THE MAINSTREET ECONOMY REPORT

July 2012

"A monthly survey of community bank CEO's"

The 25%, Not the 1%, Are Strangling the U.S. Economy:

It's not the 1 percent that is siphoning U.S. economic resources. It is the 25 percent--the portion of the U.S. population born between 1946 and 1964 or, baby boomers like me. Not only are we 25 percenters leaving the workforce at very high rates, (consuming instead of producing), we are draining the U.S. Treasury via higher Social Security (SS) benefits and greater Medicare spending. Over the past decade, SS outlays soared by 69 percent and Medicare expenditures rocketed by 135 percent, enlarging the nation's debt to $16 trillion. This debt which is the largest in the galaxy and 100 percent of GDP will ultimately be paid for by the 60 percenters (those born after 1964). We need to take steps to reduce this wealth transfer from young to old by: (1) raising the SS retirement age from 67 to 70 by increasing it 2 months per year, (2) increasing the Medicare eligibility age from 65 to 67 and, (3) cut the yearly SS infla-tion adjustment by 1 percent. Taking these actions would save $360-$400 billion between 2012 and 2021. Additionally to reverse the aging of the nation's labor market, the U.S. should expand legal immigration allowing younger workers and their families to enter the U.S. Latest U.S. Census data show the median age is 38.3 for Whites, 35.3 for Asians and 27.4 for Hispanics. By increasing legal immigration and slowing the growth in SS and Medicare spending, the U.S. would avoid the stagnation and looming economic calamities threatening Japan and Europe as a result of their aging populations and expanding pensions/healthcare payments to baby boomers. Ernie Goss.

MAINSTREET RESULTS

Rural Mainstreet Economic Growth Slows; Farmland Price Growth Lowest for Year

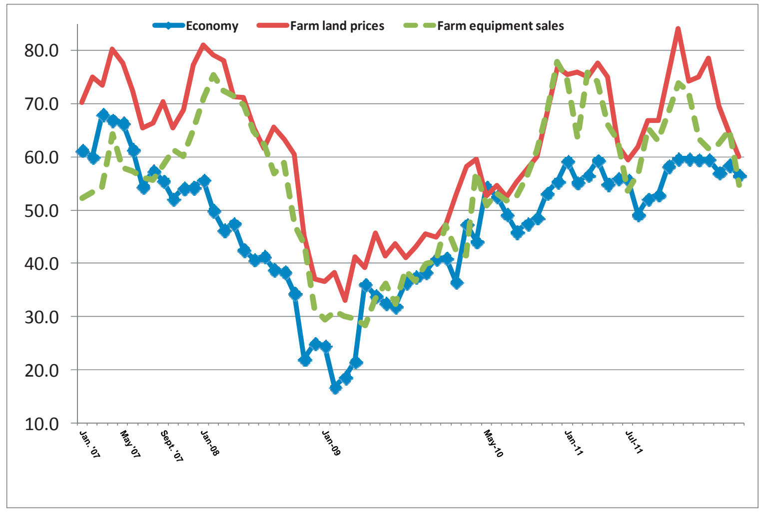
Tables 1 below summarizes the findings from the June survey with an index above 50.0 indicating growth and an index below 50.0 signifying weakness. [Index > 50.0 indicates expansion]

Table 1: The Mainstreet Economy	June 2011	May 2012	June 2012
Area Economic Index	56.0	58.5	56.7
Loan volume	59.0	56.9	64.2
Checking deposits	59.7	62.9	55.3
Certificate of deposits	41.7	41.7	38.9
Farm land prices	62.0	64.6	60.0
Farm equipment area sales	63.1	65.1	54.7
Home sales	53.0	65.2	66.4
Hiring in the area	51.5	59.2	59.1
Retail Business	47.0	54.7	54.6
Economy 6 months from now	55.3	60.2	58.5

June Survey Results at a Glance:

- Rural Mainstreet Index declines.
- Farmland prices continue to grow but at a slower pace.
- Almost 90 percent of bankers support removing food stamps from the new farm bill.
- Approximately 64 percent of bankers say the new farm bill should support agriculture and energy research.

