THE MAINSTREET ECONOMIC REPORT

A monthly survey of community bank CEOs

March 2017

Welcome to Creighton's February Bank CEO Report. Survey data over the last several months indicate that the Rural Mainstreet Economy remains weak, but is improving even as farmland prices and agriculture equipment sales decline.

Property Taxes Expanding as Farm Income Plummets

The U.S. Department of Agriculture estimates that 2017 net farm income will fall 8.7% from 2016 levels, thus marking the fourth straight year of sinking agriculture income. As a result, states that depend heavily on farming have experienced significant tax collection shortfalls producing economic stress, particularly for rural areas of agriculturally dependent states.

Even with sharply lower agriculture income, local taxing bodies have continued to raise property taxes on farmland. For example, between 2013 and 2014, farmland taxable assessed values for the 10-state Rural Mainstreet region actually expanded by an incredible 11.4% as farm earnings fell by 18.0%. Over that same period, local governments across the 10-state region increased elementary-secondary school spending per student by a median 3.3%. Not surprisingly, property taxes growth for 2013-14 for the ten states were: NE 7.3%, SD 6.7%, CO 3.1%, KS 2.6%, IA 2.0%, ND 0.9%, IL 0.7%, MO -0.1%, WY -.3.6% and MN at -5.6%.

While more recent data are not available, anecdotal evidence indicates that this same pattern has continued with lower farm income, higher K-12 spending, and ballooning property tax burdens on farmland as net farm income sinks.

In order to avoid strangling the economic viability of farmers in the region, several potential solutions should be advanced. First, slow the growth in K-12 education spending; second, base property taxes on the income of the farmer rather than estimated or historical farmland values; and third, change the state aid to education formulas to be more transparent and less detrimental to rural residents. What will not work is shifting the property tax burden to state sales and income taxes via state aid to local units. Historical evidence shows that this shift works for 2 or 3 years, but then excessive property tax growth returns, matched with higher income and/or sales taxes.

MAINSTREET RESULTS

Tables 1 and 2 summarize the findings from the February 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	Feb. 2016	Jan. 2017	Feb. 2017
Area economic index	37.0	42.8	45.8
Loan volume	48.9	52.4	50.1
Checking deposits	44.6	71.9	68.1
Certificates of deposit	39.8	43.9	46.8
Farmland prices	29.8	33.8	33.7
Farm equipment sales	11.3	16.7	20.5
Home sales	51.1	52.5	57.8
Hiring in the area	48.9	52.5	54.3
Retail business	37.0	39.1	45.8
Economy 6 months from now	30.4	42.7	45.7

February Survey Results at a Glance:

- The overall index, while remaining below growth neutral, rose to its highest level since September 2015.
- More than one-third of bank CEOs reported their local economy remains in an economic downturn. Only 14.9 percent of bankers indicated their local economy was expanding.
- On average, farmland prices have declined by 5.1 percent over the past 12 months.
- Approximately 73.9 percent of bankers expect agriculture- equipment sales to continue to decline in their area over the next year.

Rural Mainstreet, Economic Indicators, Sept. 2014 – Feb. 2017 (50.0 = growth neutral)

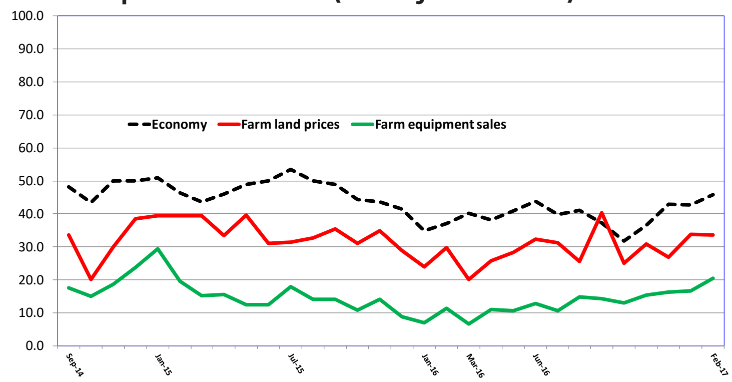

Table 2: The Rural Mainstreet Economy, February 2017

	Percentage of bankers reporting				
	Deep recession	Modest downturn	Little or no economic growth	Modest economic growth	Strong economic growth
How would you describe the economy in your area?	2.1%	31.9%	51.1%	14.9%	0.0%
	Percentage of bankers reporting				
	Significant reduction in sales	Reduction in sales	Little or no change in sales	Increases in sales	Significant increases in sales
	Percentage of bankers reporting				
In terms of agriculture equipment sales for dealers in your area for the next year, what do you expect?	32.5%	41.3%	21.7%	4.3%	0.0%
	Percentage of bankers reporting				
	Decreased 10% - 20%	Decreased 1% - 9%	No change	Increased 1% - 9%	Increased 10% - 20%
What has been the change in the price of an acre of crop land in your area over the past year?	17.0%	63.8%	8.5%	8.5%	2.1%

Rural Mainstreet Climbs to Highest Level Since September 2015: But Only 15 Percent Report Expanding Economy

The Creighton University Rural Mainstreet Index remained weak with a reading below growth neu-tral for the 18th straight month, according to the monthly survey of bank CEOs in rural areas of a 10-state region dependent on agriculture and/or energy.

