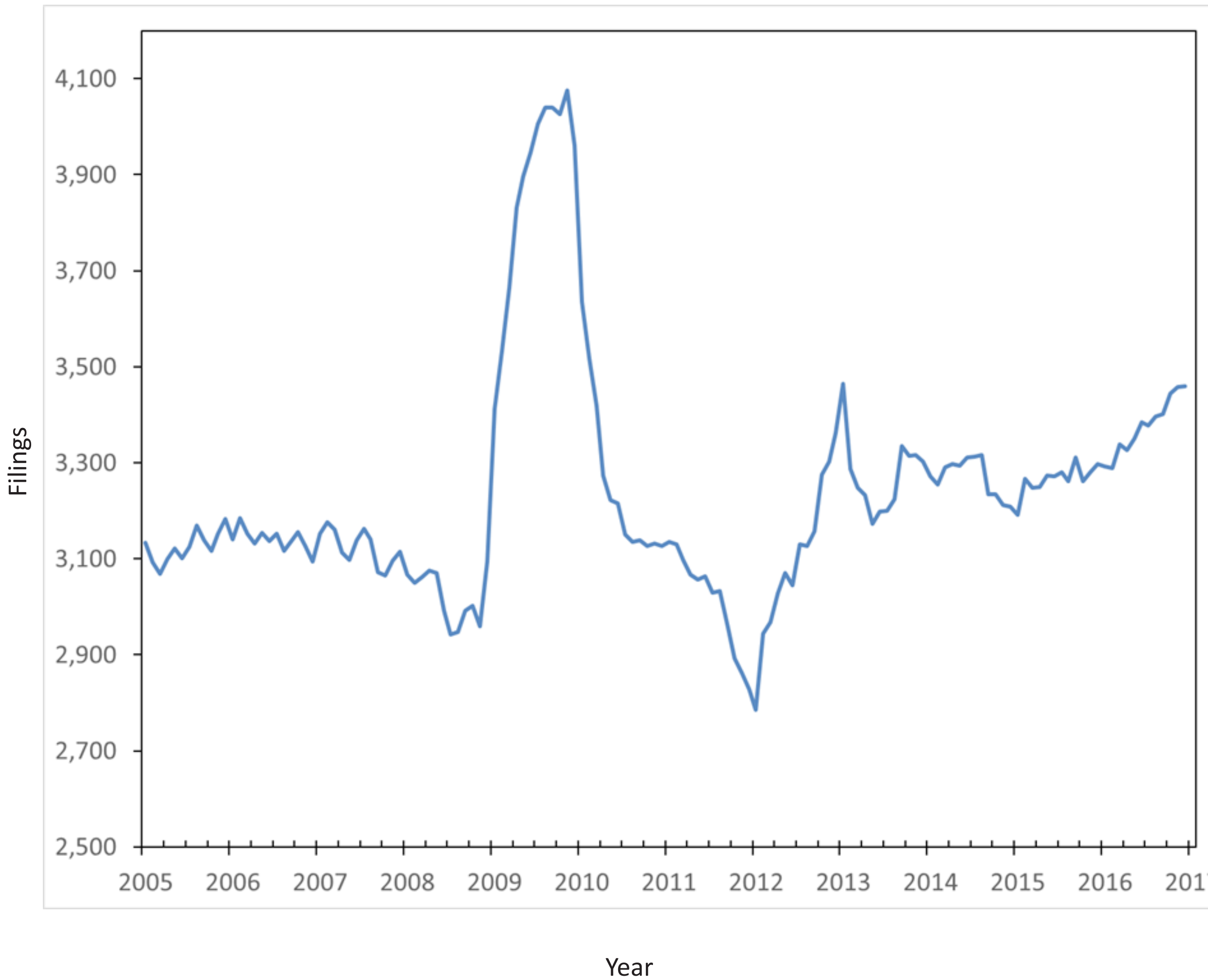
	2016	2015	Percentage change
Minnesota Business Conditions Index December	52.3	48.2	8.5%
Southeast Minnesota initial claims for unemployment insurance December	2,726	2,717	0.3%
Southeast Minnesota new filings of incorporation and LLCs Fourth Quarter	558	481	16.0%
Rochester MSA single-family building permits December	36	44	-18.2%
Consumer Sentiment, University of Michigan December	98.2	92.6	6.0%
Southeast Minnesota Leading Economic Indicators Index December (December 1999 = 100)	91.9	88.1	4.3%

Southeast Minnesota Business Filings

Fourth quarter new business filings rose 7.8 percent to a level of 798. As can be seen in the accompanying graph, the 12-month moving total of new business filings in Southeast Minnesota has trended upward since the end of 2014. The abrupt increase in new filings in the middle of 2008 is largely a result of increased new LLC filings. This outlier (resembling a shark fin) is related to considerably higher filings in the construction industry due to legal and regulatory issues and appears to be a one-time only transitory event seen in the data in all regions of Minnesota.

Note: The graphs in this section show the 12-month moving total for the various new business filings in Southeast Minnesota that are registered with the Office of the Minnesota Secretary of State. Doing so removes seasonal patterns in the data.

Total New Business Filings—Southeast Minnesota Planning Area (12-month moving total)



Quarter	IV: 2015	I: 2016	II: 2016	III: 2016	IV: 2016	2016 Quarter IV: Percent change from prior year
Southeast Minnesota Total New Business Filings	740	929	911	821	798	7.8%

