THE MAINSTEET ECONOMY REPORT

"A monthly survey of community bank CEO's"

February 2018

The Urban-Rural Economic Divide For Rural Mainstreet States

Just as the farmer with one hand in the fireplace and the other in the refrigerator is on av-erage doing well, the agriculturally and energy dependent states have been, on average, doing (performing) well. However, the state average blends healthy growth in urban areas in each state with the economic fatigue in the rural areas of the same states.

Between 2009 and 2013, the Rural Mainstreet survey typically indicated very healthy growth in rural areas dependent on agriculture and energy. During this time period, driven by Federal Reserve (Fed) easy money policies that stimulated agriculture and energy exports, our surveys and government data tracked rural areas growing at brisk paces. During the Fed's ex-pansion policies from 2009 to 2013, average yearly growth in agriculture, food and oil products exports soared by 12.6 percent.

In 2014, the Fed ended one of its major stimulus programs, entitled Quantitative Easing, which lowered long-term interest rates, and in 2015 began raising short-term interest rates. The end of the Fed interest rate stimulation programs, or easy money policies, raised the value of the U.S. dollar and restrained exports, particularly of agriculture and energy commodities.

But for urban areas of the region, more dependent on manufacturing and housing, contin-ued to expand while rural areas relying on agriculture and energy moved into negative territory. During the Fed's less accommodative money polices, 2014-17, the average yearly export sales of agriculture, food, and oil products plummeted by 6.3 percent. As a result, employment in urban areas of the region over the past three years expanded by 4.1 percent, while employment in rural areas of the same states contracted by 0.3 percent.

What do Rural Mainstreet areas need to improve growth prospects? Two things: 1) Trade policies that focus on opening up, rather than closing, foreign markets. 2) Federal Reserve interest rate policies that produce a stable but weaker U.S. dollar. This will make U.S. goods sell-ing abroad more competitively priced. Ernie Goss.

MAINSTREET RESULTS

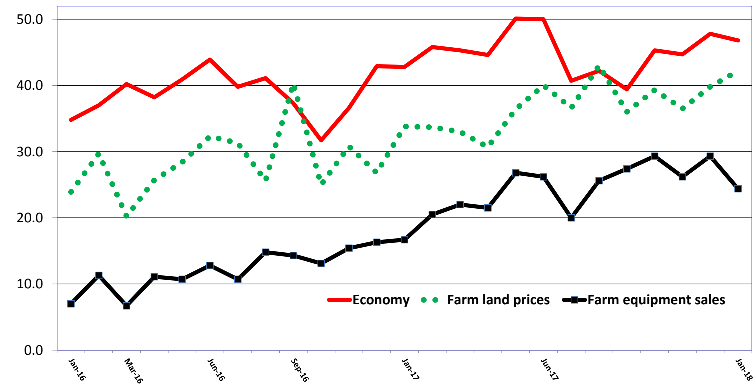
Rural Mainstreet Index Sinks for January: Rising Farm Loan Defaults Identified as Greatest 2018 Challenge

Table 1: The Mainstreet Economy	Jan 2017	Dec 2017	Jan 2018
Area Economic Index	42.8	47.8	46.8
Loan volume	52.4	67.1	54.4
Checking deposits	71.9	47.8	57.8
Certificate of deposits	43.9	42.1	43.5
Farm land prices	33.8	39.8	42.2
Farm equipment area sales	16.7	29.3	24.4
Home sales	52.5	53.5	51.2
Hiring in the area	52.5	59.6	50.0
Retail Business	39.1	52.4	43.5

Survey Results at a Glance:

- The overall index sank from December's weak reading and remained below growth neutral.
- Approximately 40 percent of bank CEOs named rising loan defaults as the greatest economic challenge for 2018.
- More than seven in 10 bankers expect that the abolition of NAFTA would have a negative impact on their economic area.
- For the 50th straight month, the farmland price index sank below growth neutral.

Rural Mainstreet, Economic Indicators, Jan. 2016 – January 2018 (50.0 = growth neutral)



The Creighton University Rural Mainstreet Index declined slightly in January from December's weak reading, remaining below growth neutral, according to the latest monthly survey of bank CEOs in rural areas of a 10-state region dependent on agriculture and/or energy.

