

"A monthly survey of supply chain managers"

Welcome to our September report covering August survey results. All three surveys, U.S., Mid-America and Mountain States are pointing to the same economic outcome for the final quarter of 2013; slow but positive growth and rising inflationary pressures. Inflation may be once again raising its ugly head meaning even higher interest rates in the months ahead. Follow my comments at: www.twitter.com/erniegoss

What Policy Actions Would End Economic Malaise? Top 10 Policy Remedies

Despite record economic stimuli from the Federal Reserve and the federal government, the U.S. economy continues to stumble. The August employment report attests to the failed economic policies. In August 2013, more than 300,000 unemployed Americans became so discouraged that they quit looking for a job. This is the 40th straight month that the number of workers leaving the workforce exceeded the number finding a job. In fact, the percentage of the working age population employed plummeted to its lowest level since August 1978. If all of these discouraged workers once again began looking for a job, the nation's unemployment rate would rise from the current "too high" 7.3 percent to approximately 10.0 percent. Even the biggest booster of past economic intervention must concede that they have not succeeded. But what government/Fed actions would perk up the economy (long and short term):

1. Reduce the incentives for not working. A new Cato Institute study concluded that the myriad of benefits provided the non-working by government including food stamps, federal disability pay, housing assistance, Medicaid and more exceed \$12 per hour.
2. Pass an immigration reform bill.
3. Approve the 19 pending applications for licenses to export LNG (liquefied natural gas).
4. Approve the Keystone XL pipeline application.
5. Allow kids to escape failing schools by providing vouchers (long term).
6. Continue federal spending sequestration. This provides businesses with greater certainty.
7. Raise the debt ceiling without conditions.
8. Begin raising the Social Security retirement age.
9. Reduce the yearly cost-of-living adjustment to Social Security payments.
10. Begin unwinding the Fed's excessive money expansion labeled QE3 this month (again provides businesses with greater certainty).

Ernie Goss.

Link to video:

<http://www.youtube.com/watch?v=sBkrw9FRCvg>

LAST MONTH'S SURVEY RESULTS

Mid-America Leading Indicator Rises for August: Inflation Gauge Up Sharply

SURVEY RESULTS AT A GLANCE:

- Regional index rises for the first time since March of this year.
- Approximately two-thirds of firms report no impact from federal spending sequestration.
- Inflationary pressures at the wholesale level rise sharply.
- Firms expect prices for products and services they buy to rise 4.6 percent over the next year.

The monthly Mid-America Business Conditions Index, a leading economic indicator for a nine-state region, rose for the first time since March. The index continues to indicate that growth for the fourth quarter of 2013 will be positive, but down from the first quarter of this year. **Overall index:** The Business Conditions Index, which ranges between 0 and 100, increased to 53.8 from July's 53.5.

As a result of strong exports and a very healthy farm economy, the Mid-America economy was expanding at a strong pace in the first quarter of this year. Our results point to positive growth for the final quarter of this year but at approximately half the rate of the first quarter. Both exports and farm income growth are down from earlier in the year.

Employment: After moving below growth neutral for January, the region's employment gauge has remained above 50.0 for the past seven months. The August reading declined to 52.8 from 55.3 in July. Nondurable goods manufacturers, especially those tied to agriculture and international markets are cutting employment in the region. Job gains were registered for durable goods producers and value-added nonmanufacturing firms. On the other hand, nondurable goods firms, except for food processors, experienced slight job losses for the month.

Wholesale Prices: The prices-paid index, which tracks the cost of purchased raw materials and supplies, increased for the first time since February of this year. The wholesale inflation gauge climbed to 61.8 from 58.0 in July.

I am concerned that this may be the first signal that the period of benign inflation is over. Weakness in inflationary pressures has provided support for the Federal Reserve's record expansionary money policies including its \$85 billion monthly bond buying program, quantitative easing 3 (QE3). I expect upturns in inflationary pressures and asset price bubbles to push the Fed to begin reducing or tapering QE3 at the next meeting of its interest rate setting committee (FOMC) at its Sept. 17-18 meetings. This will mean that interest rates will move somewhat higher in the weeks and months ahead.

