Southeast Minnesota Economic and Business Conditions Report Third Quarter 2017

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.

Office of the Minnesota Secretary of State

School of Public Affairs Research Institute
St. Cloud State University

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EXECUTIVE SUMMARY

Despite a decline in the Southeast Minnesota Index of Leading Economic Indicators (LEI), strong economic fundamentals are expected to continue to drive positive economic performance in the southeast portion of the state over the next several months. After a quarter in which the LEI fell by 1.25 points, the third quarter leading index contracted by 8.11 points as several index components recorded negative values. A rise in initial claims for unemployment benefits, a smaller number of residential building permits in Rochester, decreased new filings of incorporation and LLC in the Southeast Minnesota planning area, and a decline in the Minnesota Business Conditions Index (which serves as a general measure of statewide business conditions) all weighed on this quarter's leading index.

There were 792 new business filings with the Office of the Minnesota Secretary of State in Southeast Minnesota in the third quarter of 2017 — representing a 3.5 percent decrease from one year ago. There were 53 new regional business incorporations in the third quarter, an 18.5 percent reduction from prior year levels. At a level of 461, third quarter new limited liability company (LLC) filings in Southeast Minnesota were 11.2 percent lower than the third quarter of 2016. With 231 filings, new assumed name activity was 16.7 percent higher than the same quarter last year. There were 8 more new filings for Southeast Minnesota non-profits over the last three months compared to one year earlier.

Sixty percent of new business filers in the Southeast Minnesota planning area completed the voluntary Minnesota Business Snapshot (MBS) survey in this year's third quarter. Results of this voluntary survey indicate that 6.3 percent of new filers come from communities of color and 7.1 percent are veterans. Almost 3 percent of new filers come from the disability community and 4.2 percent of new filings are made by the immigrant community. Forty-six percent of new business filings in Southeast Minnesota in this year's third quarter were initiated by women. MBS results also show that most new business filers in Southeast Minnesota have between 0 and $10,000 in annual gross revenues (although 41 new filers have revenues in excess of $50,000). The most popular industries for new businesses in Southeast Minnesota are construction, retail trade, professional/scientific/technical and other services. Employment levels at most new firms are between 0 and 5 workers, and 50 percent of those starting a new business consider this a part-time activity.

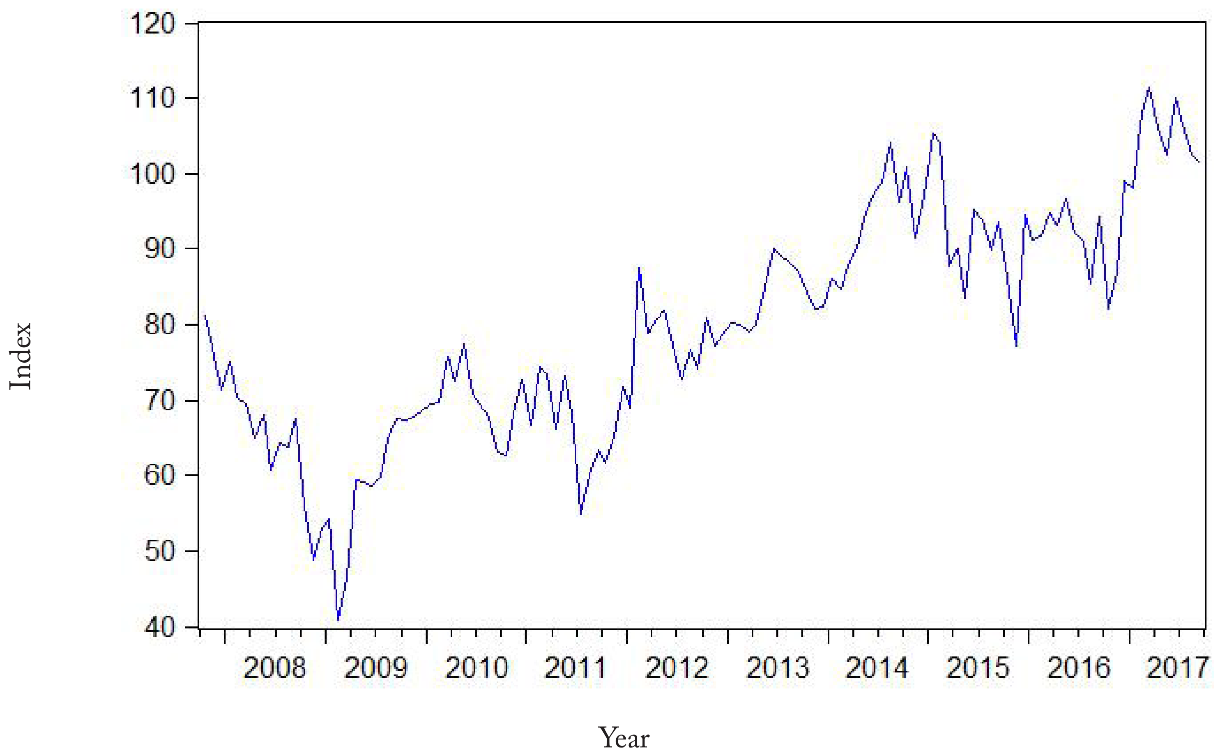
Employment of Southeast Minnesota residents rose by 2.2 percent over the year ending September 2017. The regional unemployment rate was 2.6 percent in September, lower than the 3.2 percent level recorded one year earlier. Initial claims for unemployment insurance in September 2017 declined by 17.8 percent from one year earlier and the Southeast Minnesota labor force increased by 1.5 percent. The job vacancy rate remains elevated in Southeast Minnesota and the planning area's annual bankruptcies increased slightly.

Data from the Rochester area—the largest market in Southeast Minnesota—were very favorable, with an increase in overall employment (along with employment growth in the key health/education sector), a rise in the value of residential building permits, a lower unemployment rate, a growing labor force, longer weekly work hours, and increased hourly earnings having a positive impact on the outlook. On the negative side was lower overall new business filings (including lower new incorporations and LLCs).

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 8.03 points lower in the third quarter, but is still 7.6 percent above its level of one year earlier. As can be seen in the accompanying figure, the LEI had been on the rise since the end of 2016, but has flattened out in recent quarters. Overall fundamentals in the Southeast economy remain strong, so this dip in the LEI should not cause major concerns about longer-term economic performance in this region.

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, 3rd quarter 2017	Contribution to LEI, 2nd quarter 2017
Minnesota Business Conditions Index	-4.88	3.44
Southeast Minnesota initial claims for unemployment insurance	-0.54	-0.13
Southeast Minnesota new filings of incorporation and LLCs	-1.40	-2.17
Rochester MSA residential building permits	-1.21	-1.28
Consumer Sentiment, University of Michigan	0	-1.11
TOTAL CHANGE	**-8.03**	**-1.25**

Four of five components of the LEI had a negative reading in the third quarter. Recent weakness in the Minnesota Business Conditions survey (conducted by Creighton University), which serves as a general measure of statewide business conditions, was the one of the indicators with a negative value in this quarter's index. Higher initial claims for unemployment insurance in recent months, decreased new filings of incorporation and LLC in the Southeast Minnesota planning area and a lower number of Rochester metro area residential building permits also weighed on the leading index. The consumer sentiment component of the LEI was neutral.

SCSU Southeast Minnesota Leading Economic Indicators Index

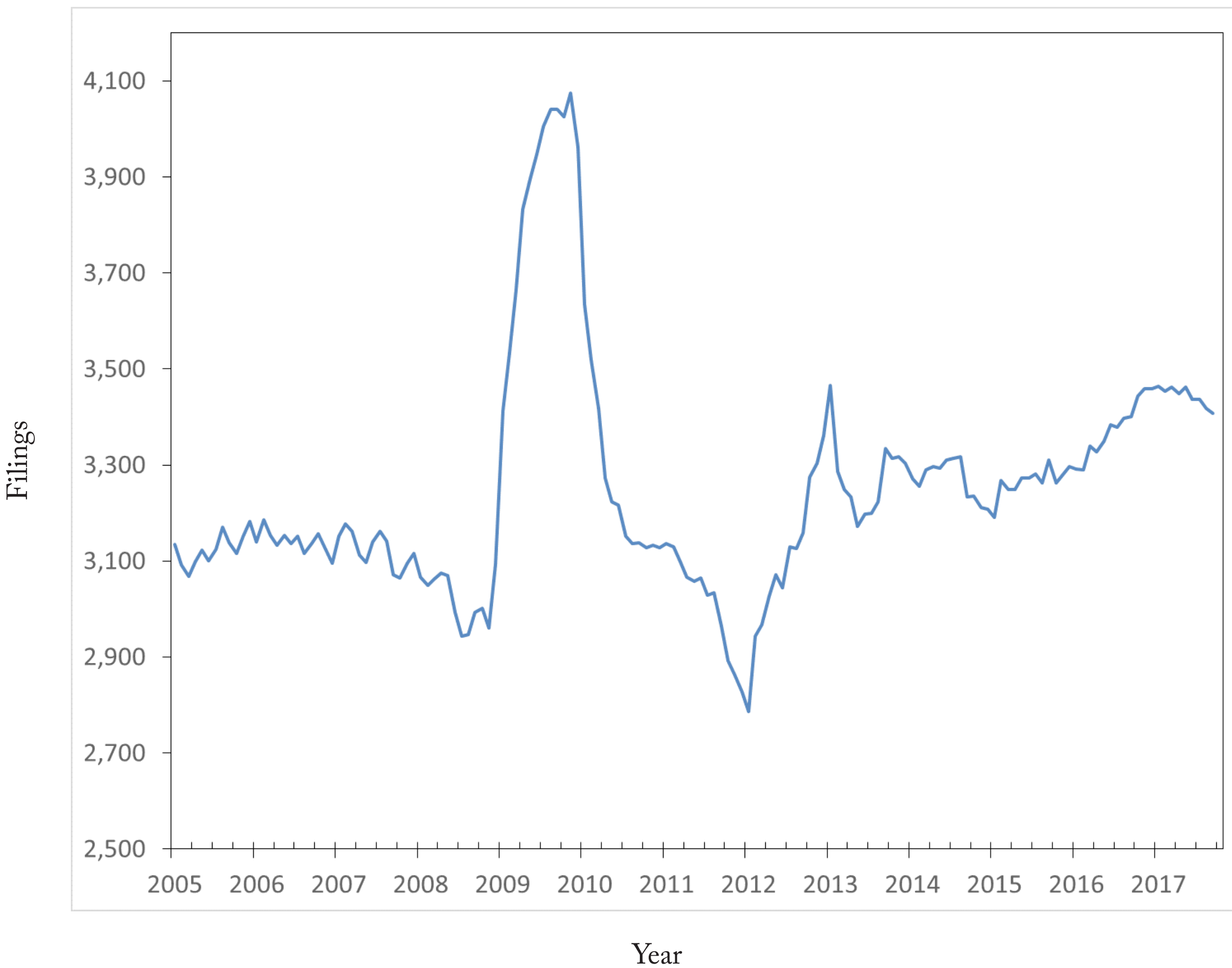
	2016	2015	Percentage change
Minnesota Business Conditions Index September	59.4	48.4	22.7%
Southeast Minnesota initial claims for unemployment insurance September	947	994	-4.7%
Southeast Minnesota new filings of incorporation and LLCs Third Quarter	514	584	-12.0%
Rochester MSA single-family building permits September	40	62	-35.5%
Consumer Sentiment, University of Michigan September	95.1	91.2	4.3%
Southeast Minnesota Leading Economic Indicators Index September (December 1999 = 100)	101.5	94.3	7.6%