Overall: The index, like all indices in the survey, ranges between 0 and 100 with 50.0 representing growth neutral, fell to 46.8 from 47.8 in December. Though the overall index remained below growth neutral, it is significantly higher than the reading for January 2017.

"While the overall Rural Mainstreet Index (RMI) for January declined and remained below growth neu-tral, year-over-year indices are trending higher. Clearly, based on our recent surveys, the negatives are getting less negative.

When asked to name the greatest 2018 economic challenge for their banks, four in 10 bankers re-ported that loan defaults represented the biggest challenges for the year ahead. This is well ahead of the second ranked challenge of competition from Farm Credit coming in at 15.6 percent.

Farming and ranching: The farmland and ranchland-price index for January rose to 42.2 from 39.8 in December. This is the 50th straight month the index has fallen below growth neutral 50.0.

However, there was a great variability among bankers regarding farmland prices. For example, Pete Haddeland, CEO of the First National Bank in Mahnomen, Minnesota, said, "Farmland values are holding in our area."

Regarding farmers that are cash renting farmland Brian Schroeder, president and CEO, Minier, Il-linois, reported, "Land owners have conceded very little to this point." However, Schroeder does expect that to change as cash rents move lower.

The January farm equipment-sales index slumped to 24.4 from December's 29.3. This marks the 53rd consecutive month the reading has dropped below growth neutral, 50.0.

Banking: Borrowing by farmers sank for January as the loan-volume index stood at 54.4, down from 67.1. The checking-deposit index expanded to 57.8 from December's 47.8, while the index for certificates of deposit and other savings instruments advanced to 43.5 from 42.1 in December.

Hiring: The employment gauge plummeted to 50.0 from December's 59.6.

Confidence: The confidence index, which reflects expectations for the economy six months out, fell to 46.7 from 51.2 in December, indicating a deterioration in the economic outlook among bankers. Concerns about trade, especially current NAFTA negotiations, and low agriculture commodity prices continue to restrain bankers' economic outlook. Approximately 71.2 percent of bankers projected that any interruption or abolition of NAFTA would have a negative impact on their area.

Home and retail sales: The home-sales index moved lower for the Rural Mainstreet economy in January, falling to 51.2 from December's 53.5. The January retail-sales index slumped to 43.5 from December's 52.4.

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.

MAIN$TREET ON YOUR $TREET

COLORADO
Colorado's Rural Mainstreet Index (RMI) increased to 51.7 from 50.3 in December. The farmland and ranchland-price index expanded to 43.7 from December's 40.5. Colorado's hiring index for January declined to 60.8 from December's 64.9.

ILLINOIS
The January RMI for Illinois dipped 46.4 from 46.7 in December. The farmland-price index rose to 42.1 from 39.9 in December. The state's new-hiring index fell to 50.2 from last month's 57.5. Brian Schroeder, president and CEO, Minier, Illinois, reported, "This agricultural economic reset has impacted all producers."

IOWA
The January RMI for Iowa dipped to 47.3 from 48.0 in December. Iowa's farmland-price index for January increased to 42.4 from December's 39.8. Iowa's new-hiring index for January declined to 52.1 from December's 60.0.

KANSAS
The Kansas RMI for January slipped to 43.1 from December's 43.3. The state's farmland-price index rose to 41.1 from 38.4 in December. The new-hiring index for Kansas slumped to 43.6 from December's 50.7.

MINNESOTA
The January RMI for Minnesota expanded to 46.5 from 45.4 in December. Minnesota's farmland-price index dipped to 41.1 from 42.5 in December. The new-hiring index for the state plummeted 43.6 from December's 78.0.

MISSOURI
The January RMI for Missouri declined to 51.6 from 55.4 in December. The farmland-price index rose to 43.6 from 40.1 in December. Missouri's new-hiring index fell to 60.6 from 78.0 in December.

NEBRASKA
The Nebraska RMI for January sank to 46.3 from December's 48.3. The state's farmland-price index climbed to 42.1 from last month's 35.8. Nebraska's new-hiring index stood at a strong 60.6, up from 59.6 in November.