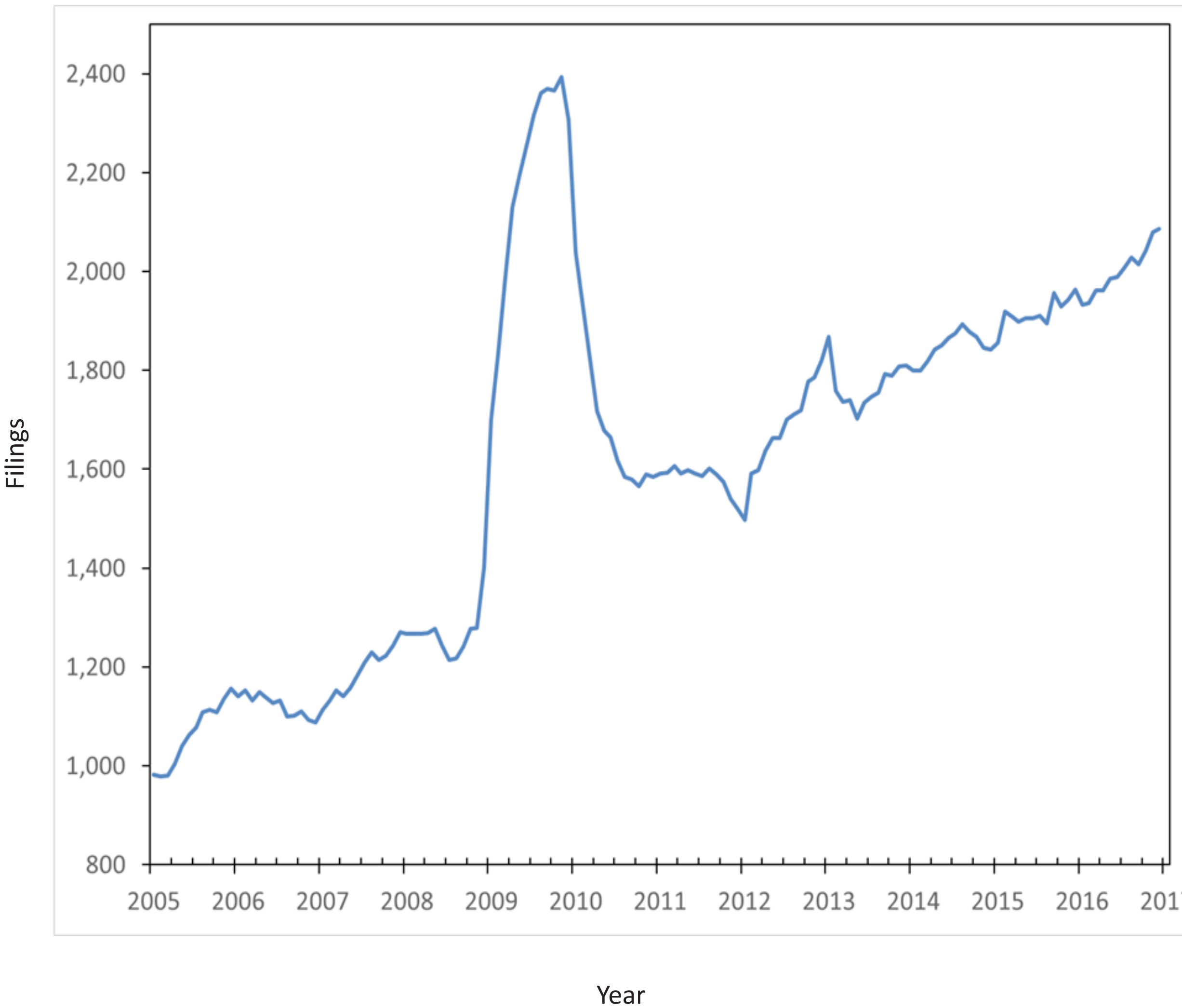
New business incorporations trended downward in Southeast Minnesota from 2005 to 2012, but have fluctuated around a fairly constant trend in recent years. New incorporations rose 6.6 percent from year earlier levels in the most recent quarter.

New Incorporations—Southeast Minnesota Planning Area (12-month moving total)

Quarter	IV: 2015	I: 2016	II: 2016	III: 2016	IV: 2016	2016 Quarter IV: Percent change from prior year
Southeast Minnesota New Business Incorporations	61	80	73	65	65	6.6%

There has been a move in Southeast Minnesota, as in all of the state, away from the traditional incorporation form of business organization towards the LLC. While new business incorporations remain an important indicator of new business formation in Southeast Minnesota, LLCs are increasingly useful in evaluating regional economic performance. As seen below, there is a considerable upward trend in LLCs in Southeast Minnesota. With the exception of the outlier period in 2008-2009, new LLC formation has shown a fairly steady rate of growth since 2005. Fourth quarter LLC filings rose by 17.4 percent over their year earlier level.

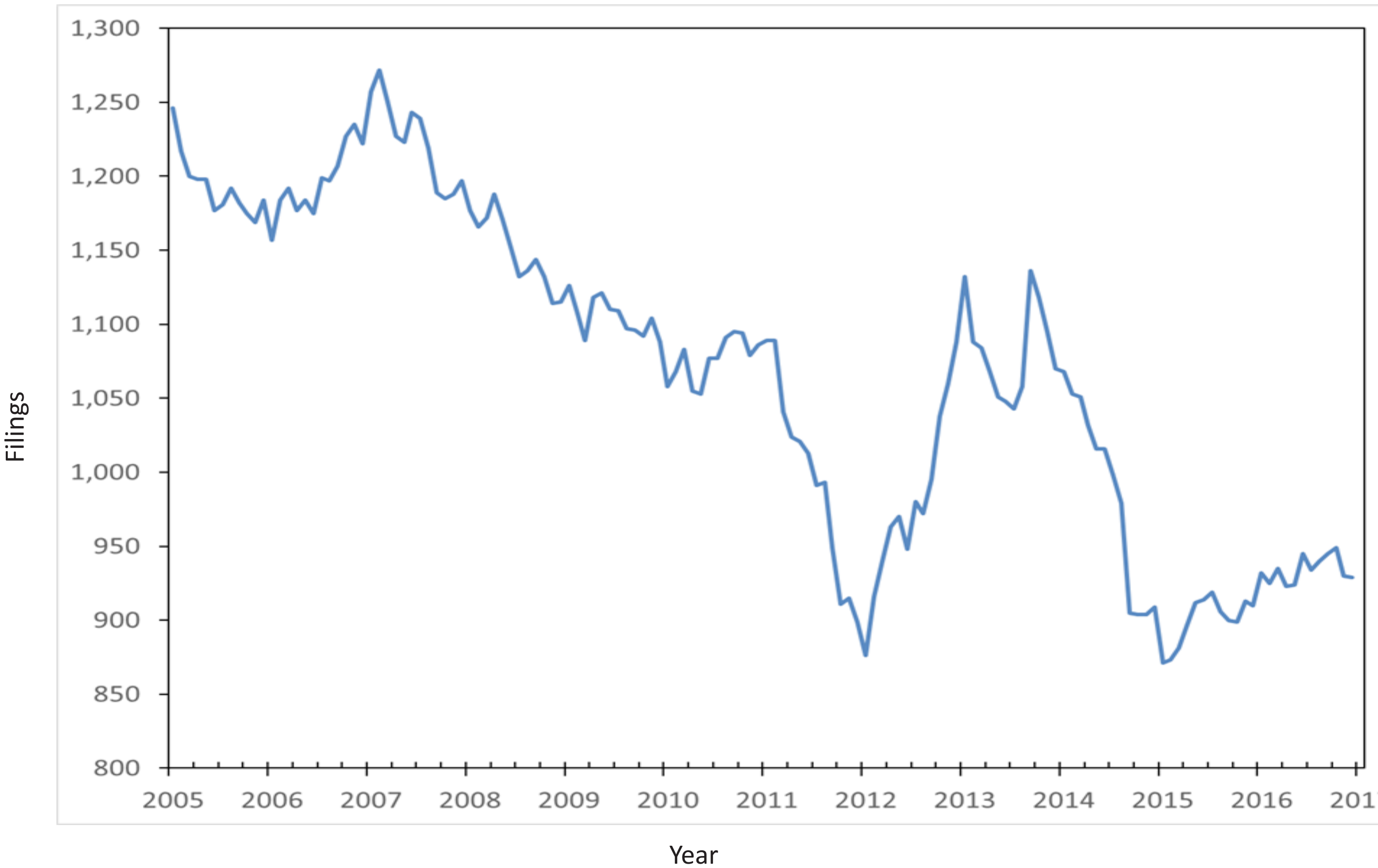
New Limited Liability Companies—Southeast Minnesota Planning Area (12-month moving total)



Quarter	IV: 2015	I: 2016	II: 2016	III: 2016	IV: 2016	2016 Quarter IV: Percent change from prior year
Southeast Minnesota New Limited Liability Companies	420	539	536	519	493	17.4%

On a year over year basis, assumed names, which include sole proprietors or organizations that do not have limited liability, declined in Southeast Minnesota in the fourth quarter. As can be seen in the accompanying graph, after increasing in 2012, this series moved downward until the beginning of 2015, at which time it began to slowly trend upward. This quarter's activity seems to have ended that upward trend.