SOUTHEAST MINNESOTA BUSINESS FILINGS

Third quarter new business filings fell 3.5 percent to a level of 792. As can be seen in the accompanying graph, the 12-month moving total of new business filings in Southeast Minnesota had trended upward since the end of 2014, but the series has begun to decline in 2017. 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.

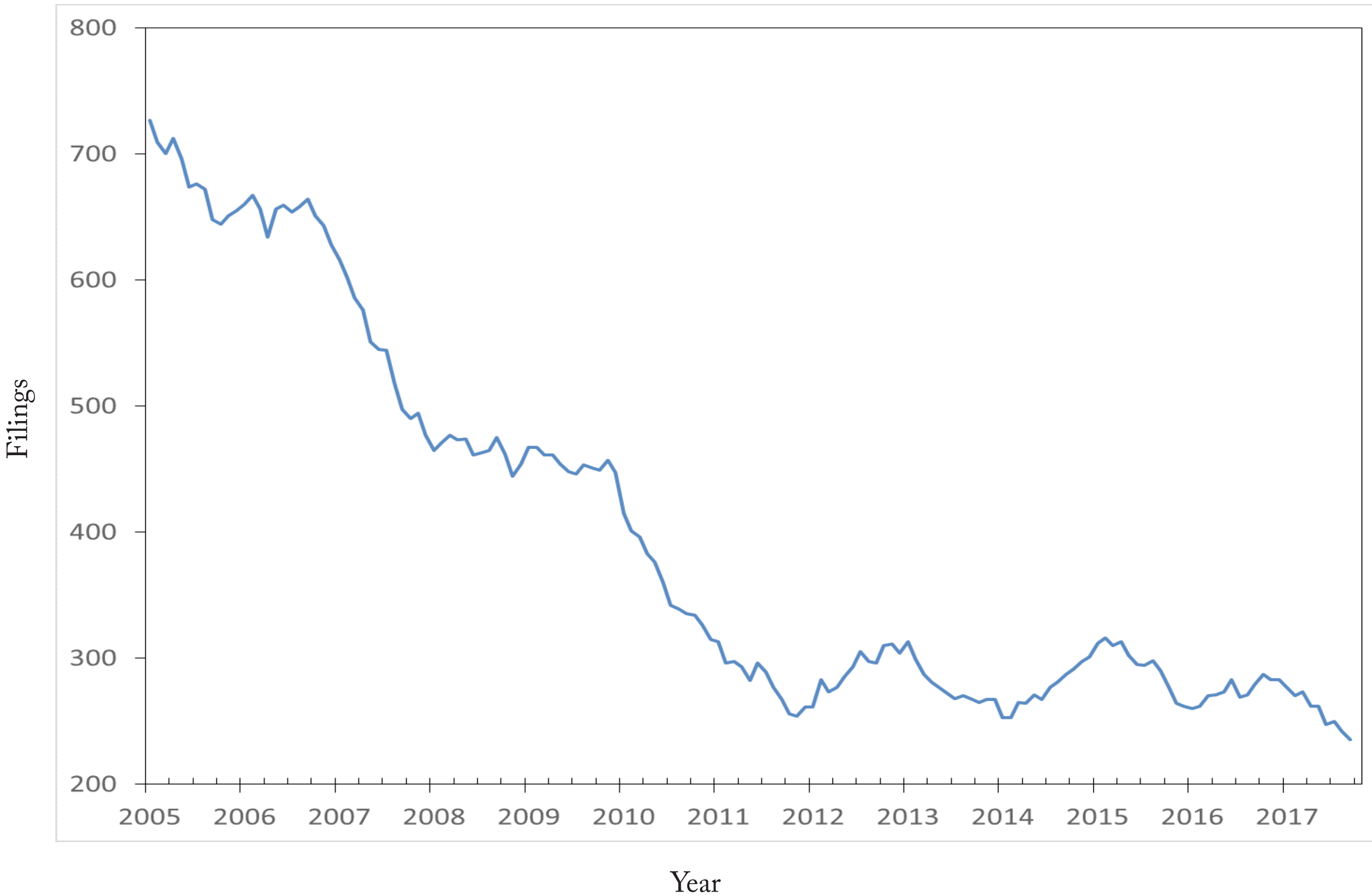
Total New Business Filings—Southeast Minnesota Planning Area (12-month moving total)



Quarter	III: 2016	IV: 2016	I: 2017	II: 2017	III: 2017	2017 Quarter III: Percent change from prior year
Southeast Minnesota Total New Business Filings	821	798	932	886	792	-3.5%

New business incorporations have slowly trended downward in Southeast Minnesota since the beginning of 2015. New incorporations fell 18.5 percent from year earlier levels in the most recent quarter.

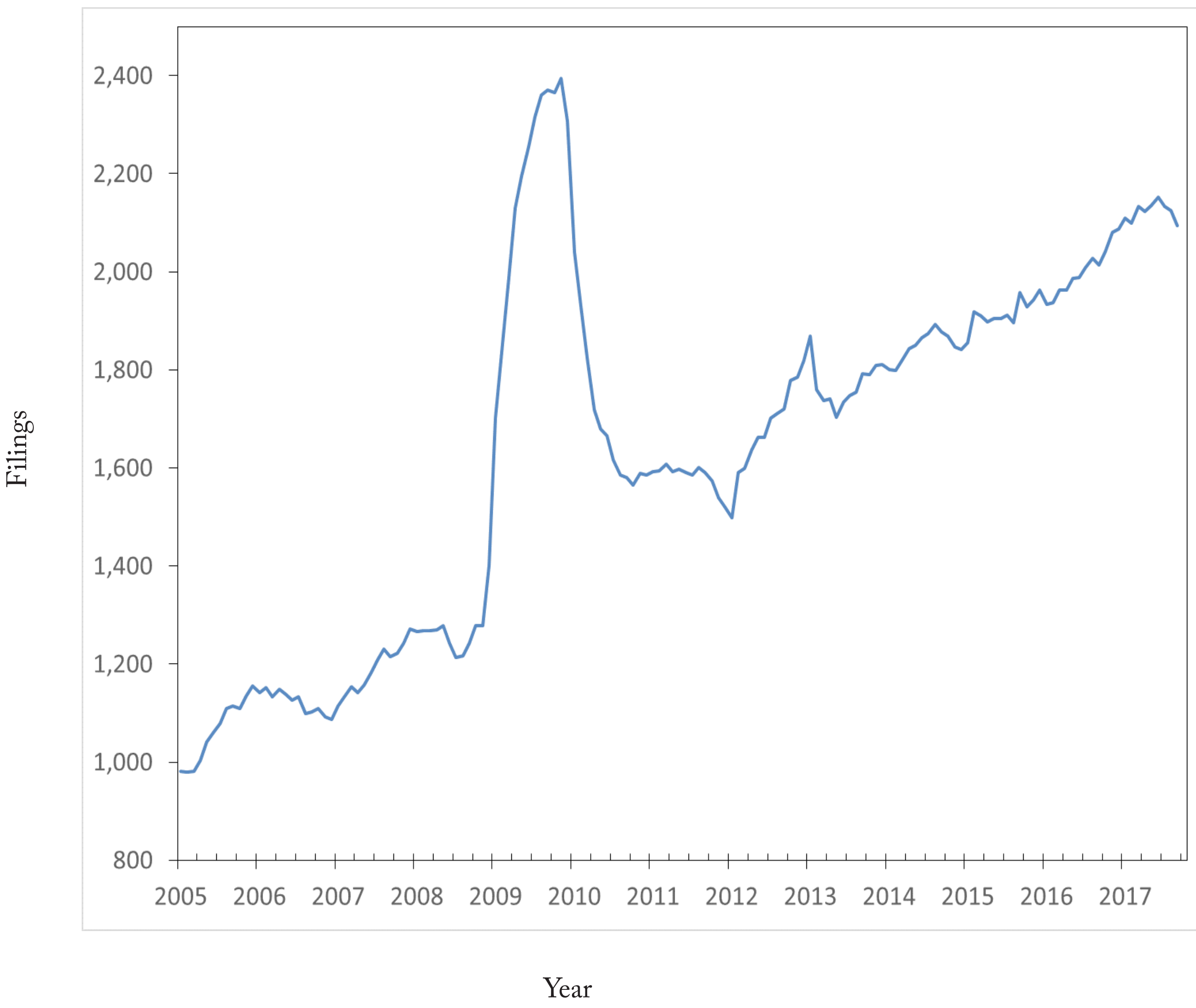
New Incorporations—Southeast Minnesota Planning Area (12-month moving total)



Quarter	III: 2016	IV: 2016	I: 2017	II: 2017	III: 2017	2017 Quarter III: Percent change from prior year
Southeast Minnesota New Business Incorporations	65	65	70	47	53	-18.5%

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. However, third quarter LLC filings fell by 11.2 percent over their year earlier level and the 12-month moving total of this series is starting to show a downward movement for the first time in several years.

