**August 2012 Bankers’ Economic Newsletter**

Do Red states, which are viewed as more pro-business and tax friendly, experience superior economic performance when compared to Blue states that are seen as more pro-government and tax burdensome? That is, have the states voting for the Democrat presidential candidate in the last three elections (Blue), or the states with electoral votes cast for the Republican in the last three elections (Red), experienced the best economic performance? Alternatively, have the Purple states, states that voted for the Democrat presidential candidate in at least one of the elections, and the Republican in at least one of the three presidential elections been the top performing group? U.S. Bureau of Economic Analysis data show that in terms of the growth of the overall state economy, or Gross Domestic Product (GDP) between 1999 and 2010, Red states grew by a median of 66.2% or significantly greater than Blue states at 52.2%, and Purple states at 60.5%. As for job addition over the same time period, Blue states again underperformed with a median growth of 0.2% compared to Red states’ expansion of 3.2% and Purple states’ of 3.3%. In terms of after-tax income per capita, the gap was substantial with Red states advancing by a median 52.3% compared to the much slower growth of Purple states at 46.1% and Blue states at 49.7%. Moreover in terms of overall growth (GDP), 8 of the top 10 performing states were Red states while only 4 of the 10 bottom performing states were Red. On the other hand, Blue states tended to have a somewhat more evenly distributed income with a median Gini coefficient of 0.450 compared to Red and Purple states’ 0.455. Gini coefficients range between 0 and 1.00 with lower coefficients indicating more evenly distributed income. Details of the analysis can be accessed at: www.economictrends.blogspot.com Ernie Goss.

### MAINSTREET RESULTS

#### Rural Mainstreet Index Nosedives: Drought Impacting Ethanol/Biodiesel Production

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

<table>
<thead>
<tr>
<th>Table 1: The Mainstreet Economy</th>
<th>July 2011</th>
<th>June 2012</th>
<th>July 2012</th>
</tr>
</thead>
<tbody>
<tr>
<td>Area Economic Index</td>
<td>55.7</td>
<td>56.7</td>
<td>47.9</td>
</tr>
<tr>
<td>Loan volume</td>
<td>66.4</td>
<td>64.2</td>
<td>65.3</td>
</tr>
<tr>
<td>Checking deposits</td>
<td>52.8</td>
<td>55.3</td>
<td>47.9</td>
</tr>
<tr>
<td>Certificate of deposits</td>
<td>43.7</td>
<td>38.9</td>
<td>41.7</td>
</tr>
<tr>
<td>Farm land prices</td>
<td>59.4</td>
<td>60.0</td>
<td>58.6</td>
</tr>
<tr>
<td>Farm equipment area sales</td>
<td>53.7</td>
<td>54.7</td>
<td>46.1</td>
</tr>
<tr>
<td>Home sales</td>
<td>51.4</td>
<td>66.4</td>
<td>58.6</td>
</tr>
<tr>
<td>Hiring in the area</td>
<td>49.3</td>
<td>59.1</td>
<td>52.8</td>
</tr>
<tr>
<td>Retail Business</td>
<td>47.9</td>
<td>54.6</td>
<td>44.4</td>
</tr>
<tr>
<td>Economy 6 months from now</td>
<td>55.0</td>
<td>58.5</td>
<td>40.0</td>
</tr>
</tbody>
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July Survey Results at a Glance:
- Rural Mainstreet Index plunges to lowest level in almost two years.
- Farmland price growth declines.
- Drought pushes agriculture-equipment sales to lowest level since recession.
- Almost two-thirds of bankers report cutback or closing of ethanol/biodiesel plants due to drought.

Drought conditions pushed the June Rural Mainstreet Index (RMI) to its lowest level since 2010. Overall: The Rural Mainstreet Index (RMI), which ranges between 0 and 100 with 50.0 representing growth neutral, declined to 47.9, its lowest level since September 2010 and down from last month’s 56.7. As reported by Jim Ashworth president of Carlinville National Bank in Carlinville, Ill., “The drought is severe in west-central Illinois. Conditions are like those in Steinbeck’s Grapes of Wrath, but no one today wants to move to California.”

The drought is putting a dent into the economies of the agriculturally dependent areas of the 10-state area. Just as the region has benefited mightily from very healthy farm income over the past few years, we are now detecting warning signals of a significant economic reversal for rural areas. Even for those areas not suffering from drought, there is concern. As the region has benefited mightily from very healthy farm income over the past few years, we are now detecting warning signals of a significant economic reversal for rural areas. Even for those areas not suffering from drought, there is concern. Pete Haddeland, CEO of First National Bank in Mahnomen, Minn., expressed the view of the minority of areas with solid growth. He commented, “Our crops look good up here, but we still need rain.”