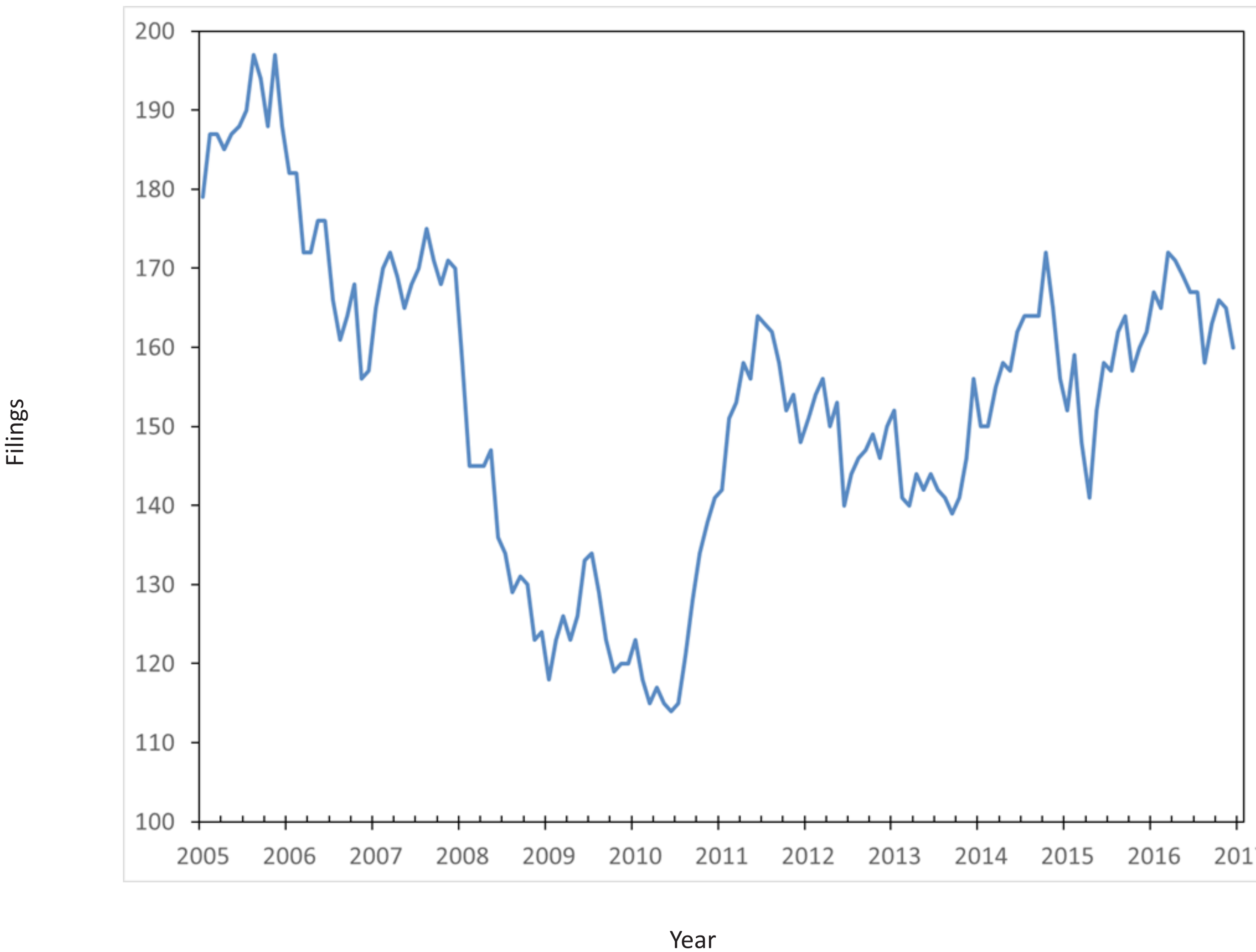
New Assumed Names—Southeast Minnesota Planning Area (12-month moving total)



Quarter	IV: 2015	I: 2016	II: 2016	III: 2016	IV: 2016	2016 Quarter IV: Percent change from prior year
Southeast Minnesota New Assumed Names	221	270	256	198	205	-7.2%

The moving total of new Southeast Minnesota non-profits registered with the Office of the Minnesota Secretary of State has been volatile over the past several years. As can be seen in the accompanying graph, this series has turned downward in 2016. The number of newly formed non-profits totaled 35 in the recent quarter (a 7.9 percent reduction from the fourth quarter of 2015).