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



Quarter	III: 2016	IV: 2016	I: 2017	II: 2017	III: 2017	2017 Quarter III: Percent change from prior year
Southeast Minnesota New Limited Liability Companies	519	493	585	555	461	-11.2%

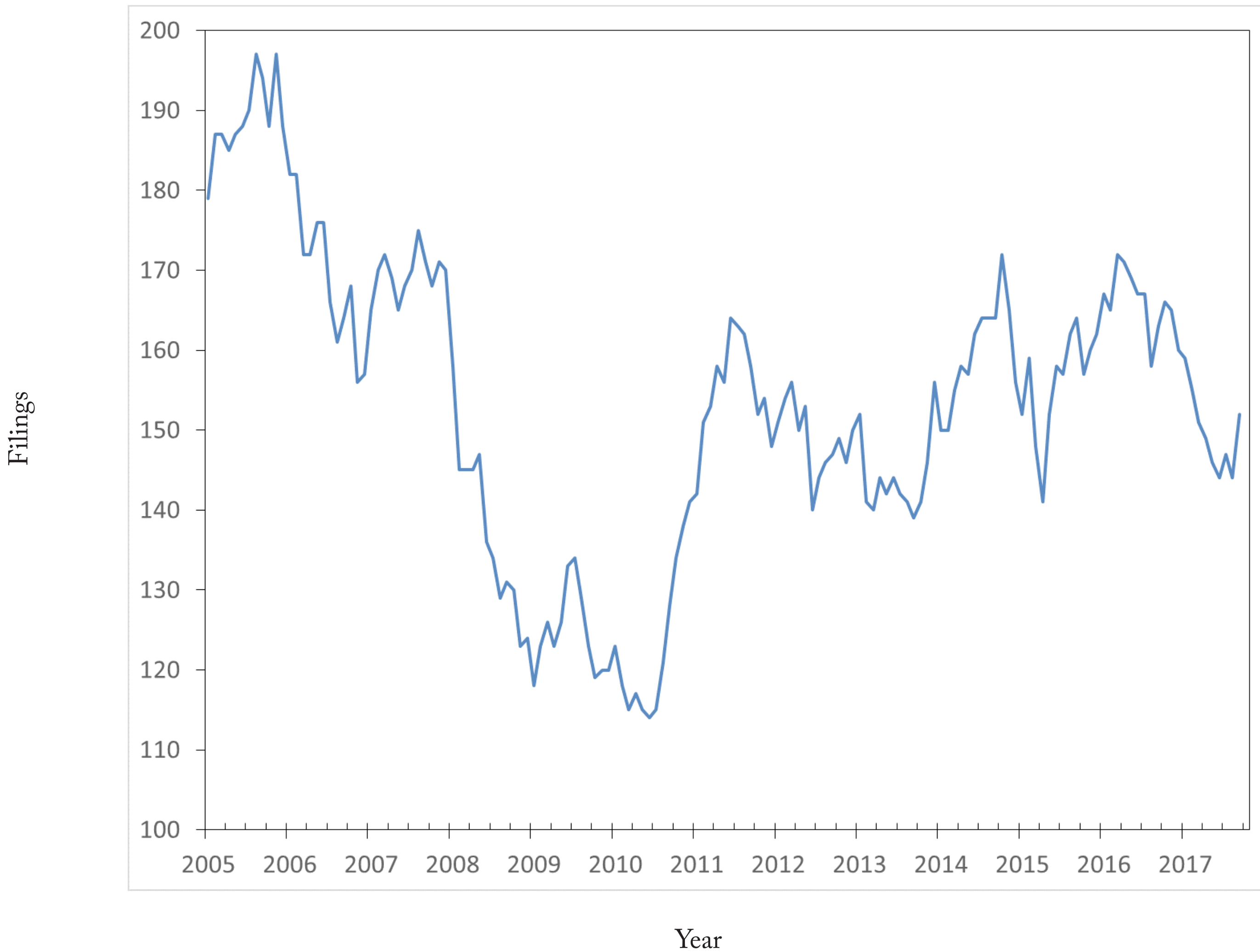
On a year over year basis, assumed names, which include sole proprietors or organizations that do not have limited liability, increased by 16.7 percent in Southeast Minnesota in the third quarter. As can be seen in the accompanying graph, after increasing in 2012, this series moved downward until the beginning of 2015, at which time it started to level out.

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

Quarter	III: 2016	IV: 2016	I: 2017	II: 2017	III: 2017	2017 Quarter III: Percent change from prior year
Southeast Minnesota New Assumed Names	198	205	246	245	231	16.7%

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 had turned downward since the beginning of 2016, but inched upward in the third quarter. The number of newly formed non-profits totaled 47 in the recent quarter (a 20.5 percent increase from the third quarter of 2016).

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



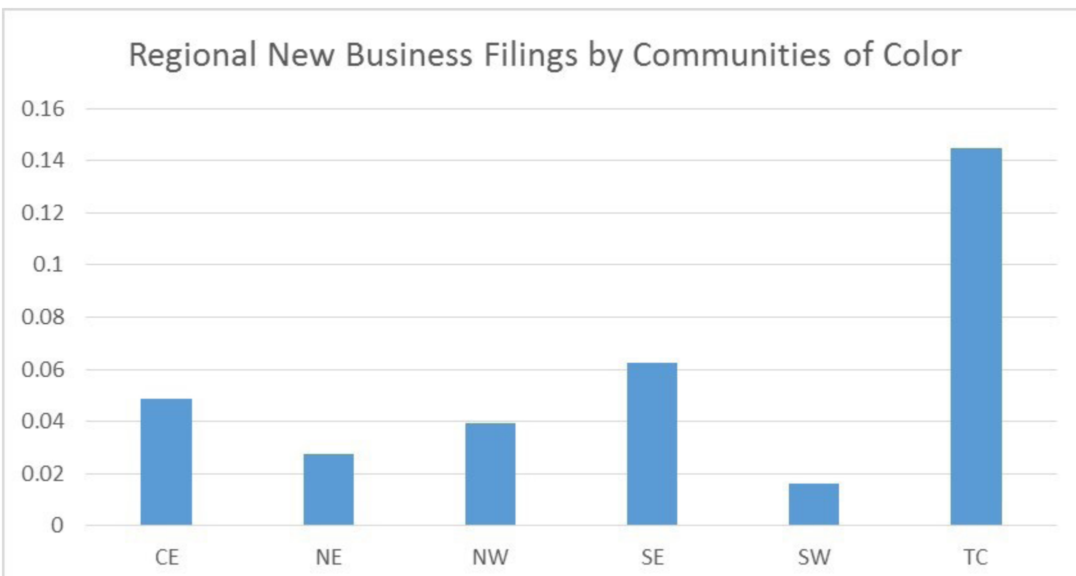
Quarter	III: 2016	IV: 2016	I: 2017	II: 2017	III: 2017	2017 Quarter III: Percent change from prior year
Southeast Minnesota New Non-Profits	39	35	31	39	47	20.5%

MINNESOTA BUSINESS SNAPSHOT SURVEY RESULTS

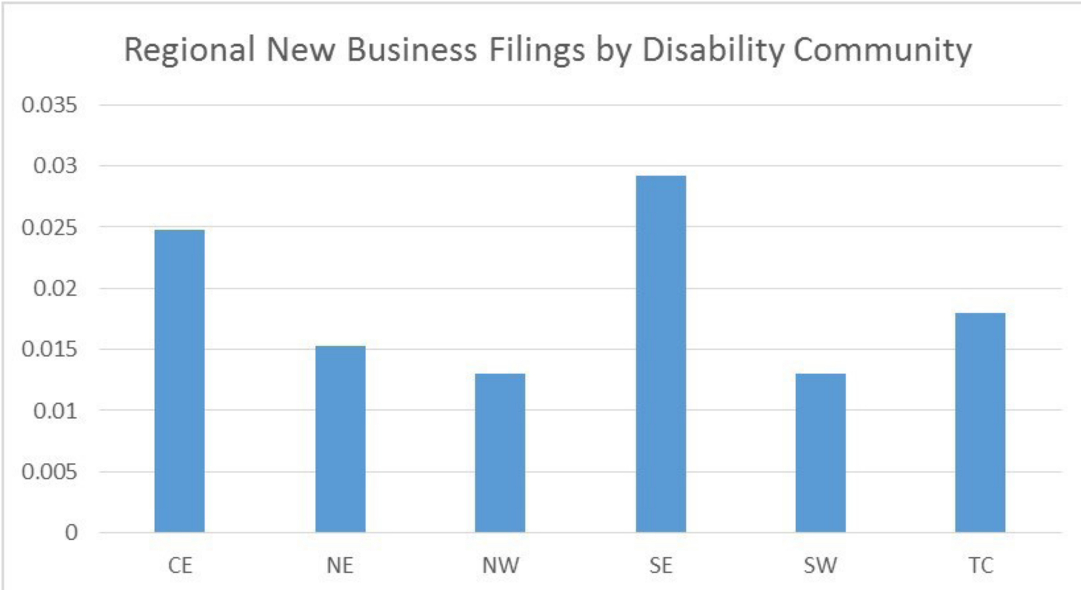
In Fall 2016, the Office of the Minnesota Secretary of State initiated a short voluntary survey (known as Minnesota Business Snapshot) for both new and continuing business filers. Questions found in the survey address basic questions related to the background of business filers, industry classification, employment levels and annual revenue of the filer, and whether the business is a full- or part-time activity for the filing entity. While a comprehensive analysis of this promising new data set is the beyond the scope of this regional economic and business conditions report, the survey results do provide useful additional background information to complement the business filing data.

To match up the Minnesota Business Snapshot (MBS) information with the data analyzed in this report, only surveys accompanying new filings in the third quarter of 2017 are analyzed. For the entire State of Minnesota, the overall response rate for this voluntary survey is approximately 61 percent. This yields thousands of self-reported records in this emerging data set. For Southeast Minnesota, slightly more than 60 percent of new business filers completed at least some portion of the MBS survey. The results are reported in this section.