Rural Mainstreet, Jan. '07 – June '12



The Rural Mainstreet Index (RMI) for June slumped to its lowest level in 2012. **Overall:** The Rural Mainstreet Index (RMI), which ranges between 0 and 100 with 50.0 representing growth neutral, declined to 56.7, its lowest level since October of last year, and down from last month's 58.5. Dale Bradley, CEO of Citizens State Bank in Miltonvale, Kans., said, "International economic problems are affecting us here (Rural Mainstreet economy)."

Our surveys point to slower but positive growth for the agriculturally and energy dependent areas of the nation. The global economic slowdown combined with a stronger U.S. dollar has pushed agriculture and energy prices lower. This is weakening overall growth for the Rural Mainstreet economy. Goss and Bill McQuillan, CEO of CNB Community Bank of Greeley, Neb., created the monthly economic survey in 2005.

Farming: According to the May survey farmland prices continue to head higher. However, for a third straight month, farmland price growth weakened with the June index dropping to 60.0, its lowest level since July of last year and down from last month's 64.6. Even so, this is the 29th consecutive month the index has been above growth neutral. The farm-equipment sales index sank to 54.7, its lowest level since July of last year and down significantly from last month's 65.1. Europe's economic turmoil has pushed the value of the U.S. dollar higher and agriculture prices lower. Over the past two months, for example, farm products have declined by 3 percent. This is slowing growth in the farm sector for both farmland and farm-equipment sales.

This month, bank CEOs were asked about changes in the new farm bill currently before Congress. Approxi-mately 87 percent supported separating the food stamps program from the 2012 farm bill. The bill under consideration includes spending for agriculture and energy research. Approximately 64 percent of the bankers support such spending while 16 percent are opposed to this spending. The remaining 19 percent expressed no opinion on this spending element. Pete Haddeland, CEO of First National Bank in Mahnomen, Minn., expressed a common theme saying, "The new farm bill should support the current crop insurance amounts."

Almost one fourth, 23.7 percent, of bankers with cattle operations in their area indicated that farmers were re-ducing the size of their herds due to dry weather, including Dan Coup, CEO of First National Bank in Hope, Kan., who reported that due to drought conditions, some ranchers were being forced to move cattle off of grass. He added, "Several ranchers are hauling water to cattle on grass due to lack of pond water. One rancher in Marion County lost 22 head of cattle caused by blue-green algae in his farm pond." Steven Lane, CEO of Security Savings Bank in Farnhamville, Iowa, said, "Dry conditions have not only affected cattle herds, they have affected land and equipment sales."

Banking: Farmers increased their demand for loans with the loan-volume index climbing to 64.2 from May's 56.9. This marks the fourth consecutive month the index has risen. The checking-deposit index sank to 55.3 from May's 62.9, while the index for certificates of deposit and other savings instruments slumped to 38.9 from 41.7 in May. As farmland prices and farm-equipment sales have risen, so have farmers' financing demands. Each month, farmers are reducing the amount of cash purchases of farmland and farm equipment and increasing the degree of bank financing.

Hiring: June's s hiring index dipped slightly to a still strong 59.1 from 59.2 in May. Job growth across the Rural Mainstreet economy continues to exhibit a great deal of geographic variation with strong growth in Colorado, Iowa, Kansas, Minnesota, and North Dakota. Employment growth was much weaker in rural Illinois, Missouri, Nebraska, South Dakota and Wyoming. Overall job growth in urban areas is currently double that in rural areas.

Confidence: The confidence index, which reflects expectations for the economy six months out, dipped to 58.5 from May's 60.2. European economic problems, weaker farm prices and slower global economic growth failed to significantly lower optimism among bankers in our survey regarding the outlook for their local economies.

Home and retail sales: For a second straight month, the June home-sales index rose to a record high at 66.4 from May's 65.2. The retail-sales index for June slipped slightly to 54.6 from 54.7 in May. The pace of sales for homes in the area is definitely picking up, much like it is urban areas of the country. As a result of strong farm income over the past couple of years, retail sales continue to expand. Bob Sutter, vice chair of Hilltop National Bank in Casper, Wyo., said, "Housing demand is high and we are seeing an increase in loan demand."