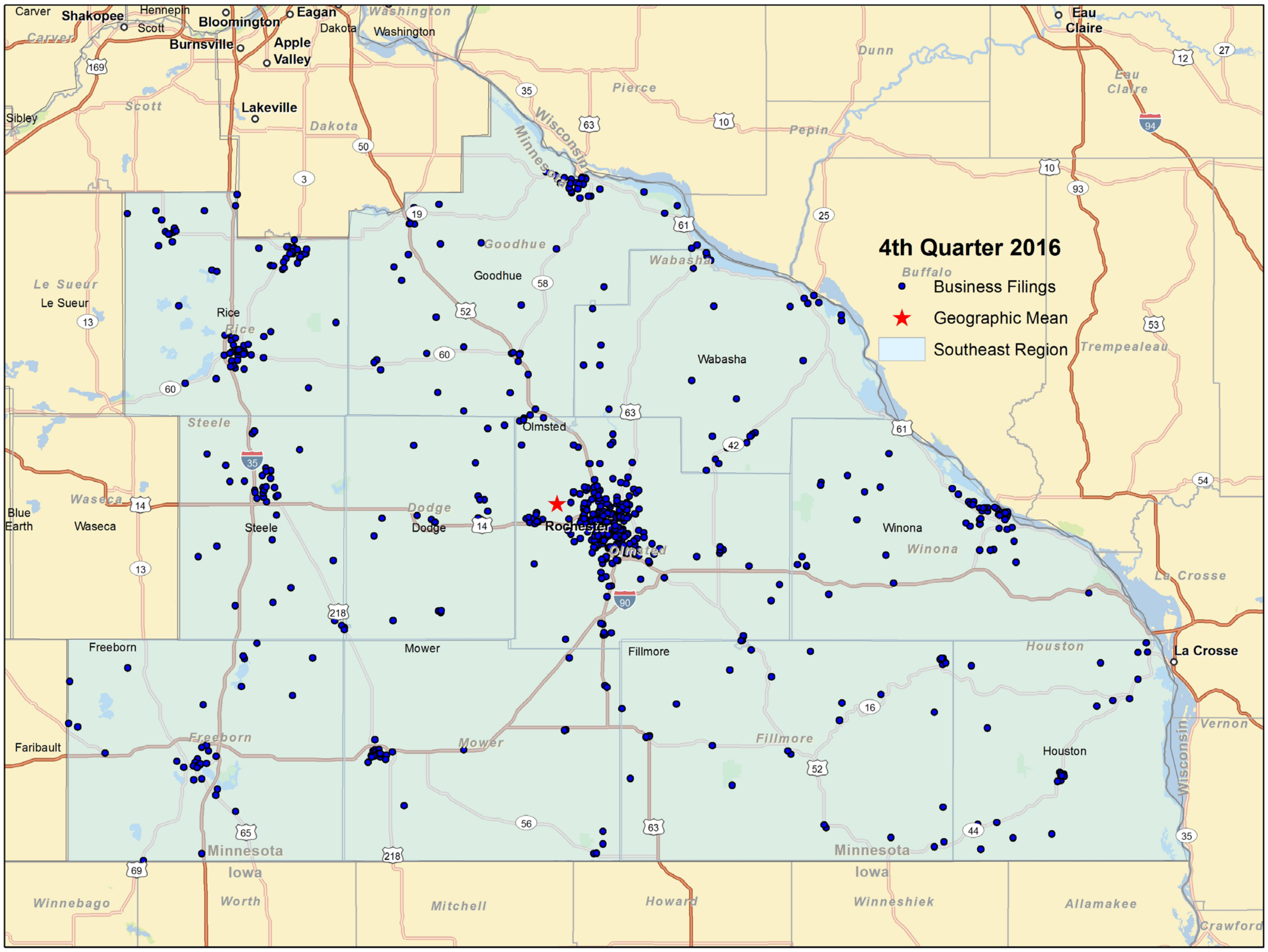
New Non-Profits—Southeast Minnesota Planning Area (12-month moving total)



Quarter	IV: 2015	I: 2016	II: 2016	III: 2016	IV: 2016	2016 Quarter IV: Percent change from prior year
Southeast Minnesota New Non-Profits	38	40	46	39	35	-7.9%

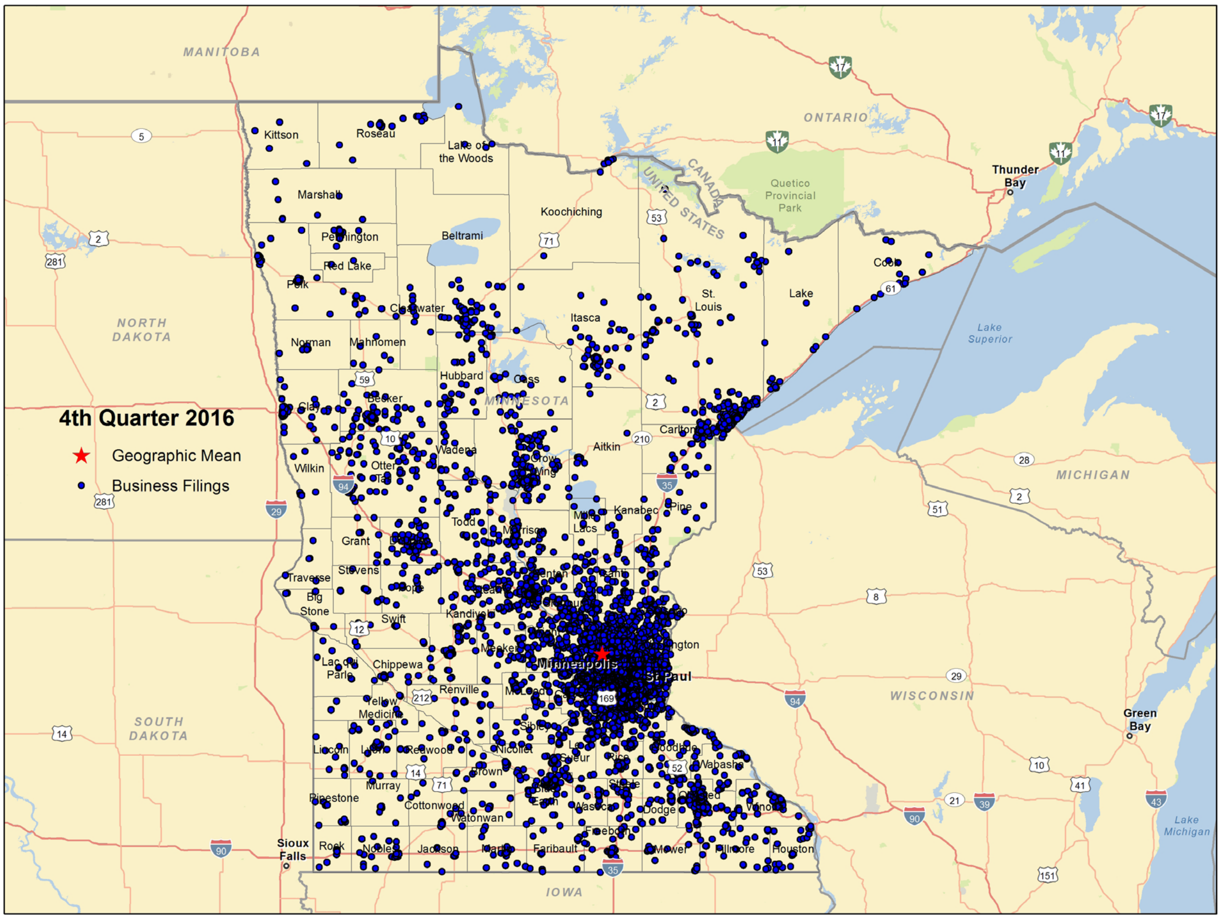
The first map shown below is a visual representation of new business filings around the Southeast Minnesota planning area in the fourth quarter of 2016. The densest areas of new business formation are in the Rochester metro. Owatonna, Faribault, Northfield, Albert Lea, Austin, and the river cities of Winona and Red Wing also generated multiple new business filings. Well-traveled roadways are also a predictor of new business formation in Southeast Minnesota.

Southeast Minnesota Planning Area--New Business Formation--Quarter 4: 2016



The second map shows new business filings for the state as a whole. This visual aid demonstrates the considerable extent to which the Twin Cities metro area dominates new business formation in the state. The map shows how the Twin Cities metro stretches along roadways into the Southeast, Southwest and Central planning areas. The map demonstrates the importance of cities and roadways in encouraging economic development. St. Cloud now appears to be integrated into the Twin Cities metro as the I-94/US-10 corridor continues to be a magnet for new business formation.