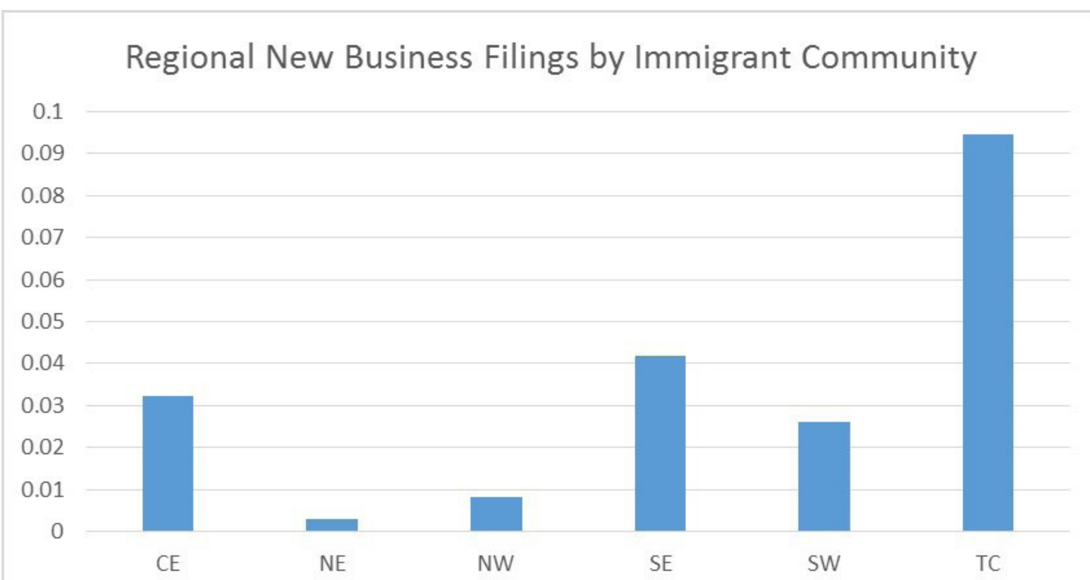
About 6.2 percent of those new filers completing the MBS from the Southeast Minnesota planning area report being from a community of color. This is a considerably lower percentage than in the Twin Cities, but is higher than all other outstate regions of Minnesota.



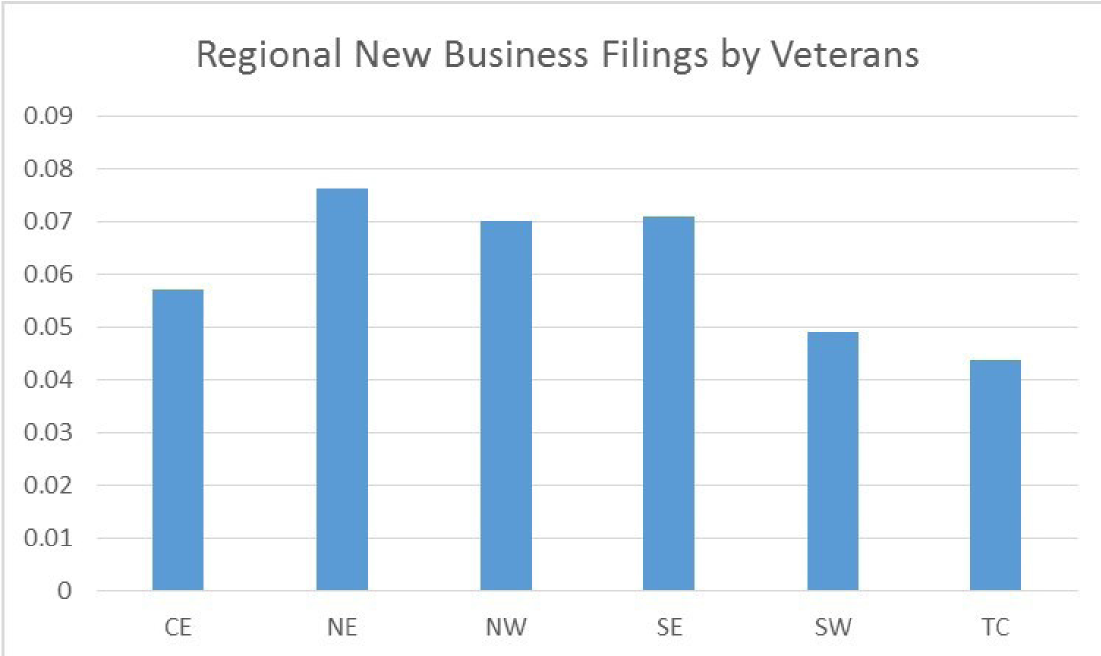
A little under 3 percent of Southeast Minnesota's new filers are from the disability community.



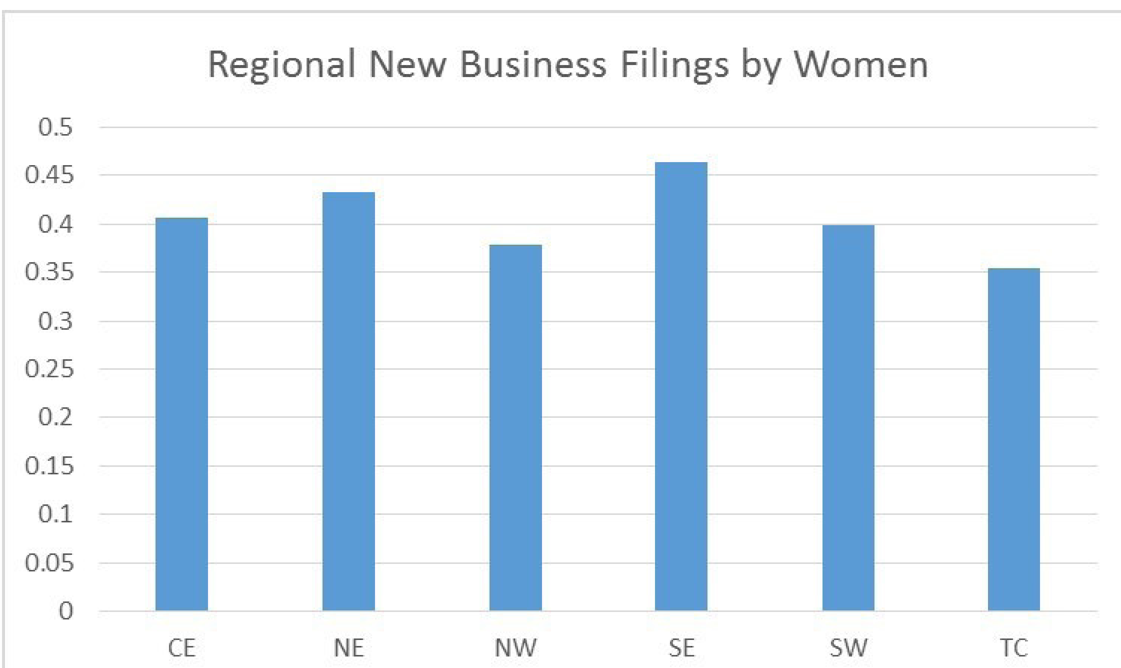
Almost 4.2 percent of new business filings in Southeast Minnesota come from the immigrant community. This is a much larger percentage than is found in the northeast and northwest portions of the state.



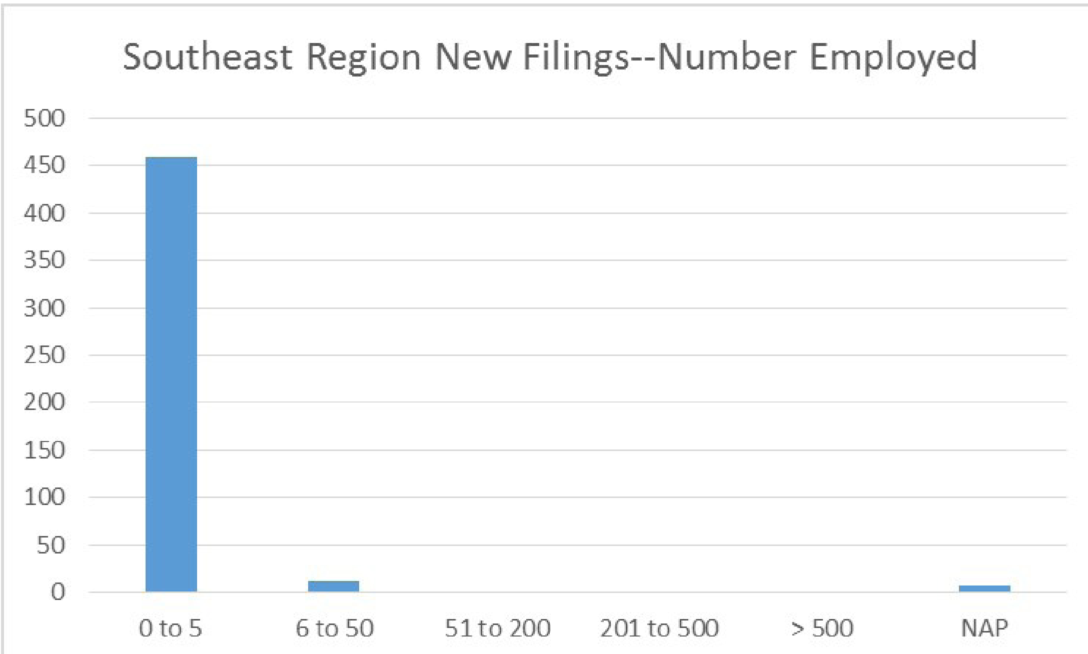
A little over 7 percent of new filings in Southeast Minnesota come from military veterans.