Overall: The index, which ranges between 0 and 100 advanced to 45.8 from 42.8 in January. This is the highest overall index since September 2015. Weak farm commodity prices continue to squeeze Rural Mainstreet economies. However, the negatives are getting less negative. Over the past 12 months, livestock commodity prices have tumbled by 9.4 percent and grain commodity prices have slumped by 6.3 percent, both an improvement over last month.

Only 14.9 percent of bankers reported that their local economy was expanding. Approximately 34 percent indicated their local economy was in a recession with the remaining 51.1 percent indicating little or no economic growth.

Pierre, South Dakota, What we see in the agriculture industry is that farmers hurt the worst are those who farm small grain crops exclusively." Douglas indicated operators that diversify in cattle, cattle feeding, hogs and other like type lines, are maintaining, or at least not experiencing as large a drop in net worth.

Farming and ranching: The farmland and ranchland-price index for February dipped to a frail 33.7 from January's 33.8. This is the 39th straight month the index has languished below growth neutral 50.0.

Bankers indicated that farmland prices in their area had declined by an average of 5.1 percent across the region over the past 12 months.

But there was a great deal of variation across the region. Pete Haddeland, CEO First National Bank in Mahnomen, Minnesota, for example, reported, "Land values are holding up here. We did not see the big prices increases." He also indicated that farmers harvested great crops last year.

The February farm equipment-sales index increased to 20.5 from 16.7 in January.

Almost three-fourths of the bankers expect agriculture equipment sales to continue to decline over the next 12 months. Only 4.3 percent expect agriculture equipment sales to increase over the same period of time.

Banking: Borrowing by farmers remained above growth neutral for February, but is growing at a much slower pace than for January as the loan-volume index fell to 50.1 from last month's 52.4. The checking-deposit index slipped to 68.1 from 71.9 in January, while the index for certificates of deposit and other savings instruments increased to 46.8 from 43.9 in January.

Despite weaker farm income, defaults remain relatively low. As stated by Don Reynolds, CEO of Regional Missouri Bank in Marceline, Missouri, "We are pleased that most of our farm customers have been able to meet payment obligations this year."

Hiring: The job gauge rose to 54.3 from January's 52.5. For the region, Rural Mainstreet employment is down by 0.6 percent over the past 12 months. Over the same period of time, urban employment for the region expanded by 1.2 percent.

Confidence: The confidence index, which reflects expectations for the economy six months out, improved to a weak 45.7 from 42.7 in January indicating a continued pessimistic outlook among bankers. Until agricultural commodity prices begin to trend higher, I expect banker's economic outlook to remain weak.

Home and retail sales: Home sales moved higher for the Rural Mainstreet economy for February with a reading of 57.8, which is up from January's 52.5. The February retail-sales index increased to 45.8 from January's 39.1.

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 com-munities and their projected economic outlooks six months down the road. Bankers from Colorado, Illi-nois, Iowa, Kansas, Minnesota, Missouri, Nebraska, North Dakota, South Dakota and Wyoming are in-cluded. 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 re-gional 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.

MAIN$TREET ON YOUR $TREET

COLORADO

Colorado's Rural Mainstreet Index (RMI) rose to 37.1 from 24.9 in January. The farmland and ranchland-price index soared to 66.6 from January's 25.5. Colorado's hiring index for January climbed to 68.2 from January's 55.2.

ILLINOIS

The February RMI for Illinois improved to 46.4 from 34.2 in January. The farmland-price index grew to 34.8 from January's 17.9. The state's new-hiring index climbed to 56.7 from last month's 52.4.

IOWA

The February RMI for Iowa fell to 46.1 from 50.2 in January. Iowa's farmland-price index for February sank to 40.1 from 48.6 in January. Iowa's new-hiring index for February slipped to a still strong 58.6 from January's 60.1.

KANSAS

The Kansas RMI for February increased to 40.8 from January's 29.6. The state's farmland-price index slumped to 16.8 from 18.3 in January. The new-hiring index for Kansas slipped to 48.3 from 49.0 in January.

MINNESOTA

The February RMI for Minnesota climbed to 47.5 from January's 39.0. Minnesota's farmland-price index rose to 38.1 from 30.1 in January. The new-hiring index for the state jumped to 57.9 from last month's 53.3.

MISSOURI

The February RMI for Missouri advanced to 55.9 from 51.3 in January. The farmland-price index jumped to 56.2 from January's 19.9. Missouri's new-hiring index rose to 64.4 from 49.6 in January.