Minnesota--New Business Formation--Quarter 4: 2016

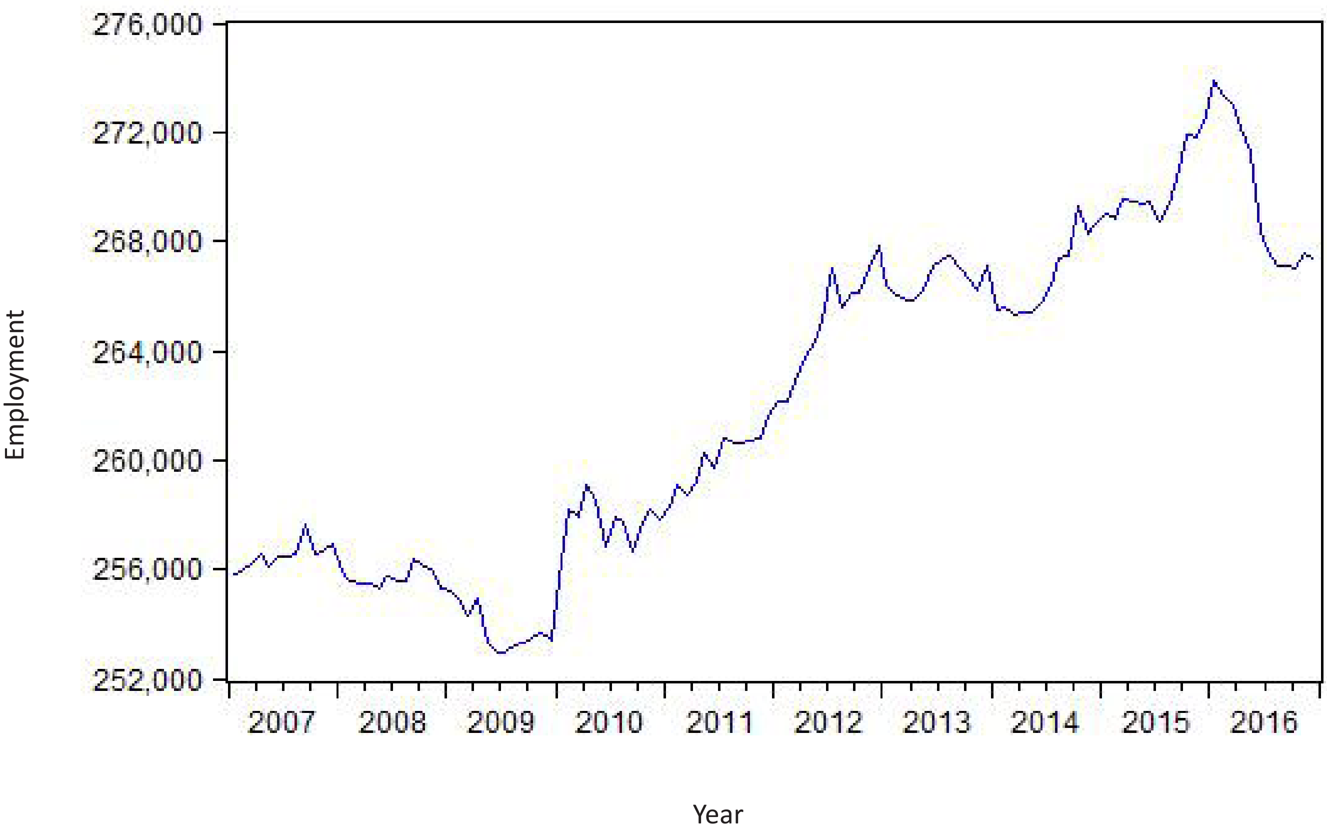


Southeast Minnesota Labor Market Conditions

Employment of those living in the Southeast Minnesota planning area fell by 1.9 percent over the past year. As shown in the accompanying graph, the 12-month moving average of total employment had been trending upward since the end of the Great Recession. But this trend appears to have been reversed in 2016. It should be noted that upcoming benchmark revisions to regional employment data might alter some of the data patterns found in this section.

Note: seasonally adjusted labor market data are typically not available to evaluate regional economic performance so some series have been created to illustrate seasonal patterns of the regional labor market. Graphs of these indicators are found in this section of the report. Tabular data are not seasonally adjusted.

Employment—Southeast Minnesota Planning Area (12-month moving average)



Month	December 2015	July 2016	August 2016	September 2016	October 2016	November 2016	December 2016
Employment (Not seasonally adjusted)	271,754	270,080	269,279	266,908	268,990	268,783	266,571

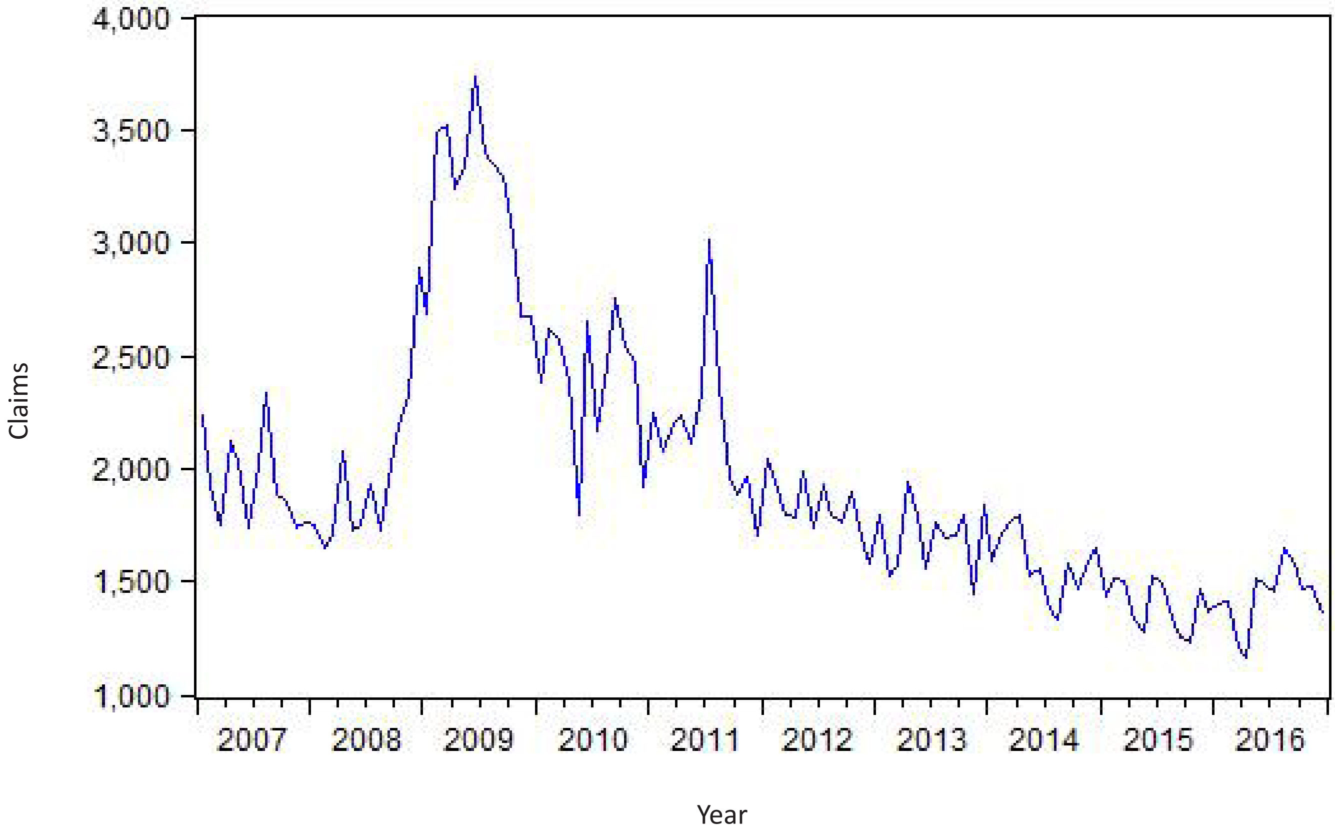
The seasonally adjusted unemployment rate in Southeast Minnesota has started to rise over the past couple of quarters. The non-seasonally adjusted unemployment rate stands at 3.6 percent, considerably higher than the 3.1 percent rate observed one year ago.