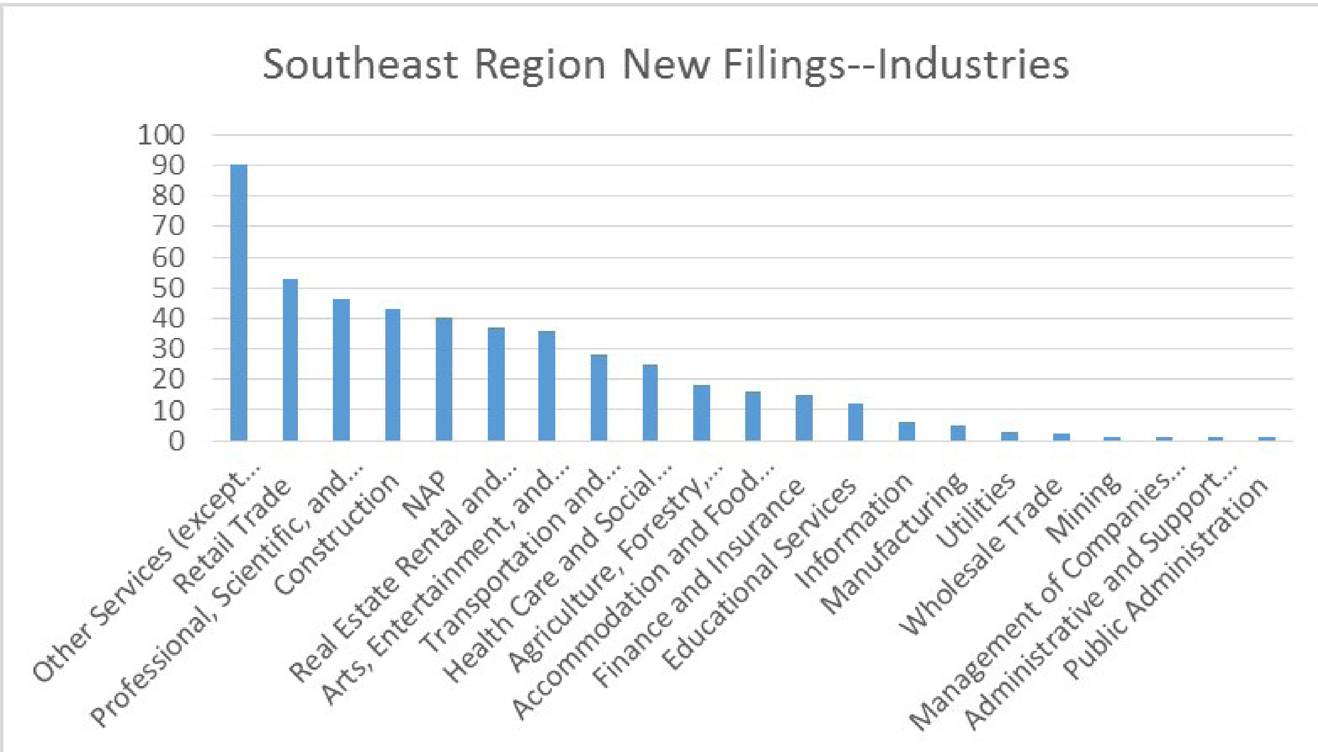
Woman owners represented 46 percent of the new business filings in Southeast Minnesota in the third quarter of 2017. This is the largest percentage of female new business filers in the state.



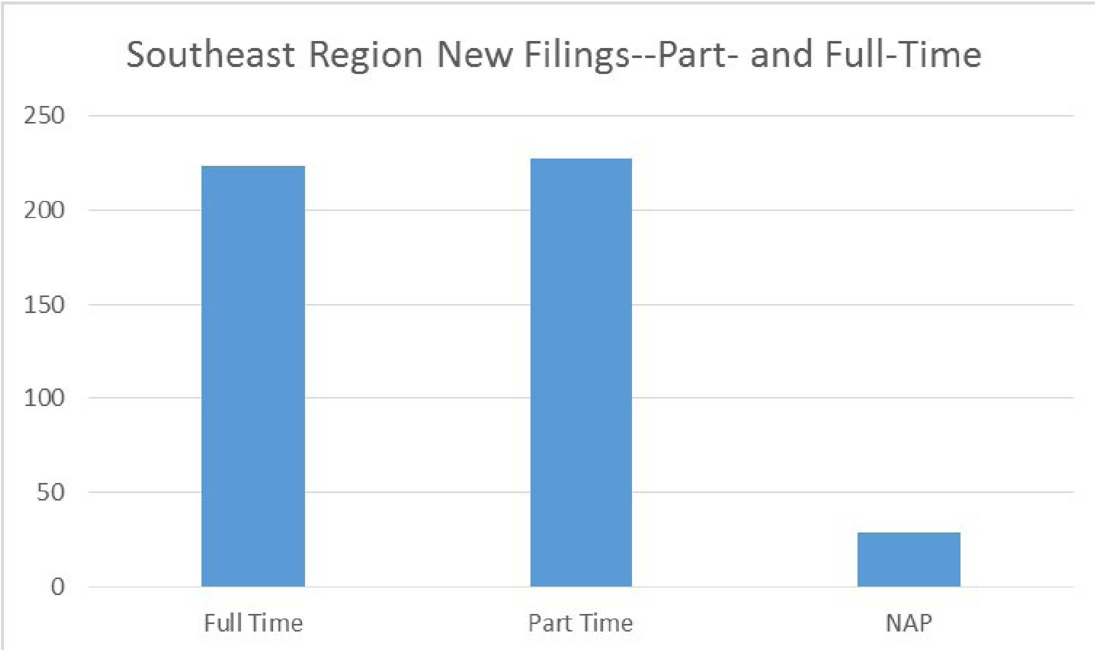
While not all of those participating in the survey completed all portions of the Minnesota Business Snapshot (those not responding to a particular question are represented in this section by "NAP"—no answer provided), 472 responses were tallied to a question asking the new business filer to indicate the range of employment at the business. As expected, most new businesses start small—employment at most companies submitting a new filing ranges from 0-5 employees.



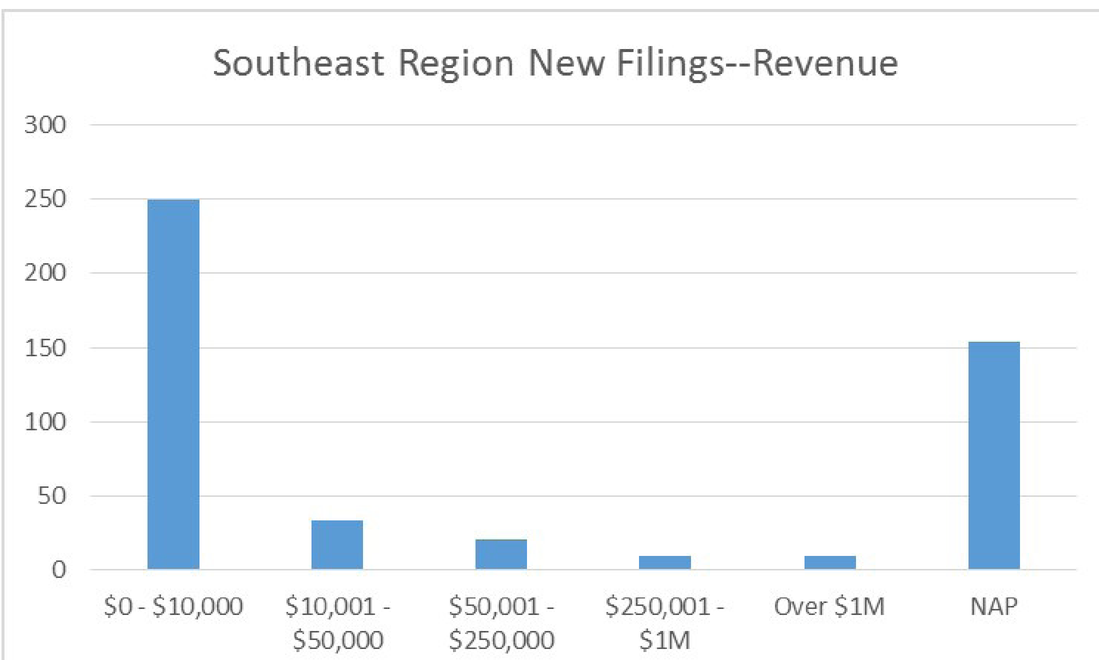
Using the North American Industry Classification System (NAICS), businesses submitting new filings were asked to identify the industry in which their company was operating. While a range of industries were reported, retail trade, professional/scientific/technical, construction and "other services" lead the way. Since businesses are often unsure of their industrial classification, the "other services" category is likely to represent a "catch-all" category for service-related businesses who were unable to specify their industry. Forty new firms did not provide an answer to this survey item (see "NAP")



A little over fifty percent of those submitting a new business filing in Southeast Minnesota in the third quarter of 2017 are part-time business owners.



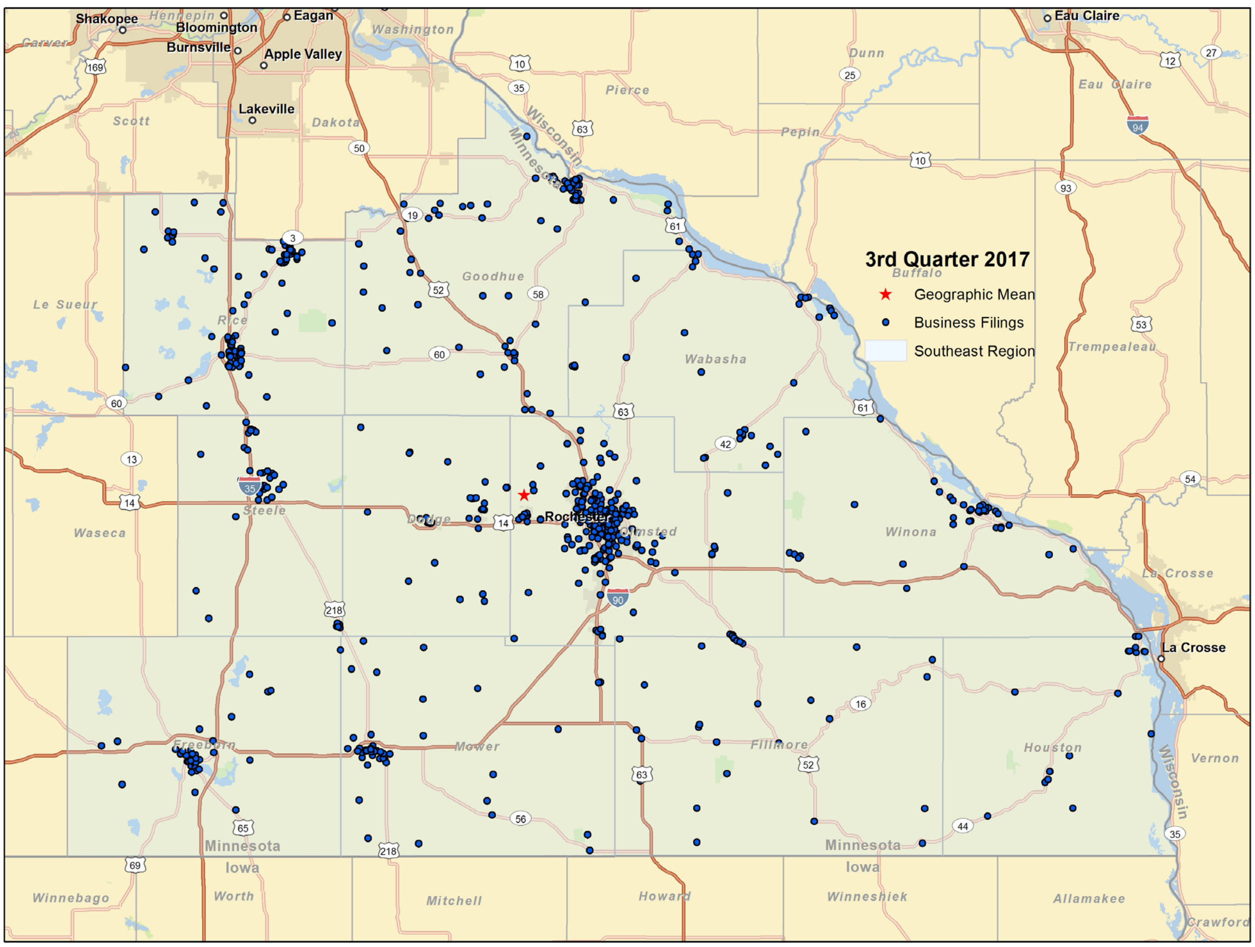
One hundred fifty-four new filers in Southeast Minnesota did not provide an answer to the MBS item that asked them to report the company's revenue. Of those businesses that answered the question, the largest share report revenues less than $10,000. Forty-one firms report annual revenues in excess of $50,000.