**Farming:** According to the July survey, farmland prices continue to head higher but at a much slower rate. However, for a third straight month, farmland price growth weakened with the July index dropping to 58.6, its lowest level since September of 2010 and down from last month’s 60.0. Even so, this is the 30th consecutive month the index has been above growth neutral. The farm-equipment sales index sank to 46.1, its lowest level since March 2009, and was down significantly from last month’s 54.7. Much weaker economic conditions are slowing growth in farmland prices. Furthermore, farmers are clearly reducing their purchases of agriculture equipment. This pullback will soon affect urban areas of the region.

This month, bank CEOs were asked about the impact of the drought on ethanol/biodiesel production in their ar-ea. Of banks with plants in their area, almost two-thirds, or 64.3 percent, reported negative impacts with 21.4 percent indicating plant closures and 42.9 percent detailing cutback in operations. Only 35.7 percent reported no impact from the drought. The lack of available crops and higher prices for corn and soybean are having significant and negative impacts on ethanol and biodiesel producers in the area. The impacts of the drought are particularly negative for livestock producers. Korey Schow, CEO of the Ban of Keystone in Keystone, Neb, said, “Persistent hot and dry conditions are causing cow/calf producers to sell a portion of their herd due to lack of pasture.”

**Banking:** Farmers increased their demand for loans with the loan-volume index climbing to 65.3 from June’s 64.2. This marks the fifth consecutive month the index has risen. Bankers were asked what the impact of the drought was on farmer
Mainstreet on your street

Colorado
For the 19th straight month, Colorado’s Rural Mainstreet Index (RMI) remained above growth neutral. However, the index for July declined to a weak 50.1 from June’s 57.6 and 65.2 in May. The farmland and ranchland price index declined to 61.3 from June’s 62.4. Colorado’s hiring index for July was 51.8, down from June’s 57.5. Mike Bass, President of the First National Bank of Hugo said, “Wheat harvest in our area was 2 and one-half weeks early. Average yield for our area was 30 bushels per acre, a decrease of 30 percent from the previous year.”

Illinois
For a second straight month, the RMI for Illinois moved below growth neutral. The July index slumped to 36.1 from June’s 43.6. Farmland prices remained above growth neutral with a reading of 50.4, down from June’s 51.5. The state’s new-hiring index dipped to 44.6 from 50.2 in June. Southern Illinois is being battered by the drought. According to Jim Eckert, President of Anchor State Bank in Anchor, “Many corn fields will yield next to nothing. Most will have drastically reduced yields unless rain comes quickly. Soybeans are badly hurt by the drought, but could still be revived by timely rains.”

Iowa
The July RMI for Iowa decreased to 48.6 from 56.1 in June. The farmland price index slumped to 63.5 from June’s 64.6. Iowa’s new-hiring index for July dipped to 53.3 from June’s 58.9. Larry Winum, President of Glenwood State Bank in Glenwood, reported that, “Last year we battled flooding, this year we have no moisture. We need to find the right rain dance or crop yields are going to be in serious trouble.” Additionally Bill Hess, CEO of Iowa Savings Bank in Carroll, said, “Rated crops in the area as fair but poor may be a better term if high temperatures and no rain remain the pattern.”

Kansas
The Kansas RMI for July slumped to 43.2 from June’s 50.7 and May’s much stronger 62.1. The farmland price index sank to 58.4 from June’s 59.6. The state’s new-hiring index decreased to 49.9 from 55.6 in June. In most states, some areas are doing well while others not. For example, Michael Johnson, CEO of Swedish American State Bank in Courtland, reported, “We have been blessed with recent rain.” On the other hand, Dale Bradley CEO of the Citizens State Bank in Miltonvale, said, “A weak economy and continued drought conditions make it difficult for us all.”

Minnesota
The July RMI for Minnesota declined to 54.6 from June’s 62.1. Minnesota’s farmland price index dipped to 66.2 from June’s 67.4. Minnesota’s new-hiring index decreased to 55.1 from June 60.9. Minnesota farming conditions appear to be much better than those found in other states. Bryan Grove, CEO of American State Bank in Grygla, said, “Our area of northwest Minnesota has had spotty rains, keeping crop conditions good. Small grains look decent – harvest should start within 10 days. Soybeans also look good, but are needing rain soon to maximize potential.” Brian Nicklasen, President of Woodland Bank in Remer, said, “We have limited farming in our area but the soybeans and corn crops look outstanding. The logging industry is still struggling due to lack of markets in the paper Industry.”

Missouri
The RMI for Missouri declined to 44.3 from 48.9 in June. The farmland price index for June slipped to 50.2 from June’s 51.2. Missouri’s new-hiring index slumped to 35.8 from 41.4 in June. Don Reynolds, President of Regional Missouri Bank in Salisbury, reported, “Dry weather and poor crop prospects are starting to take a toll on attitudes.”