Unemployment Rate, seasonally adjusted—Southeast Minnesota Planning Area

Month	December 2015	July 2016	August 2016	September 2016	October 2016	November 2016	December 2016
Unemployment Rate (Not seasonally adjusted)	3.1%	3.4%	3.4%	3%	2.8%	2.8%	3.6%

New claims for unemployment insurance in December 2016 were 0.3 percent higher than one year earlier. On a seasonally adjusted basis, these claims appear to have flattened out in recent quarters.

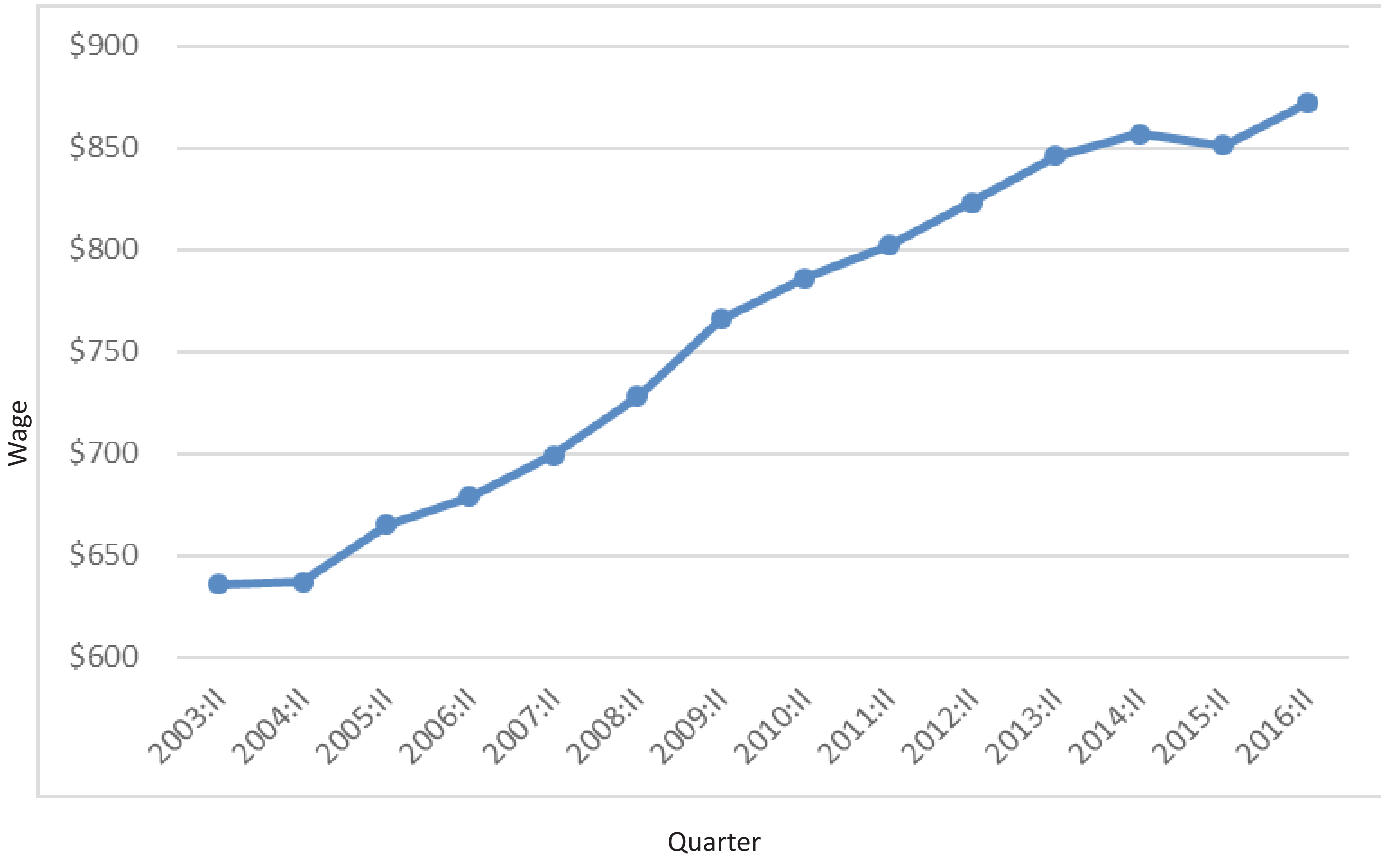
Total Initial Claims for Unemployment Insurance, seasonally adjusted—Southeast Minnesota Planning Area



Period	December 2015	July 2016	August 2016	September 2016	October 2016	November 2016	December 2016
Initial claims (Not seasonally adjusted)	2,717	1,118	977	994	1,110	2,385	2,726

The Southeast region has the second highest average weekly wage of Minnesota's six planning areas (at $1,117, the Twin Cities region has the highest average wages). With an average wage of $872, Southeast Minnesota wages are considerably higher than the wage scale faced by Central Minnesota workers who have the next highest pay at $766 per week.