Each month, community bank presidents and CEOs in nonurban, agriculturally and energy-dependent portions of a 10-state area are surveyed regarding current economic conditions in their communities and their projected economic outlooks six months down the road. Bankers from Colorado, Illinois, Iowa, Kansas, Minnesota, Missouri, Nebraska, North Dakota, South Dakota and Wyoming are included. This survey represents an early snapshot of the economy of rural, agriculturally and energy-dependent portions of the nation. The Rural Mainstreet Index (RMI) is a unique index covering 10 regional states, focusing on approximately 200 rural communities with an average popu-lation of 1,300. It gives the most current real-time analysis of the rural economy.

MAIN$TREET ON YOUR $TREET

COLORADO

For the 18th straight month, Colorado's Rural Mainstreet Index (RMI) remained above growth neutral. The index for June declined to a still solid 57.6 from 65.2 in May. The farmland and ranchland price index de-clined to 62.4 from May's 77.9. Colorado's hiring index for June was 57.5, down from May's 65.3. According to Fred Bauer, president of Farmers Bank in Ault, "Drought still going on in our area, affecting crops (will have lower yields) and what moisture we have had came with hail in some areas."

ILLINOIS

For the first time in more than two years, the RMI for Illinois moved below growth neutral. The June RMI slumped to 43.6 from May's 50.4. Farmland prices remained above growth neutral with a reading of 51.5 from May's 56.0. The state's new-hiring index dipped to 50.2 from 50.6 in May.

IOWA

Iowa's June RMI decreased to 56.1 from 60.2 in May. The farmland price index slipped to 64.6 from May's 68.7. Iowa's new-hiring index for June dipped to 58.9 from May's 59.1. According to Charles Helscher, president of Farmers Savings Bank in Keota, "Early planted corn still looks very good in our area, but we need rain in the next week. Late, or replanted, corn is struggling and predicted high temps with no rain will begin to reduce yield potential."

KANSAS

The Kansas RMI for June slumped to 50.7 from May's strong 62.1. The farmland price index sank to 59.6 from 70.9 in June. The state's new-hiring index decreased to 55.6 from May's 60.5.

MINNESOTA

The June RMI for Minnesota expanded to 62.1 from 59.8. Minnesota's farmland price index dipped to 67.4 from 71.6 in May. Minnesota's new-hiring index advanced to 60.9 from May's 60.5. Bryan Grove, CEO of American State Bank in Grygla, summarized what many bankers reported for the month, "Recent timely rains in our area were very welcome. Small grain crops are developing nicely with great potential." Pete Haddeland, CEO of First National Bank in Mahnomen, added that crops in his area look "great."

MISSOURI

The RMI for Missouri declined to 48.9 from 51.8 in May. The farmland price index for June slipped to 51.2 from 52.5 in May. Missouri's new-hiring index slumped to 41.4 from May's 52.3. Don Reynolds, president of Regional Missouri Bank in Salisbury reported, "Dry weather and poor crop prospects are starting to take a tool on attitudes."

NEBRASKA

Growth in Nebraska's rural economy, while still positive, remains weak. The June RMI for Nebraska rose slightly to 50.9 from 50.1 in May. The farmland price index slipped to 53.4 from 54.2 in May. Nebraska's new-hiring index advanced to a tepid 51.4 from May's 49.4. Jim Stanosheck, CEO of State Bank in Odell said, "A two inch rain last night pushed back the doomsday for crops in our area."

NORTH DAKOTA

The North Dakota RMI for June declined to a robust and regional high 88.9 from 91.5 in May. The farmland price index expanded to 90.2 from 88.5 in May. North Dakota's new-hiring index declined to 79.4 from 92.2 in May. North Dakota's expansion continues and is the healthiest in the region and nation.

SOUTH DAKOTA

The June RMI for South Dakota declined to 49.5 from May's growth-neutral 50.0. The farmland price index dipped to 51.5 from 57.2 in May. South Dakota's new-hiring index for June dipped 50.2 from 51.4 in May.