This month supply managers indicated that they expect the prices of products and services they buy to rise by 4.6 percent over the next year. This is up significantly from the 2 percent reported in April of this year.

Confidence: Looking six months ahead, economic optimism, as captured by the August business confidence index, fell to 53.9 from July's 56.9. International tensions and uncertainty surrounding implementation of health care reform pushed supply managers' economic outlook lower for the month.

In each of the last six months, supply managers were asked how the federal spending sequestration was affecting their company. In the August survey, approximately two-thirds of supply managers indicated that the cuts have had no impact to date. Slightly less than one-third reported only modest impacts from sequestration. Only 1 percent of businesses reported significant impacts. Thus, the federal spending sequestration remains a non-event in terms of the regional economy.

Inventories: After eight straight months of inventory gains, supply managers reported pullbacks in the level of raw materials and supplies to support future production. The August inventory index sank to 49.4 from 52.7 in July. In anticipation of slower sales and growth in new orders, companies in our survey have, for the first time since November of last year, reduced inventory levels.

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In terms of sustainable purchasing, 77.5 percent of firms reported no change in their practices, 21.3 percent indicated an expansion and 1.2 percent detailed reduction in such programs.

Trade: The new export orders index rose briskly to 56.2 from July's 50.0. The import index slumped to 49.3 from July's 53.6. Slow regional growth weighed on purchases from abroad for the month. Even though the export reading was up significantly for the month, readings over the past several months have been trending lower as a result of slower global growth.

Other components: Other components of the August Business Conditions Index were new orders at 56.8, up from July's 52.2; production or sales at 60.1, up from last month's 54.2; and delivery lead time at 50.0, down from 53.3 in July.

The Creighton Economic Forecasting Group has conducted the monthly survey of supply managers in nine states since 1994 to produce leading economic indicators of the Mid-America economy. States included in the survey are Arkansas, Iowa, Kansas, Minnesota, Missouri, Nebraska, North Dakota, Oklahoma and South Dakota.

The forecasting group's overall index, referred to as the Business Conditions Index, ranges between 0 and 100. An index greater than 50 indicates an expansionary economy over the course of the next three to six months. The Business Conditions Index is a mathematical average of indices for new orders, production or sales, employment, inventories and delivery lead time. This is the same methodology used by the National Institute for Supply Management, formerly the Purchasing Management Association, since 1931.

MID-AMERICA STATES

ARKANSAS

The August overall index for Arkansas fell to 45.8 from July's 52.9. Components of the index from the survey of supply managers were new orders at 36.6, production or sales at 40.4, delivery lead time at 54.4, inventories at 45.8, and employment at 51.8. Overall manufacturers in the state detailed reductions in business activity for the month with expansions for durable goods producers more than offset by nondurable goods manufacturing losses for the month. As the national unemployment rate has declined for 2013, Arkansas' jobless rate has risen. Based on our survey results, the state's unemployment rate will change little in the months ahead.

IOWA

The Iowa Business Conditions Index declined for a third straight month but remains at a healthy level. The overall index from a survey of supply managers for August slipped to a strong 65.6 from July's 67.4. Components of the index for August were new orders at 77.1, production or sales at 73.2, delivery lead time at 51.5, employment at 61.7, and inventories at 64.4. Business gains for durable and nondurable goods producers combined to make Iowa's manufacturing sector the strongest in the region for the month. This has spilled over into the broader Iowa economy.

KANSAS

The Kansas Business Conditions Index for August strengthened to 60.0 from 57.3 in July. Components of the leading economic indicator from the monthly survey of supply managers were new orders at 67.8, production or sales at 74.2, delivery lead time at 49.4, employment at 63.9, and inventories at 44.8.

Business gains for durable and nondurable goods producers combined to push the state's manufacturing sector into solid growth territory. Over the past year, Kansas has added approximately 5,000 individuals to its unemployment rolls. Our surveys over the past several months point to an improvement in the state's jobless rate for the rest of the year.