NORTH DAKOTA
The North Dakota RMI for January increased to 51.4 from December's 52.2. The state's farmland-price index moved higher to 43.1 from 41.1 in December. North Dakota's new-hiring index declined to 57.2 from 68.4 in December.

SOUTH DAKOTA
The January RMI for South Dakota sank to 40.2 from 41.2 in December. The state's farmland-price index climbed to 40.2 from 37.8 in December. South Dakota's new-hiring index slumped to 37.9 from December's 46.5.

WYOMING
The January RMI for Wyoming slipped to 44.3 from December's 45.7. The January farmland and ranchland-price index climbed to 41.5 from 39.1 in December. Wyoming's new-hiring index fell to 50.2 from December's 55.5.

THE BULLISH NEWS

- Average wages expanded by 2.9% for the 12 months ending in January. This is good news for wage earners, but is a harbinger of higher interest rates.
- The U.S labor market added 200,000 jobs for January (even with an unemployment rate of 4.1%, a 17-year low).
- U.S. home prices rose 6.2% in November from one year earlier.

THE BEARISH NEWS

- The U.S. trade deficit rose to nearly a 6-year high in November driven by imports. (note: a larger trade deficit is a by-product of an expanding U.S. economy).
- Great Britain's Brexit negotiations could have significant impacts on the value of the U.S. dollar. Major disruptions would boost the value of the U.S. dollar.
- Due to fears of inflation and higher interest rates, the S&P 500 index by almost 4% in the week ending Feb. 2.

WHAT TO WATCH

- **Inflation, Inflation, Inflation:** The Bureau of Labor

Statistics will release the inflation gauge for February on March 13. An annualized increase above 2.5% will be bullish for stock prices and bearish for bond prices (rising yields, falling prices).

- **Wage Growth**: On March 9, the U.S. Bureau of Economic Analysis releases its February jobs report. Focus on the wage growth number. Year-over-year growth over 2.8% will be viewed as a signal of budding inflation with higher interest rates to follow.

- **Home Price. On the last Tuesday of the month, Fabruary 27**: S&P Corelogic will release its Case-Shiller home price index for December. Home prices have been rising by over 5.0% (annualized) since November 2015. Air will continue to inflate this bubble with too little housing supply.

THE OUTLOOK

FROM GOSS:

- I expect **four more Federal Reserve rate hikes by the end of 2018 (1.0% or 100 basis points); **the nation's consumer prices to expand by 2.9% in 2018; wage growth to pick up in 2018 with hourly wages growing by 3.3% in 2018. ***the nation's trade deficit to worsen for all of 2018. A rapidly expanding U.S. economy boosts imports more than exports.

OTHER FORECASTS:

- **NABE Business Conditions Survey (January 2018):** ""The results of the January 2018 NABE Business Conditions Survey show widespread sales and profit gains in the fourth quarter of 2017, but also notable increases in materials costs, wages, and shortages of skilled labor," said NABE Vice President Kevin Swift, CBE, chief economist, American Chemistry Council. "The panel's outlook for growth in the overall economy over the next four quarters surpasses the relatively positive assessments of the past few quarterly surveys. Compared to the near-term outlook three months ago, more firms expect increases in the next three months in their firms' profits, employment and capital spending. However, optimism regarding sales in the first quarter of 2018 is less widespread than it has been since 2016. "More respondents report that their firms are hiring—and having trouble filling positions—than in the October survey," added Swift. "Looking at 2018 as a whole, 63% of respondents expect their firms to increase sales, and three times as many expect hiring to increase rather than decrease."

GOSS EGGS (RECENT DUMB ECONOMIC MOVES)

- California municipalities are lying to either jurors or investors. For example, the Oakland city government contended in its recent lawsuit against U.S. oil companies that the city will be experiencing a 100-year flood every week" soon due to climate change. However, in its prospectus for Oakland general obligation bond investors, the city states that it cannot predict when and if the city will be threatened by floods, or other natural disasters. Sounds like Presidential candidate Kerry's doubletalk "I voted for this bill before I voted against it.

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This month's survey results will be released on the third Thursday of the month, February 15th.