WYOMING

The June RMI for Wyoming slumped to 46.8 from 52.3 in May. The June farmland and ranchland price index declined to 53.4 from 58.8 in May. Wyoming's new-hiring index sank to 51.5 from 52.5 in May. Bob Sutter, Vice Chair of Hilltop National Bank in Casper, Wyo. said, "Wyoming state revenues are down due to the low natural gas prices, even though the oil exploration continues at a high level. This is due in part to our strong oil and gas exploration infrastructure that is active both in Wyoming and in the North Dakota shale play."

THE BULLISH NEWS

- Over the past 12 months consumer prices increased by only 1.7 percent.

- Retreating oil prices probably kept a lid on the value of U.S. imports and inflation in May and June. Brent crude traded declined to $98.19 a barrel on July 6, down from a 2012 high of $126.22 on March 13.

- Initial claims for unemployment insurance dropped by 14,000 to 374,000 in the week ended June 30.

THE BEARISH NEWS

- June jobs data indicate that the nation added only 80,000 jobs and the unemployment rate remained at an unacceptably high 8.2 percent.

- The S&P/Case-Shiller index of property values in 20 cities dropped 1.9% in April.

- The national ISM leading economic indicator dropped below growth neutral for the first time since the recession. This is a major, major negative signal.

- The yield (interest rate) on Spanish sovereign debt rose approximately 7 percent signaling continuing concerns about Spain's potential default.

WHAT TO WATCH

- **PMI's:** On August 1, Creighton's releases its regional leading economic indicators (PMIs) and the national Institute for Supply Management releases its national PMI. These are the first releases for August another PMI below 50.0 will be very, very bearish for the U.S. economy.

- **Jobs:** On Friday August 3, the U.S. Bureau of Labor Statistics (BLS) will release the employment report for July. Another weak employment reading (less than 80,000 jobs added) will be bearish for equity markets and the U.S. economy.

- **US GDP:** On July 27, the U.S. Bureau of Economic Analysis releases its 2nd quarter GDP estimates. Annualized growth of less than one percent will get a very negative reception from investors and economists (including me).

THE OUTLOOK

FROM GOSS:

- I expect annualized GDP growth for the second quarter of 2012 to be less than one percent. It should be 3%-4% or above.

- If the "Bush" tax cuts expire on January 1, 2013 for every taxpayers, as currently in place, I expect the U.S. economy to move back into a recession in 2013.

- The U.S. trade deficit will shrink in the months ahead but for the wrong reasons—both imports and exports will shrink. The U.S. and global economies are slipping close to a recession.

OTHER FORECASTS:

- Chief Economist, Conference Board (July 2012). "The slow labor market improvement reflected in this month's 80,000 increase in jobs once again confirms that the better payroll increases in the beginning of the year were another false start. The pullback marks the third straight disappointing year. Subdued demand has been the one consistent factor in this sluggish economic expansion. On top of moderately rising labor costs, companies' profit growth is also slowing. There is little hope of an acceleration in the pace of job growth any time soon. These conditions are likely to persist at least through the summer and possibly longer. This economy has no forward momentum and little help from monetary or fiscal policy. As if that were not enough, ill winds are blowing in from both a contracting Europe and slowing growth in emerging markets. Also, domestic lawmakers' inaction on the upcoming "fiscal cliff" creates uncertainty that is not conducive to hiring."

- The Congressional Budget Office (June 2012): "Over the past few years, the federal government has been recording budget deficits that are the largest as a share of the economy since 1945. Consequently, the amount of federal debt held by the public has surged. By the end of this year, CBO projects that the federal debt will reach roughly 70 percent of gross domestic product (GDP), the highest percentage since shortly after World War II." Note: 70% does not include borrowing from Social Security Trust fund.

GOSS EGGS (RECENT DUMB ECONOMIC MOVES)

- San Bernardino County, Calif. via eminent domain is proposing to seize mortgages and restructure them for underwater homeowners. This sounds like something out of an undergraduate economics class. Interestingly, the plan targets only the holders of those bundled, privately held securit-ized mortgages. (i.e. Fannie Mae and Freddie Mac loans will be exempt).

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