MAPS

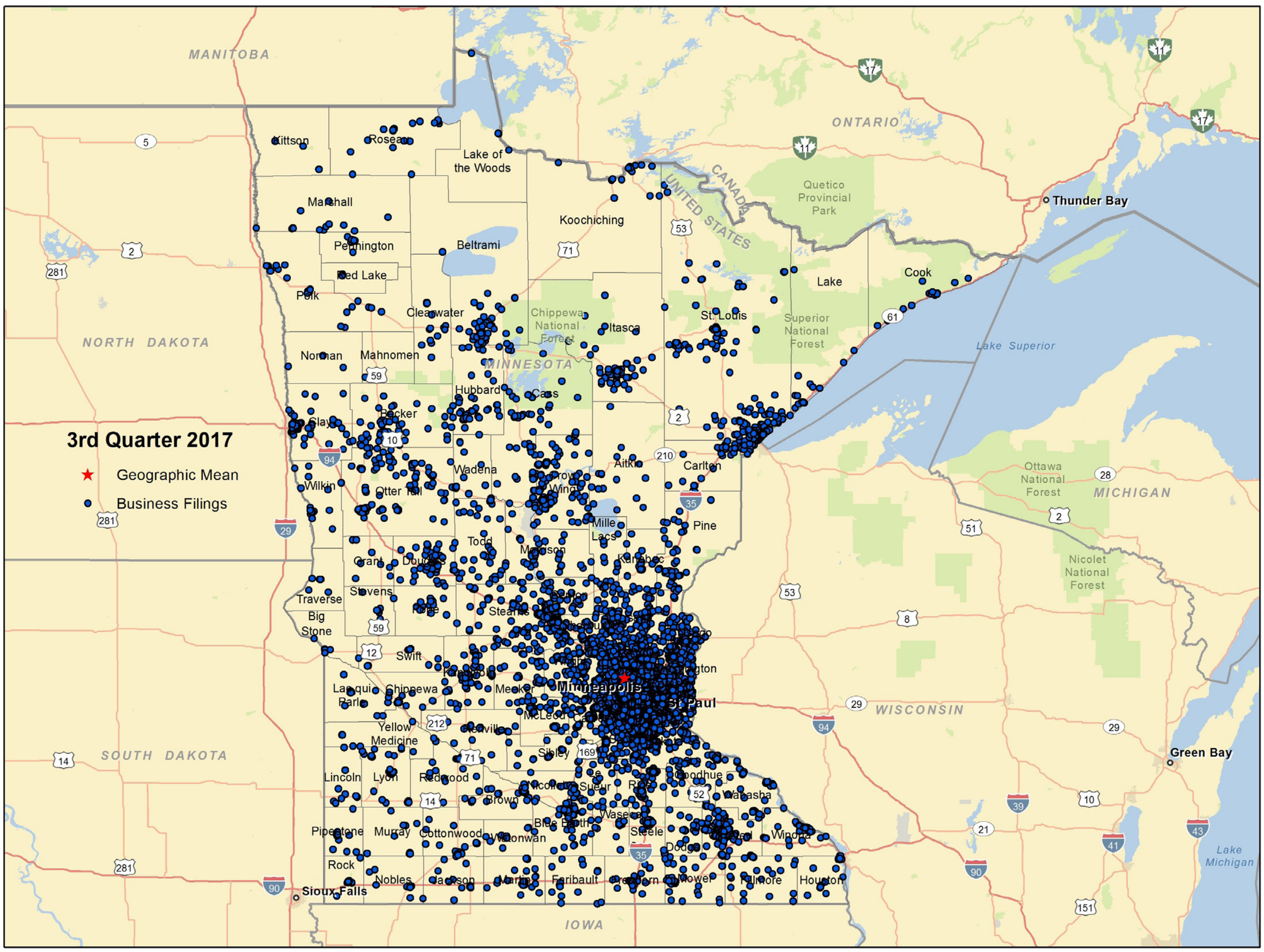
The first map shown below is a visual representation of new business filings around the Southeast Minnesota planning area in the third quarter of 2017. The densest areas of new business formation are in the Rochester metro. Owatonna, Faribault, Northfield, Albert Lea, Austin, and Red Wing also generated 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 3: 2017



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. The importance of Interstates 90 and 35 as well as US-10 and MN 61 (along the North Shore) in new business filings is also easily seen in this map.

Minnesota--New Business Formation--Quarter 3: 2017

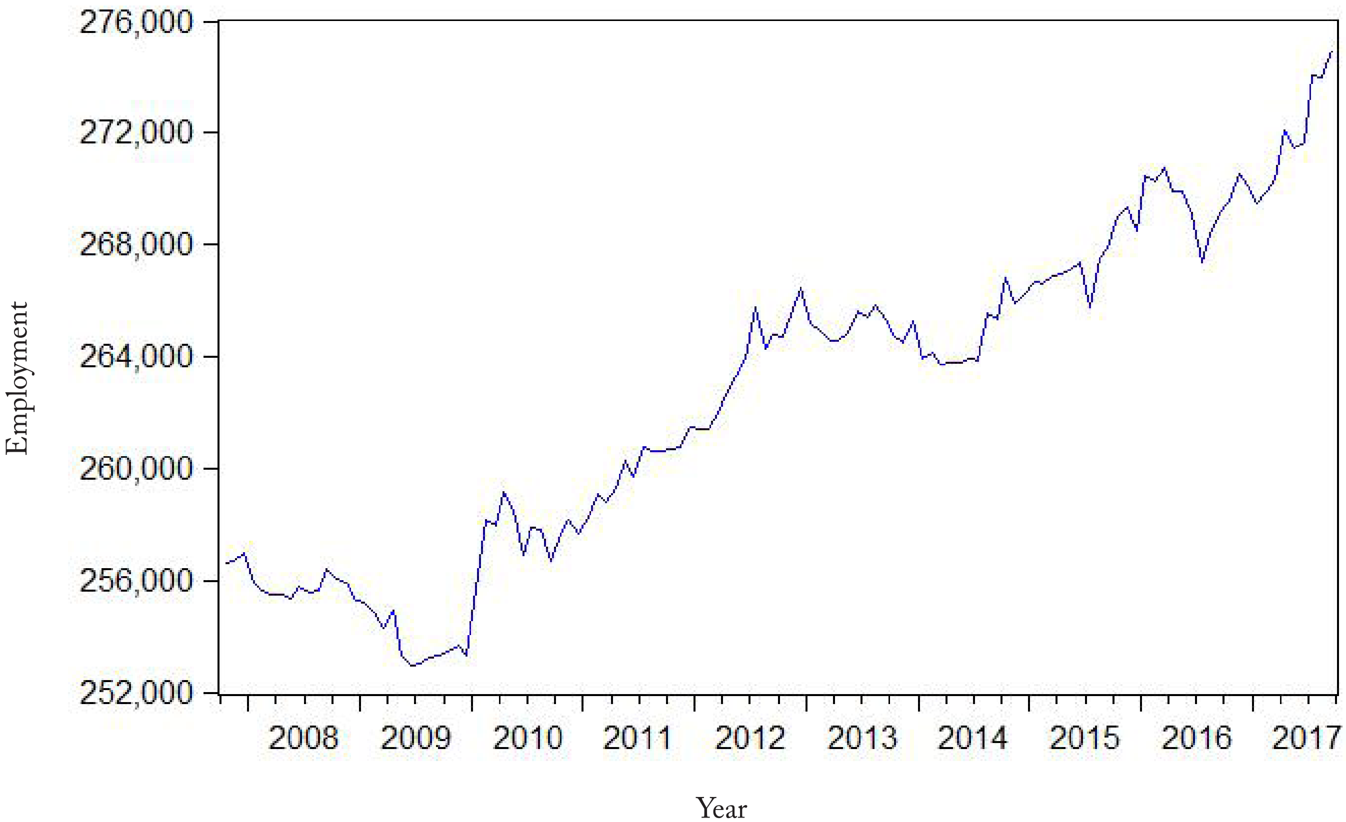


SOUTHEAST MINNESOTA LABOR MARKET CONDITIONS

Employment of those living in the Southeast Minnesota planning area rose by 2.2 percent over the past year. As shown in the accompanying graph, the 12-month moving average of total employment has been trending upward (with some brief interruptions) since the end of the Great Recession.

