

State Aid Fuels Local Spending Growth and Provides No Property Tax Relief

Politicians running for statewide office routinely promise to reduce property taxes, which are actually set at the local level by local officials. Instead of focusing on the real problem, which is overspending at the local level, governors and legislators promise to increase state aid to local units anticipating that the funds will be used to limit the growth in property taxes and local spending. This approach has proved futile in terms of economic outcomes. Between 2000 and 2011 as a share of gross domestic product (GDP), the 26 states that increased state aid to local government raised property taxes by a median of 0.31 percentage points while the 24 states that reduced state aid to local units expanded property taxes by a smaller 0.26 percentage points. Furthermore over the same time period, the same 26 states that increased state aid boosted local spending by 1.05 percentage points while the same 24 states that reduced state aid enlarged local spending by a smaller 0.27 percentage points. Thus, past data show that not only did state aid not provide property tax relief, as customarily promised, property tax burdens and overall local spending actually rose more quickly for states that grew state aid more swiftly. What should state policymakers do instead? States should limit the increase state aid to local units to the growth local population plus the increase in prices. This action would tend to reduce state tax burdens and encourage local political leaders to limit growth in local spending. Ernie Goss.

MAINSTREET RESULTS

Rural Mainstreet Economy for March: Still Weak with Declines in Farmland Prices

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

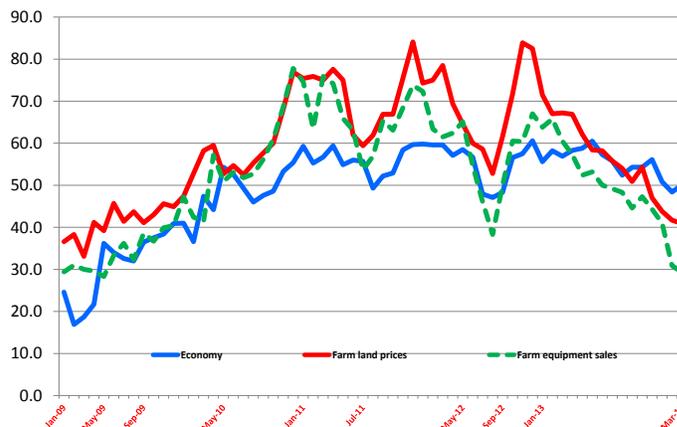
Table 1: The Mainstreet Economy	Mar. 2013	Feb. 2014	Mar. 2014
Area Economic Index	56.9	48.4	50.1
Loan volume	51.5	50.0	65.5
Checking deposits	70.5	61.7	65.5
Certificate of deposits	42.4	42.5	42.5
Farm land prices	67.2	41.7	40.9
Farm equipment area sales	60.5	30.9	29.3
Home sales	69.2	53.4	51.8
Hiring in the area	59.4	54.3	60.0
Retail Business	51.6	40.1	49.2
Economy 6 months from now	52.3	47.4	47.3

Survey Results at a Glance:

- Rural Mainstreet Index up slightly for the month indicating only slim growth.
- Farmland price index sinks to lowest level since March 2009.
- Agriculture equipment sales decline to lowest level since May 2009.

- Cash rents for farmland expected to increase by less than 1 percent over next year.

Rural Mainstreet Economy January '09 – March '14



After moving below growth neutral for February, the Rural Mainstreet economy rose slightly above 50.0, according to the March survey of bank CEOs in a 10-state area. **Overall:** The Rural Mainstreet Index (RMI), which ranges between 0 and 100, with 50.0 representing growth neutral, increased to 50.1 from 48.4 in February.

Scott Tweksbury, president of Heartland State Bank in Edgeley, N. D. reported, "Our market had yield reductions due to drought in 2013 and that has had some bearing on local conditions. Livestock producers, cow-calf in particular, are generally enjoying record profits offsetting reductions in crop farming income."

The overall index for the Rural Mainstreet Economy indicates that the areas of the nation highly dependent on agriculture and energy experiencing slow, to no growth over recent months. Slight upturns in agriculture commodity prices over the past several months have yet to boost the Rural Mainstreet Economy. We will need to see additional increases in farm commodity prices to push the agriculture based economy back into healthy growth territory such as was experienced in 2012 and early 2013.