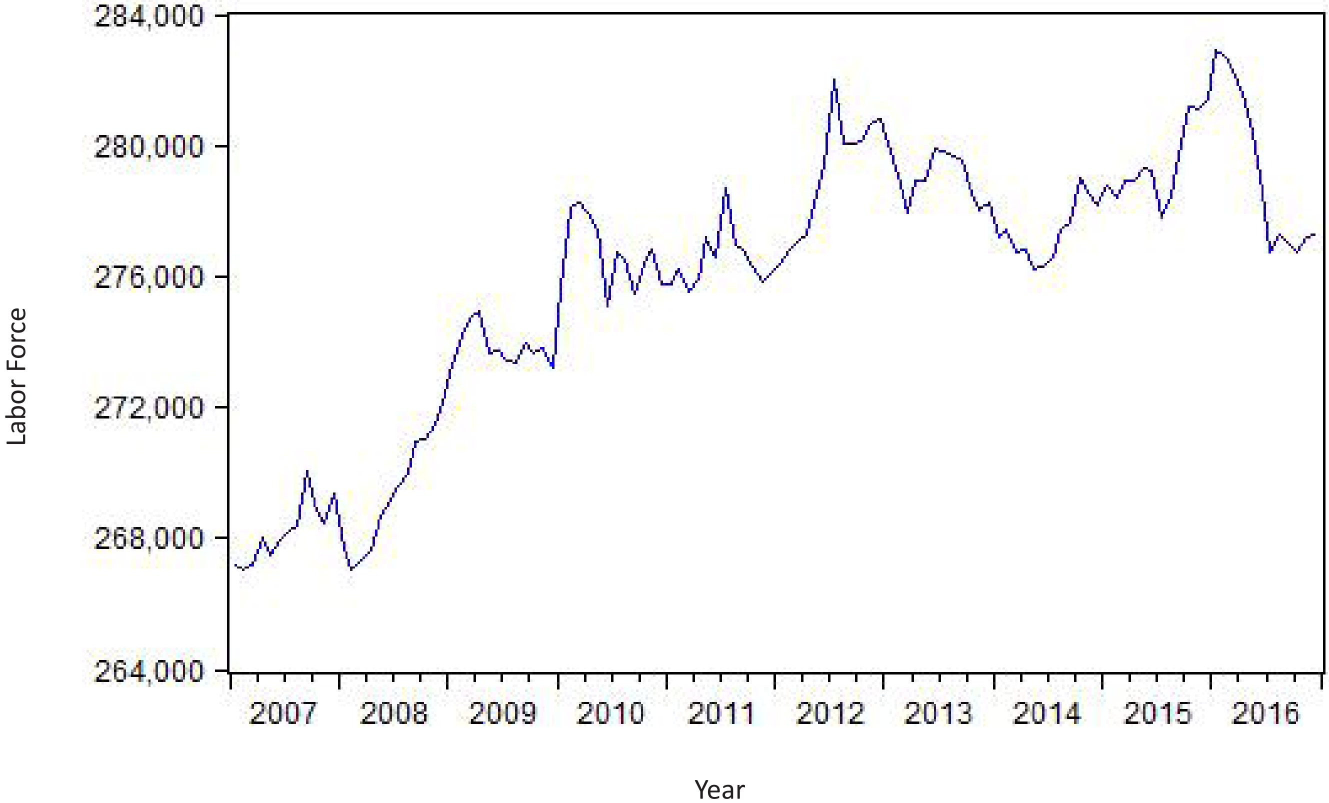
Average Weekly Wage---Southeast Minnesota Planning Area



Quarter	2011:II	2012:II	2013:II	2014:II	2015:II	2016:II
Average Weekly Wage	$802	$823	$846	$857	$851	$872

The Southeast Minnesota labor force contracted by 1.5 percent over the last year. The regional labor force is now 4,107 lower than in December 2015.

Labor Force—Southeast Minnesota Planning Area (12-month moving average)

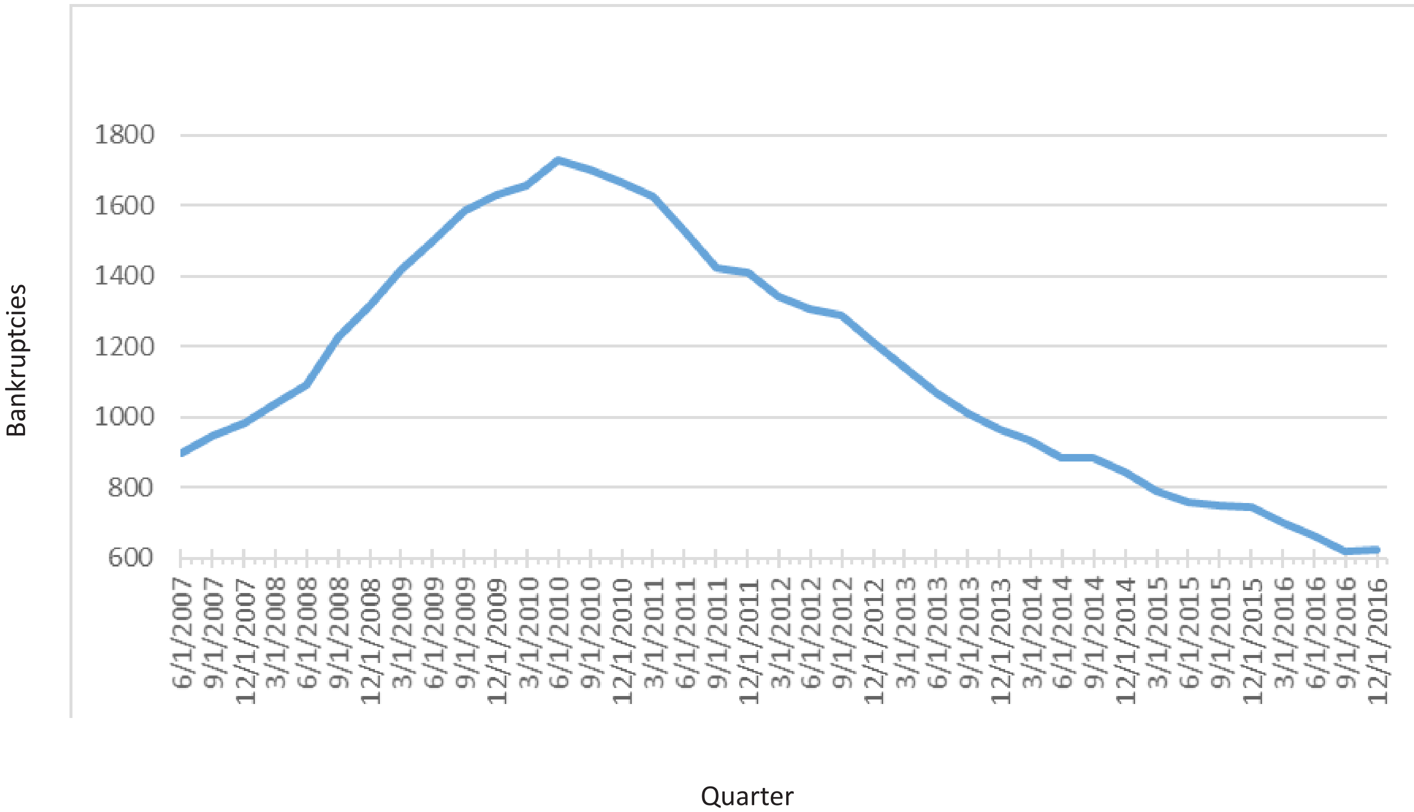


Year (December)	2011	2012	2013	2014	2015	2016
Labor Force (Not seasonally adjusted)	274,395	279,393	277,115	277,218	280,588	276,481

Southeast Minnesota Bankruptcies

The figure below shows the 12-month moving total for Southeast Minnesota bankruptcies since the second quarter of 2007 (shortly before the beginning of the Great Recession). As can be seen in the figure, this moving total increased through the second quarter of 2010, and has steadily declined since that time). With 623 bankruptcies over the past twelve months, bankruptcies in Southeast Minnesota have now begun to level out.