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	September 2016	April 2017	May 2017	June 2017	July 2017	August 2017	September 2017
Employment (Not seasonally adjusted)	268,806	271,373	271,675	273,567	277,235	275,247	274,609

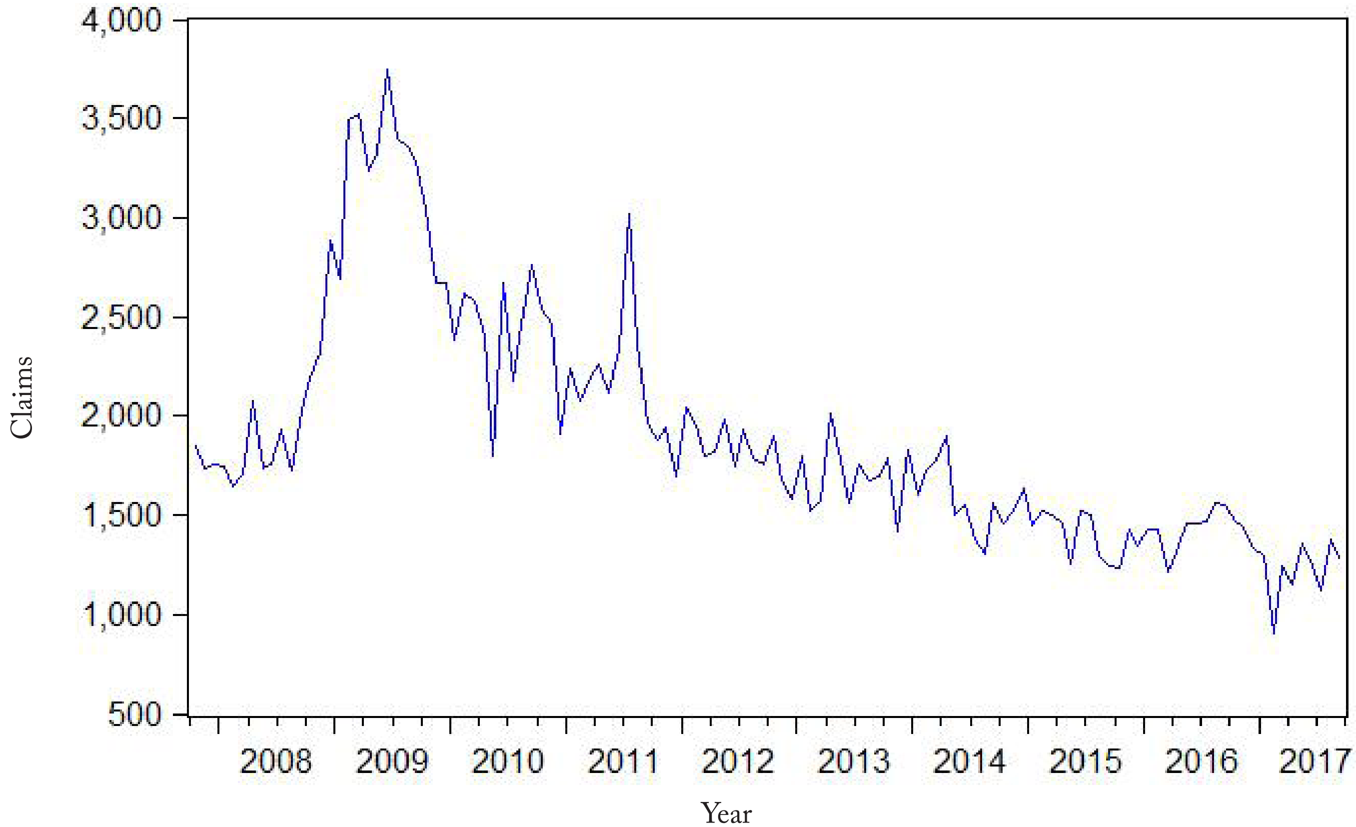
The seasonally adjusted unemployment rate in Southeast Minnesota has been declining since the end of 2016. The non-seasonally adjusted unemployment rate stands at 2.6 percent, lower than the 3.2 percent rate observed one year ago.

Unemployment Rate, seasonally adjusted—Southeast Minnesota Planning Area

Month	September 2016	April 2017	May 2017	June 2017	July 2017	August 2017	September 2017
Unemployment Rate (Not seasonally adjusted)	3.2%	3.2%	3.0%	3.4%	3.1%	3.2%	2.6%

New claims for unemployment insurance in September 2017 were 17.8 percent lower than one year earlier. On a seasonally adjusted basis, these claims have leveled out in 2017.

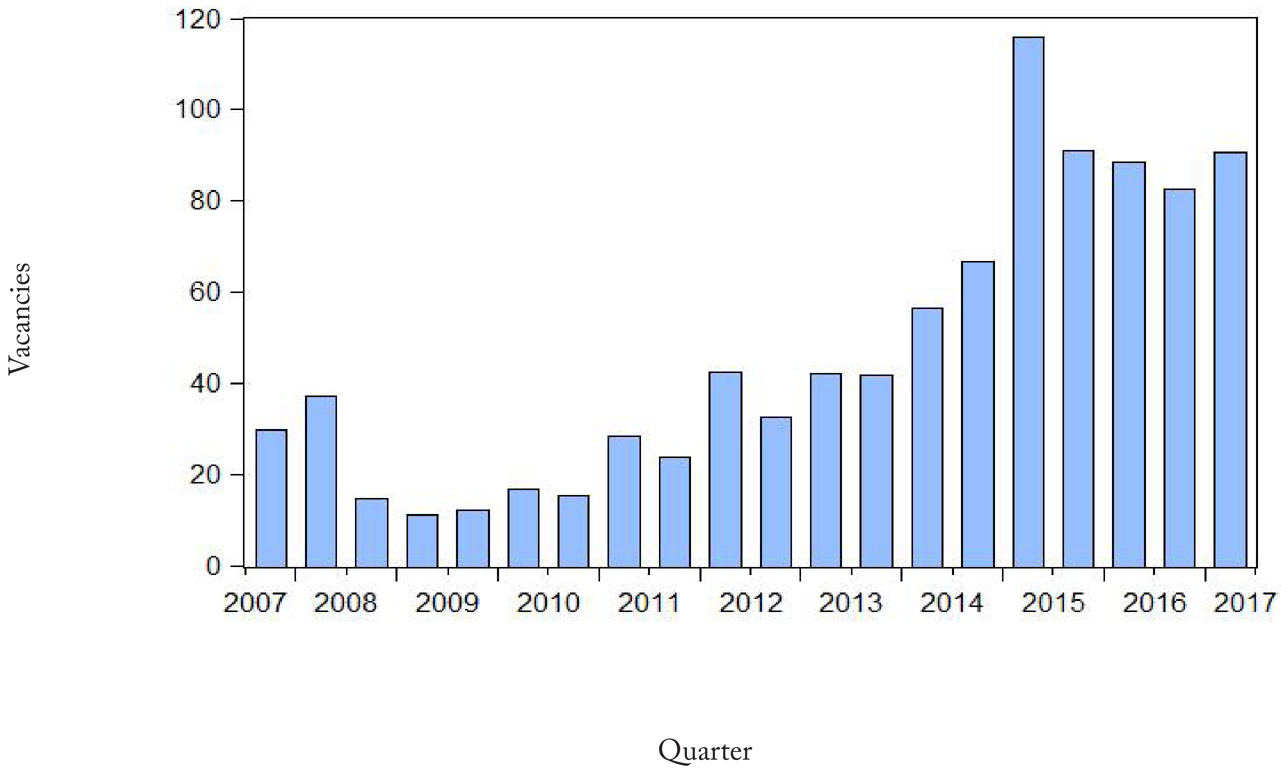
Total Initial Claims for Unemployment Insurance, seasonally adjusted—Southeast Minnesota Planning Area



Period	September 2016	April 2017	May 2017	June 2017	July 2017	August 2017	September 2017
Initial claims (Not seasonally adjusted)	994	779	1,086	1,120	850	867	817

The ratio of job vacancies per 100 unemployed increased slightly in Southeast Minnesota in the second quarter of this year. While a rising labor force in the region may be helping to relieve some of the strain on area employers who are looking for qualified workers, this ratio is now 95.23 job vacancies per 100 unemployed. It is worth noting that all of Minnesota's regions are experiencing high job vacancy ratios. In fact, the Twin Cities, Northeast, and Southwest Minnesota planning areas have job vacancy ratios in excess of 100, suggesting that even if those on unemployment rolls were a match with available jobs, employers would still be unable to fill all of their job vacancies in these regions.

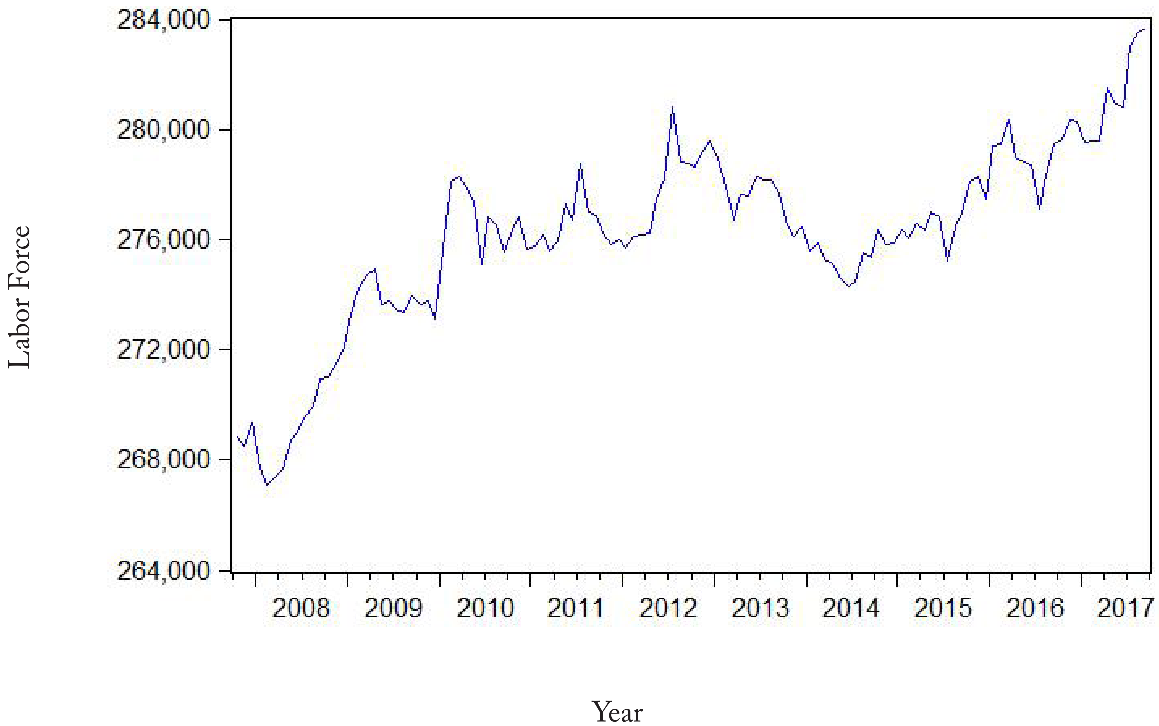
Job Vacancies per 100 Unemployed---Southeast Minnesota Planning Area



Quarter	2014:IV	2015:II	2015:IV	2016:II	2016:IV	2017:II
Job Vacancies per 100 Unemployed	78.35	120.65	105.28	91.73	94.44	95.23

The Southeast Minnesota labor force increased by 1.5 percent over the last year. The 12 month moving average of the regional labor force has steadily increased since the beginning of 2014 and is now at its highest level of the past decade.