Farming and ranching: The farmland and ranchland-price index for March sank to 40.9, its lowest level since March 2009, and down from February's very weak 41.7. This is the fourth straight month that the farmland and ranchland-price index has moved below growth neutral. Farm equipment sales remained below growth neutral for the ninth straight month. The March index sank to a weak 29.3, its lowest reading since May of 2009, and down from 30.9 last month. Agriculture equipment and implement dealers in the agriculture based areas of the region are experiencing very weak sales to farmers even as farm equipment manufacturers are experiencing positive growth due to healthy sales abroad.

This month bankers were asked the current value of annual cash rents for farmland in their area and how much they expected values to change over the next 12 months. A regional average of \$258 per acre was recorded with growth of only 0.6 percent expected over the next 12 months. More than one-third, or 35.8 percent, expect cash rents to decline over the course of the next year. Last March when we asked this same question, bankers anticipated that cash rents would rise by 9.3 percent over the next year. This is a significant deterioration in the outlook for cash rents from this time last year.

Tweksbury said, "We are seeing renters requesting reductions from landlords but few landlords agreeing. I think

little will change for 2014 but if commodity prices remain unchanged then some reductions likely for 2015."

With the Federal Reserve continuing to withdraw their economic stimulus, I expect rising interest rates to put even more downward pressures on farmland prices and cash rents.

Banking: The loan-volume index advanced to a robust 65.5 from February's 50.0. The checking-deposit index expanded to 65.5 from February's 61.7, while the index for certificates of deposit and other savings instruments was unchanged from February's 42.5. This month bankers were also asked to report factors restraining loan demand for their banks. More than one-third, or 34.7 percent, indicated that loan demand was normal and with lending advancing as usual. However, 44.9 percent reported that lack of demand from borrowers was limiting lending. More than 10 percent detailed lending pullbacks due to poor credit quality of applicants. Additionally 10.2 percent of bankers reported that banking regulations were restricting bank loans.

Bryan Grove, CEO of American State Bank in Grygla, Minn., "Strong (farm) profits over the past few years and excellent working capital positions (of farmers) limit operating loan demand from existing customers." Furthermore, Grove indicates that his bank has plenty of liquidity but demand is soft and 2014 projections show tighter cash flows for farmers.

Hiring: Rural Mainstreet businesses continue to hire at a solid pace. The March hiring index advanced to 60.0 from 54.3 in February. While the farm economy slows, businesses on Rural Mainstreet continue to expand their payrolls.

Confidence: The confidence index, which reflects expectations for the economy six months out, fell to 47.3 from last month's 47.4. Weaker agriculture commodity prices have not only reduced overall economic activity and farmland prices, they have undermined economic confidence.

Home and retail sales: The March home-sales index declined to 51.8 from February's 53.4. The March retail-sales index rose to 49.2 from 40.1 in February. Even though the index remained below growth neutral, weather improvements pushed the index higher from February's poor reading.

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. The survey is supported by a grant from Security State Bank in Ansley, Neb.

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 population of 1,300. It gives the most current real-time analysis of the rural economy. Goss and Bill McQuillan, former chairman of the Independent Community Banks of America, created the monthly economic survey in 2005.

growth neutral. The index increased slightly to 49.2 from 49.0 in February. The Illinois farmland-price index increased to 30.6 from February's 29.9. The state's new-hiring index improved to 50.7 from 44.5 in February.

IOWA

The March RMI for Iowa expanded to 49.8 from February's 48.4. The farmland-price index for March advanced to 37.6 from February's 36.3. Iowa's new-hiring index for March rose to 56.3 from 49.1 in February.

KANSAS

The Kansas RMI for March climbed to 50.1 from 49.8 in February. The farmland-price index for March declined to 41.3 from February's 54.4. The state's new-hiring index declined to 59.2 from February's 64.1.

MINNESOTA

The March RMI for Minnesota rose to 50.4 from February's 47.6. Minnesota's farmland-price index for March fell to 40.3 from February's 50.6. The new-hiring index declined to 57.3 from 67.2 in February.

MISSOURI

The March RMI for Missouri increased slightly to 50.9 from February's 50.3. The farmland-price index for March slumped to 49.7 from February's 64.7. Missouri's new-hiring index decreased to 66.0 from 72.3 in February.

NEBRASKA

For a second straight month, Nebraska's Rural Mainstreet Index moved below growth neutral. The index improved slightly to 49.5 from February's 48.8. The farmland-price index for March plummeted to 27.7 from February's 42.6. Nebraska's new-hiring index declined to 48.4 from February's 52.2.