NEBRASKA

The Nebraska RMI for February declined to 47.1 from 52.6 in January. The state's farmland-price index rose to 39.3 from January's 37.7. Nebraska's new-hiring index climbed 58.3 from 56.1 in January.

NORTH DAKOTA
The North Dakota RMI for February increased to 38.0 from January's 37.9. The farmland-price index sank to 19.9 from January's 31.2. North Dakota's new-hiring index increased to 38.1 from 34.0 in January.

SOUTH DAKOTA
The February RMI for South Dakota fell to a healthy 55.9 from January's 56.9 . The farmland-price index climbed to 59.2 from January's 43.4. South Dakota's new-hiring index advanced to 65.5 from January's 58.2.

WYOMING
The February RMI for Wyoming increased to a weak 42.3 from 37.8 in January. The February farmland and ranchland-price index fell to 22.3 from January's 24.5. Wyoming's new-hiring index increased to 46.1 from January's 42.8.

THE BULLISH NEWS

- The Dow-Jones Industrial average broke 21,000 in March for the first time ever. In my judgment, U.S. stocks are priced for perfection—low interest rates, higher earnings, less regulatory burdens, and lower corporate taxes.
- Both Creighton's and the ISM's manufacturing index (PMI) rose sharply for February.
- The Mexican Peso has soared by 6% since January 1. This is good news for companies and farmers that export to Mexico since it makes U.S. products more price competitive.

THE BEARISH NEWS

- The U.S. trade deficit climbed to a five-year high in January to a $48.5 billion gap between exports and imports.
- Total foreign reserves held by the 30 largest emerging market countries rose to $3.9 trillion. This likely signals concerns among these nations regarding international financial turmoil.
- European economic growth is finally improving. This will be a slight but positive stimulus for the U.S. economy.

STATISTIC OF THE MONTH

- Shares of Caterpillar, US Steel, and construction services firms rose by anywhere from 7 to 20% on Wednesday, November 9, after Trump's victory (in anticipation of an infrastructure bill that may not be forthcoming in my judgment).

WHAT TO WATCH

- Repatriation: Signals from Congress to reduce corporate tax rates on foreign earnings for U.S. corpora-tions brought home. It will increase the value of the U.S. dollar.
- CPI: (March 15) BLS releases CPI for February. YOY growth (core) above the Fed target of 2.0% for the past 14 months. Annualized growth above 2.5% is getting "too hot" for the Fed.
- Jobs: (March 10). BLS releases its February jobs report. A strong year-over-year wage growth number (>3.0%) could push the Federal Reserve to raise interest rates on March 15.

THE OUTLOOK

National Association of Business Economics (NABE): "In general, NABE Policy Survey panelists feel that current monetary and fiscal policies are 'about right,'" said NABE President Stuart Mackintosh, CBE, executive director, Group of Thirty. "However, a large majority of panelists believes the Trump administration's proposed fiscal policies are likely to increase the federal budget deficit as a share of the economy over the next decade," he continued. "Most panelists would prefer to see the deficit share shrink." At the same time, survey respondents hold a more positive view about NAFTA and immigration policies than those proposed by the Trump Administration, with a general preference for relaxed immigration policies," added NABE Policy Survey Chair Richard DeKaser, CBE, executive vice president and corporate economist, Wells Fargo. "Panelists especially favor expanding the H-1B visa program for high-skill workers. Only 5% favor increased spending to deport unauthorized immigrants. Regarding changes to the Affordable Care Act, or 'Obamacare,' survey participants favor a system that increases consumer choice and control, supported by tax credits."

FROM GOSS:
- I expect the U.S. trade deficit to continue to widen putting more and more pressure on politicians to take ill conceived actions.
- I expect short term and long term interest rates to continue to move higher through the first quarter of 2017, albeit at a slower pace than over the last four months. **I expect wages to continue to grow, but at a faster pace approaching 3.5% annualized by the middle of 2017.

GOSS EGGS (RECENT DUMB ECONOMIC MOVES)

- Las Vegas taxpayers approved $750 million in public funding via hotel tax to support the Oakland Raiders move to the gambling mecca. This a lousy bet that enriches NFL owners at the expense of the taxpayer.

BANKER READING ROOM

ICBA Urges Congress to Avoid Farm Bill Cuts (Feb. 21, 2017). ICBA asked Congress not to make further cuts to the farm bill in 2018 following the substantial deficit reduction contained in the bill that passed in 2014. In a letter to congressional appropriators, ICBA and more than 500 other agricultural and business groups noted that the last farm bill was projected to contribute $23 billion to deficit reduction over 10 years when it passed but has now been scored as saving nearly $100 billion more than initially projected. Lawmakers should recognize these savings and not hamstring the House and Senate agriculture committees with further cuts amid severe economic troubles in the agricultural and rural economy, the coalition wrote.
http://www.icba.org/news-events/news-details/2017/02/22/icba-urges-congress-to-avoid-farm-bill-cuts

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This month's survey results will be released on the third Thursday of the month, March 17th.