MINNESOTA

For a ninth straight month, Minnesota's Business Conditions Index moved above growth neutral. The index from a monthly survey of supply managers in the state rose to a healthy 59.0 from July's 54.0. Components of the index from the August survey were new orders at 58.0, production or sales at 64.8, delivery lead time at 55.3, inventories at 63.0, and employment at 53.9. Expansions among durable goods producers in the state more than offset slightly negative conditions for nondurable goods firms, including food processors, pushing the overall manufacturing sector and economy forward.

MISSOURI

The August Business Conditions Index for Missouri declined slightly to 53.6 from 55.7 in July. Components of the survey of supply managers in the state were new orders at 52.2, production or sales at 60.1, delivery lead time at 50.1, inventories at 48.0, and employment at 57.7. The state's manufacturing sector, especially durable goods producers, is pushing the state's economy forward. On the other side of the economic coin, telecommunication firms in the state continue to shed jobs.

NEBRASKA

After declining below growth neutral for July, Nebraska's overall index, or leading economic indicator, moved above the 50.0 threshold to 50.6 from July's 49.1. Components of the index for August were new orders at 52.4, production or sales at 51.6, delivery lead time at 49.6, inventories at 48.3, and employment at 51.3. Durable and nondurable manufacturers combined to push the overall manufacturing sector forward for the month. Food processors in the state experienced solid business growth for the month.

NORTH DAKOTA

North Dakota's leading economic indicator sank for August. The overall index, termed the Business Conditions Index, from a survey of supply managers in the state declined to 54.4 from 57.5 in July. Components of the overall index for August were new orders at 53.1, production or sales at 51.4, delivery lead time at 71.4, employment at 54.7, and inventories at 41.5. Business gains for durable and nondurable goods producers combined to push North Dakota's manufacturing sector into positive growth territory for the month. The mining sector continues to drive state growth higher.

OKLAHOMA

The Business Conditions Index for Oklahoma dipped below growth neutral for August to 49.7 from 52.3 in July. Components of the August survey of supply managers in the state were new orders at 51.9, production or sales at 47.7, delivery lead time at 54.9, inventories at 49.4, and employment at 44.8. Pullbacks in business activity for nondurable goods producers, including food processors, more than offset gains for durable goods manufacturers. August declines for mining firms and companies linked to the mining sector shed jobs for the month.

SOUTH DAKOTA

For a ninth straight month, South Dakota's leading economic indicator from a survey of supply managers has remained above growth neutral 50.0. The overall index, termed the Business

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Conditions Index, declined to a healthy 57.4 from July's 64.8. Components of the index for August were new orders at 64.4, production or sales at 62.0, delivery lead time at 55.4, inventories at 50.5, and employment at 54.5. Manufacturers in the state are reporting solid gains in jobs and business activity. Our surveys point to continuing growth for South Dakota's economy.



THE BULLISH NEWS

- The Case-Shiller home price index advanced by more than two percent for June and was up by more than 12% over the past 12 months. Are we seeing another bubble?
- Both the non-manufacturing and manufacturing ISM numbers were up strongly for August. I do not think the economy is as strong as these two reports indicate.
- US retail sales rose 0.2% month-on-month in July following an upward revision to June to 0.6% from 0.4%. The two-month increase indicates that the U.S. consumer buying.



THE BEARISH NEWS

- The U.S. trade deficit widened in July from a four-year low in June. American consumers bought more foreign cars and other imported goods, while U.S. companies exported fewer long-lasting manufactured goods. This will subtract from GDP for the third quarter.
- Total nonfarm payroll employment increased by 169,000 in August, and the unemployment rate was little changed at 7.3%. Much of the gain in employment was in retail trade and food services, two low wage industries. Furthermore, June and July employment numbers were revised downward.
- The consumer price index has expanded by 0.7% over the past two months. This is too high for the Fed to sit on the economic sidelines.