NORTH DAKOTA

The North Dakota RMI for March declined to 52.6 from February's 54.7. The farmland-price index declined to 58.6 from 63.2 in February. North Dakota's new-hiring index rose to 73.1 from 71.1 in February.

SOUTH DAKOTA

The March RMI for South Dakota expanded to a weak 49.2 from February's 48.9. The farmland-price index for March sank to 29.4 from 44.3 in February. South Dakota's new-hiring index for March fell to 49.7 from February's 52.5.

WYOMING

The March RMI for Wyoming increased to 49.5 from 48.7 in February. The March farmland and ranchland-price index sank to 33.1 from February's 37.2. Wyoming's new-hiring index for March improved to 52.7 from February's 50.2.

MAINSTREET ON YOUR STREET

COLORADO

After moving below growth neutral for February, Colorado's Rural Mainstreet Index (RMI) inched above the 50.0 threshold, advancing to 50.9 from 48.6 in February. The farmland and ranchland-price index expanded to 43.8 from February's 39.2. Colorado's hiring index for March rose to 61.3 from February's 51.8.

ILLINOIS

For a third straight month, the RMI for Illinois remained below

THE BULLISH NEWS

- For March, Creighton University's survey of supply managers and the national survey of supply managers point to improving growth for the first half of 2014.
- U.S. employers added 192,000 jobs in March and January/February jobs gains were revised by +37,000.
- Real estate data provider CoreLogic said last week that prices for existing homes rose 12.2% in February from a

year ago. That was up slightly from January's year-over-year pace of 12%. On a month-to-month basis, prices in February rose 0.8% from January.

in a variety of areas—including labor, consumer, and housing markets—are expected to improve over the next two years, while inflation remains tame."

THE BEARISH NEWS

- The U.S. trade deficit climbed to \$42.3 billion in February, its highest level in 5 months.
- The percent of the working age population in the labor force remains at its lowest level since 1978.
- Over the last 12 months, hourly wages have grown by a puny 2.1%

WHAT TO WATCH

- **1st Quarter GDP:** On April 30, the U.S. Bureau of Economic Analysis will release Quarter 1 GDP. Annualized growth above 3.0% will be bad for bond prices resulting in even higher long-term interest rates.
- **Jobs:** On Friday May 24, the U.S. Bureau of Labor Statistics (BLS) will release employment report for April. Strong job additions (above 200,000) will result in long term interest rates rising more quickly.
- **CPI:** On May 15, the Bureau of Labor Statistics releases consumer price indices for April. A monthly increase of 0.2% or more will encourage the Fed to maintain and potentially reduce its monthly bond buying program. It will point to higher long-term interest rates. No change in short-term interest rates in 2014.

THE OUTLOOK

FROM GOSS:

- Short term interest rates will change very little, up or down, in 2014.
- The regional and U.S. economies to continue to improve for the 2nd Quarter 2014.
- Inflationary pressures to rise in the months ahead but to a still modest pace or approximately 2.2% annually.

OTHER FORECASTS:

- National Association of Business Economics (March 2014). "Summary: "Despite a challenging start to the year in which adverse weather conditions will likely shave nearly one half of one percentage point from first-quarter real GDP growth, NABE's March 2014 Outlook Survey panel expects the pace of economic expansion to accelerate this year—and next," said NABE President Jack Kleinhenz, chief economist of the National Retail Federation. "The consensus of the panelists is that real GDP will advance at a weak 1.9% annualized rate in the first three months of the year but pick up by year end to a pace of more than 3%. On an annual average basis, real GDP growth is forecasted to increase from 1.9% last year to 2.8% this year, and to 3.1% in 2015. Conditions

GOSS EGGS (RECENT DUMB ECONOMIC MOVES)

- The federal government continues to incentivize leisure and punish work and educational advancement via a broken income tax system. For 2013, a two parent family with two children earning; the minimum wage-will pay no income taxes and get a refund of \$7,172; \$35,000 will pay no taxes and get a refund of \$4,092; \$45,000 will pay no taxes and get a refund of \$662; \$75,000 paid \$4,188 in income taxes; \$105,000 paid \$9,158 in income taxes; \$200,000 paid \$35,682 in income taxes; \$300,000 paid \$68,553 in income taxes.

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