Southeast Minnesota Bankruptcies (12-month moving total)



Year (Fourth Quarter)	2011	2012	2013	2014	2015	2016
Annual Bankruptcies (not seasonally adjusted)	1,411	1,213	963	843	746	623

Economic Indicators

Rochester MSA Indicators

	Period Covered	Current Period	Prior Year	Annual Percent Change	Long-Term Average (since 1999, unless noted)
Labor Market					
Employment	December 2016 (m)	119,657	116,626	2.6% ↑	0.9%
Manufacturing Employment	December 2016 (m)	10,761	10,786	-0.2% ↓	-2.7%
Educational and Health Employment	December 2016 (m)	48,650	47,117	3.3% ↑	2.7%
Average Weekly Work Hours Private Sector	December 2016 (m)	NA	NA	NA	NA
Average Earnings Per Hour Private Sector	December 2016 (m)	NA	NA	NA	NA
Unemployment Rate	December 2016 (m)	3.3%	2.9%	NA ↑	3.9%
Labor Force	December 2016 (m)	118,324	118,705	-0.3% ↓	0.6%
Initial Jobless Claims	December 2016 (m)	1,075	1,028	4.6% ↑	NA
Business Formation					
Total New Business Filings	Fourth Quarter 2016 (q)	431	377	14.3% ↑	341 (since 2000)
New Business Incorporations	Fourth Quarter 2016 (q)	25	28	-10.7% ↓	49 (since 2000)
New Limited Liability Companies	Fourth Quarter 2016 (q)	284	211	34.6% ↑	165 (since 2000)
New Assumed Names	Fourth Quarter 2016 (q)	101	117	-13.7% ↓	108 (since 2000)
New Non-profits	Fourth Quarter 2016 (q)	21	21	0.0% ↔	19 (since 2000)
Rochester Residential Building Permit Valuation, in thousands	December 2016 (m)	24,532	11,583	111.8% ↑	NA

(m) represents a monthly series
(q) represents a quarterly series

Southeast Minnesota contains the Rochester MSA, an area that derives much of its employment from the educational and health sector. This sector continues to be a pillar of economic vitality for Rochester (and for Southeast Minnesota). Year-over-year overall employment in the Rochester area increased by 2.6 percent in December 2016 and employment in the key education/health sector rose by 3.3 percent (above the 2.7 percent long-term annualized growth of employment in this sector). Note that the share of employment in Rochester's educational and health sector has increased from 29.4 percent of employment to more than 40 percent since 1999. The number of new business filings increased in the area and the value of residential building permits rose in the Rochester area during the most recent reporting period. However, the labor force contracted, the unemployment rate rose, initial jobless claims increased and manufacturing employment declined.

State and National Indicators

MINNESOTA Indicators	Dec 2016	Sep 2015	Dec 2015	Change from one quarter ago	Annual Change
Nonfarm payroll employment, SA	2,919,300	2,905,600	2,875,700	0.5%	1.0%
Average weekly hours worked, private sector	33.9	34.1	33.7	-0.6%	0.6%
Unemployment rate, seasonally adjusted	3.9%	4.0%	3.7%	NA	NA
Earnings per hour, private sector	$27.87	$27.33	$26.36	2.0%	5.7%
Philadelphia Fed Coincident Indicator, MN	181.73	180.23	176.73	0.8%	2.8%
Philadelphia Fed Leading Indicator, MN	2.01	1.19	1.23	68.9%	63.4%
Minnesota Business Conditions Index	52.3	48.4	39.4	8.1%	32.7%
Price of milk received by farmers (cwt)	$19.70	$17.90	$17.00	10.1%	15.9%
Enplanements, MSP airport, thousands	1,456.8	1,536.1	1,429.0	-5.2%	1.9%

NATIONAL Indicators	Dec 2016	Sep 2015	Dec 2015	Change from one quarter ago	Annual Change
Nonfarm payroll employment, SA, thousands	145,303	144,808	143,146	0.3%	1.5%
Industrial production, index, SA	104.6	104.2	104.0	0.4%	0.6%
Real retail sales, SA ($)	193,017	191,817	189,246	0.6%	2%
Real personal income less transfers ($, bill.)	12,074.8	12,022.9	11,848.2	0.4%	1.9%
Real personal consumption expenditures ($, bill.)	11,672.4	11,603.3	11,351.5	0.6%	2.8%
Unemployment rate, SA	4.7%	4.9%	5.0%	NA	NA
New building permits, SA, thousands	17,581	20,857	17,620	-15.7%	-0.2%
Standard & Poor's 500 stock price index	2,246.6	2,157.7	2,054.1	4.1%	9.4%
Oil, price per barrel in Cushing, OK	$51.97	$45.18	$37.19	15.0%	39.7%

Across the state there was growth in payrolls, higher earnings per hour, and more average weekly hours worked in the private sector over the past twelve months. The seasonally adjusted unemployment rate rose over the past twelve months. Indicators from the Federal Reserve Bank of Philadelphia are favorable—current conditions are stronger and the future conditions index surged compared to one year earlier. The Minnesota Business Conditions index also turned positive this quarter. Milk prices have finally started to rise and enplanements at the Minneapolis-St. Paul airport increased by 1.9 percent over the last twelve months.

The national economic indicators reported in the table are also largely favorable. Over the past twelve months, stock prices rose, employment increased, and real income and consumer expenditures expanded. The national unemployment rate fell and retail sales improved. Industrial production picked up. National building permits were nearly unchanged from one year earlier and oil prices have begun to rise. While rising oil prices will adversely impact the discretionary income of households, it will also improve the economic well-being of those employed in the energy sector (which has been struggling over the last two years).

The Southeast Minnesota Quarterly Economic and Business Conditions Report is a collaboration between the Office of the Minnesota Secretary of State and the School of Public Affairs Research Institute (SOPARI) of St. Cloud State University. All calculations and text are the result of work by SOPARI, which is solely responsible for errors and omissions herein.

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Thomson Reuters and University of Michigan, Index of Consumer Sentiment

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