WHAT TO WATCH

- PMIs: On Oct. 1, Creighton University and the Institute for Supply Management will release purchasing management indices (PMI) for September. This is the first economic data for September. Keep an eye on the overall index and the prices-paid index. Any significant upturn will push the Federal Reserve to be more aggressive in its QE3 taper. This will mean higher long-term interest rates.
- Retail Sales: On Oct. 11, the U.S. Census Bureau releases its retail sales numbers for September. We will get another read on the strength of the U.S. consumer.
- Jobs: On Friday Oct. 4, the U.S. Bureau of Labor Statistics (BLS) will release the employment report for September. A very weak report (jobs under 120,000, unemployment rate up, and 100,000 discourage workers) will factor into a Fed QE3 taper that is very, very slight.

THE OUTLOOK

FROM GOSS:

- Over the next 6 months, I expect inflationary pressures as captured by the consumer price index to move above the Federal Reserve's comfort level of 2.0%. I expect the annual rate to rise to 3.0% by the end of the year.
- If the U.S. goes to war with Syria and it lasts more than several weeks, oil prices will move significantly higher. Prices could approach \$130 per barrel. This will be another factor contributing to rising inflationary pressures and slower economic growth.

OTHER FORECASTS:

- National Association of Business Economics (August 2013 survey). "An overwhelming majority of the NABE Economic Policy Survey panel believes that the projected deficits over the next few decades represent a principal challenge facing the nation, although there was no consensus among panelists who participate in the NABE Policy Survey regarding the appropriateness of fiscal policy at present," said NABE Policy Survey Committee Chair Jay Bryson, Global Economist at Wells Fargo Securities. "Most panelists favor a mix of policy approaches that includes some form of spending restraint as the best way to address long-term deficits, with a plurality favoring a mixed approach of spending restraint and revenue increases. About half of the panelists believe that the Federal Reserve will begin to wind down its asset purchase program by the end of the year, while the vast majority looks for the Fed to maintain its current target for the fed funds rate through the first half of 2014."

Goss Eggs (Recent Dumb Economic Moves)

- The U.S. Justice Department is trying to stop a school vouchers program in Louisiana that attempt to help poor families send their children to independent schools instead of under-performing public schools. Fully 90% of the children who benefit from the program are minorities. The DOJ's logic is that as blacks flee to better schools, the failing schools that they leave become more segregated.

Survey results for September will be released on the first business day of the month, Oct 1.

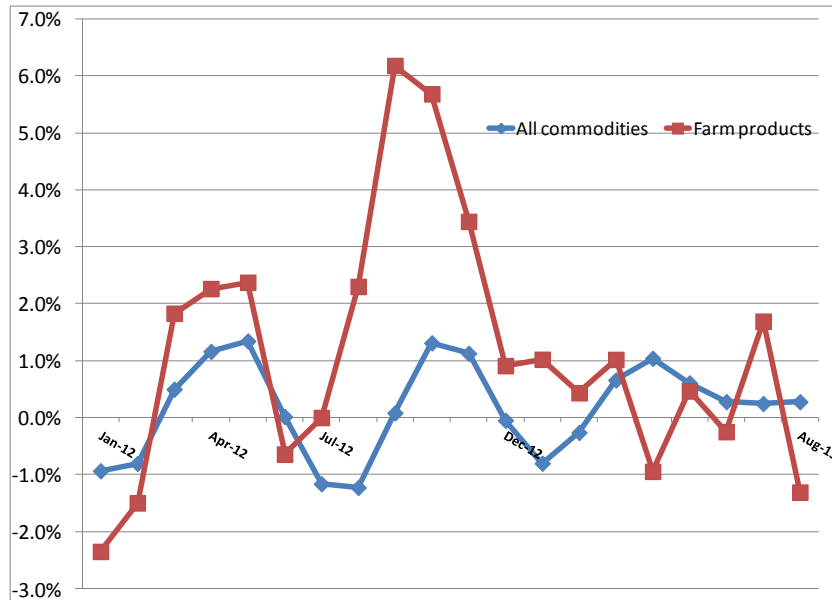
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PRICE DATA

ALL COMMODITIES/FARM PRODUCTS 2007-2013
 FUELS & RELATED/METALS & METAL PRODUCTS

Price changes, 3 month moving average, 2012- August 2013



Price changes, 3 month moving average, 2012 - August 2013