Nebraska
Growth in Nebraska’s rural economy moved into negative territory for July. The July RMI for the state slumped to 43.4 from June’s 50.9. The farmland price index slumped to 52.3 from 53.4 in June. Nebraska’s new-hiring index declined to 45.8 from June’s 51.4. Lyndell Woodbury, reporting for banks in seven Nebraska communities said, “The drought has affected the pastures most significantly in north central Nebraska, and dryland crops have been significantly impacted in all of our communities. Impact to Main Street will be felt 4th quarter of this year and into 2013.” Kelly Hammerlun reporting from Imperial, indicated that crops in irrigated areas were doing well while those in nonirrigated areas were “worthless.”

North Dakota
The North Dakota RMI for July declined but remained strong with a regional high 75.6 from June’s 88.9. The farmland price index slumped to 73.6 from June’s 90.2. North Dakota’s new-hiring index declined to 66.4 from 79.4 in June. John Brown, executive director of the Independent Community Banks of North Dakota reported, “Crops look really good in our area at this time.”

South Dakota
The July RMI for South Dakota declined to 46.7 from June’s 49.5. The farmland price index dipped to 50.4 from June’s 51.5. South Dakota’s new-hiring index for July slumped to 44.6 from 50.2 in June.
WYOMING
The July RMI for Wyoming slumped to 39.3 from 46.8 in June. The July farmland and ranchland price index declined to 52.3 from 53.4 in June. Wyoming’s new-hiring index sank to 45.8 from 51.5 in June. 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

• The U.S. economy added 163,000 jobs in July. Not enough to keep unemployment from rising to 8.3% but better than expected.

• The Case-Shiller home price index rose 2.2% from April. This was the largest one-month increase in 12 years of the 20-city index.

• Energy price growth continues to moderate.

THE BEARISH NEWS

• U.S. Gross Domestic Product growth for the second quarter of 2012 (annualized and seasonally adjust) was 1.5%. Growth should be more than triple this in the so-called recovery.

• National and Creighton’s regional PMIs (leading economic indicators) dropped below growth neutral. Both are indicating slow to NO growth for the next 3-6 months.

• U.S. retail sales growth has been virtually flat for the last two months.

WHAT TO WATCH

• PMI’s: On Sept. 4, Creighton’s releases its regional leading economic indicators (PMIs) and the national Institute for Supply Management releases its national PMI. I cannot overemphasize the importance of this data. They are the first economic releases for September. Further declines in the overall PMI will be very bearish for the U.S. economy.

• Jobs: On Friday September 7, the U.S. Bureau of Labor Statistics (BLS) will release the employment report for August. Another semi-strong employment reading (above 150,000 jobs added) will be bullish for equity markets and the U.S. economy.

• Retail Sales: On August 14, the U.S. Census Bureau releases its retail sales data for July. The last two months have been awful. Growth from June that is flat or negative will be the first solid indicator of a significantly higher risk of a recession.

THE OUTLOOK

FROM GOSS:

• The risk of a 2013 recession has risen from 20% to 35% over the past three months.

• There will be another European eruption in the next 30 days pushing the European Central Bank to open the “money” spigot. What they need is substantial economic restructuring.

• Third quarter GDP growth will be less than 1% as economic uncertainty rises as we approach the “fiscal cliff.”

OTHER FORECASTS:

• The National Association of Business Economics (NABE) (July 2012): “The July survey results suggest that the increase in sales experienced earlier in the year may have been short-lived. Fewer panelists in the July survey (39%) reported rising sales than in the April survey, in which 60% of panelists reported rising sales. The survey suggests fewer capital spending increases and panelists continue to forecast stability in capital spending over the next 12 months. NABE panelists express significant concerns about the impact on their sales if Bush-era tax cuts expire in late December and the automatic government spending cuts take place in early January. Indeed, 65% of the panelists expect sales to fall under this scenario, while 30% of the panelists expect that sales would stay the same.

• ICBA: Camden R. Fine, president and CEO of the Independent Community Bankers of America (ICBA) released this statement today in response to recent headlines about the need for too-big-to-fail financial institutions to be split up. “There is a growing chorus of support for downsizing too-big-to-fail financial institutions, which enjoy implicit government support and continually put our nation’s taxpayers at risk. Splitting up these systemically risky financial firms will help restore discipline to the financial markets and prevent future crises, which would have a devastating impact on community banks and the communities they serve. Policymakers should examine the appropriate means to break up the largest and riskiest financial institutions to ensure they never again put the nation’s financial system, taxpayers, and the economy in jeopardy.”

GOSS EGGS

(RECENT DUMB ECONOMIC MOVES)

• Both the Republican House and the Democrat Senate wasted ink, time and money by passing different versions of the extension of the “Bush” tax cuts. Nothing is going to happen regarding the “fiscal cliff” until after the elections in November. The fiscal cliff slated for January 2013 is a record increase in taxes for all and $110 billion in spending cuts.

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