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

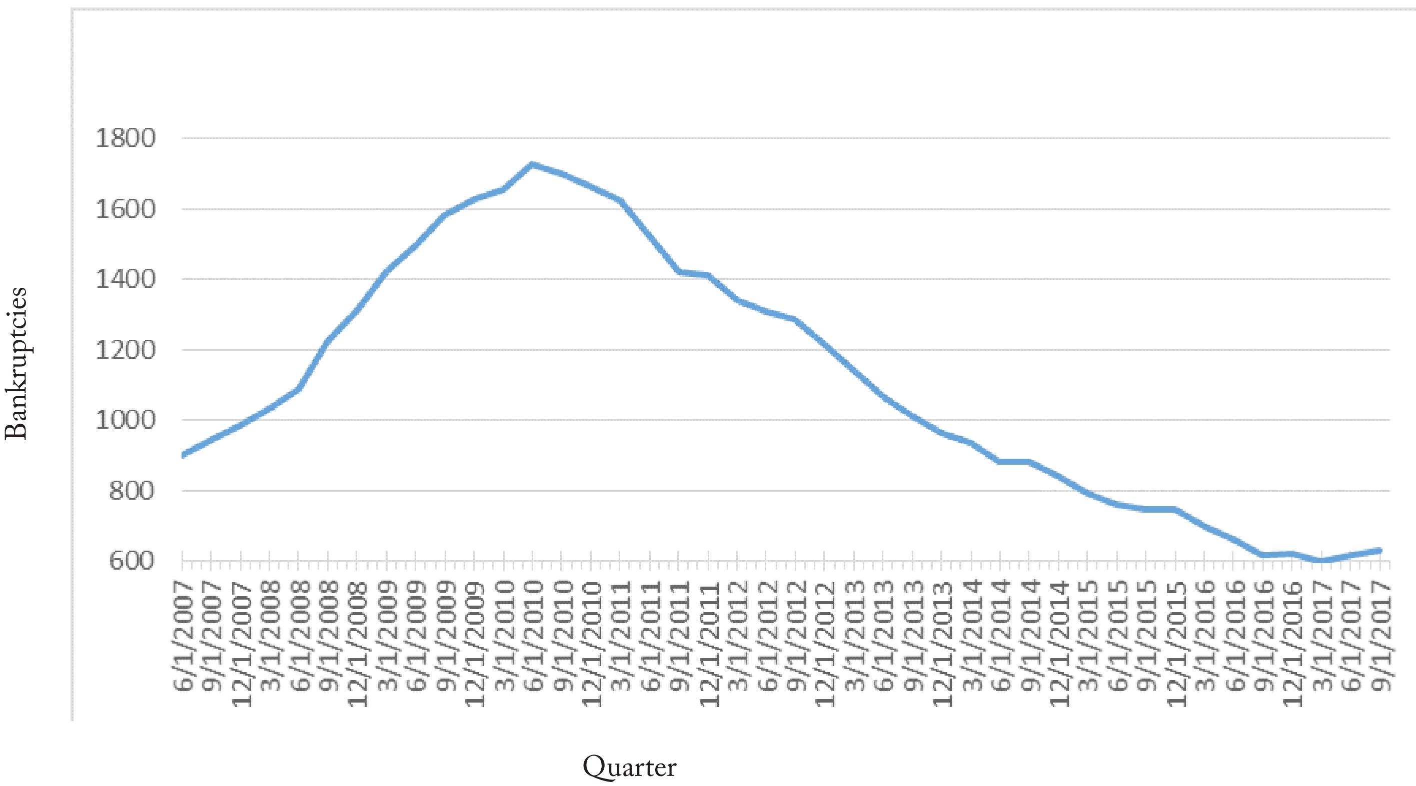


Year (September)	2012	2013	2014	2015	2016	2017
Labor Force (Not seasonally adjusted)	277,532	276,355	273,889	275,375	277,689	281,854

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 steadily declined until the beginning of this year. With 629 bankruptcies over the past twelve months, bankruptcies in Southeast Minnesota rose slightly from last quarter's annual total of 617.

Southeast Minnesota Bankruptcies (12-month moving total)



Year (Third Quarter)	2012	2013	2014	2015	2016	2017
Annual Bankruptcies (not seasonally adjusted)	1,288	1,011	883	749	618	629

ECONOMIC INDICATORS

Rochester MSA Indicators	Period Covered	Current Period	Prior Year	Annual Percent Change		Long-Term Average (since 1999, unless noted)	
Labor Market							
Employment	September 2017 (m)	120,094	119,209	0.7%	↑	0.9%	
Manufacturing Employment	September 2017 (m)	11,017	10,866	1.4%	↑	-2.7%	
Educational and Health Employment	September 2017 (m)	48,478	48,340	0.3%	↑	2.6%	
Average Weekly Work Hours Private Sector	September 2017 (m)	34.1	34.0	0.3%	↑	33.2	
Average Earnings Per Hour Private Sector	September 2017 (m)	$35.94	$34.16	5.2%	↑	3.9%	
Unemployment Rate	September 2017 (m)	2.5%	3.1%	NA	↓	3.7%	
Labor Force	September 2017 (m)	119,804	118,212	1.3%	↑	0.6%	
Initial Jobless Claims	September 2017 (m)	318	417	-23.7%	↓	NA	
Business Formation							
Total New Business Filings	Third Quarter 2017 (q)	389	413	-5.8%	↓	331	(since 2000)
New Business Incorporations	Third Quarter 2017 (q)	23	33	-30.3%	↓	45	(since 2000)
New Limited Liability Companies	Third Quarter 2017 (q)	229	268	-14.6%	↓	156	(since 2000)
New Assumed Names	Third Quarter 2017 (q)	116	94	23.4%	↑	110	(since 2000)
New Non-profits	Third Quarter 2017 (q)	21	18	16.7%	↑	19	(since 2000)
Rochester Residential Building Permit Valuation, in thousands	September 2017 (m)	36,437	25,328	43.9%	↑	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 0.7 percent in September 2017 and employment in the key education/health sector rose by 0.3 percent (which is well below the 2.6 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 29.9 percent in July 1999 to over 40 percent today. The overall number of new business filings decreased (as did new incorporations and LLCs), but the value of residential building permits rose in the Rochester area during the most recent reporting period. Average hourly earnings were higher and average weekly work hours rose. The unemployment rate was lower and the labor force grew.

STATE AND NATIONAL INDICATORS

MINNESOTA Indicators	Sep 2017	Jun 2017	Sep 2016	Change from one quarter ago	Annual Change
Nonfarm payroll employment, SA	2,955,300	2,952,100	2,903,100	0.1%	1.8%
Average weekly hours worked, private sector	34.1	34.2	34.1	-0.3%	0.0%
Unemployment rate, seasonally adjusted	3.7%	3.7%	4.0%	NA	NA
Earnings per hour, private sector	$28.59	$27.94	$27.32	2.3%	4.6%
Philadelphia Fed Coincident Indicator, MN	199.61	198.65	192.95	0.5%	3.5%
Philadelphia Fed Leading Indicator, MN	1.76	1.66	0.86	6.0 %	104.7%
Minnesota Business Conditions Index	59.4	68.0	48.4	-12.6%	22.7%
Price of milk received by farmers (cwt)	$17.90	$17.50	$17.90	2.3%	0%
Enplanements, MSP airport, thousands	1,522.7	1,738.8	1,536.1	-12.4%	-0.9%
NATIONAL Indicators	Sep 2017	Jun 2017	Sep 2016	Change from one quarter ago	Annual Change
Nonfarm payroll employment, SA, thousands	146,749	146,385	144,882	0.2%	1.3%
Industrial production, index, SA	104.6	105.2	103.0	-0.6%	1.6%
Real retail sales, SA ($)	196,407	194,630	192,238	0.9%	2.2%
Real personal income less transfers, billions	12,096.5	12,062.7	11,922.9	0.3%	1.5%
Real personal consumption expenditures, bill.	11,969.8	11,871.6	11,656.3	0.8%	2.7%
Unemployment rate, SA	4.2%	4.4%	4.9%	NA	NA
New building permits, SA, thousands	20,470	25,160	20,857	-18.6%	-1.9%
Standard & Poor's 500 stock price index	2,492.8	2,434.0	2,157.7	2.4%	15.5%
Oil, price per barrel in Cushing, OK	$49.82	$45.18	$45.18	10.3%	10.3%

For the state as a whole, most categories of economic performance found in the State and National Indicators table are favorable. There was growth in payrolls, higher earnings per hour, and a lower seasonally adjusted unemployment rate compared to last quarter as well as one year ago. Coincident and leading indicators from the Federal Reserve Bank of Philadelphia are each higher than last quarter and last year, but the Minnesota Business Conditions index slipped in the last quarter (but is still well above its level from one year ago). Milk prices were flat over the past year, although they did increase 2.3 percent in the past quarter. Enplanements at the Minneapolis-St. Paul airport were lower over the past year. Average weekly work hours were lower than three months ago and were unchanged from September 2016.

The national economic indicators found in the table are also generally favorable. Over the past quarter as well as the past year, stock prices rose, employment increased, real income and consumer expenditures expanded, and retail sales picked up. The national unemployment rate also fell. Industrial production rose over the past year, but declined from one quarter ago. National building permits were lower than in September 2016. Consumers also saw higher oil prices last quarter. Oil prices are now 10.3 percent higher than they were one year ago.

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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