

## **Rural Minnesota and the Great Recession: A Look at St. Cloud and Beyond**

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St. Cloud, Minnesota, grew from its inception as a trading post for pioneers in two main directions. Like other river cities of the upper Midwest, it provided a transshipment point for farmers sending goods out and receiving finished products into their homes. It also developed fairly quickly its own resource extraction in granite. (It is referred to as the Granite City to this day; its former minor league baseball team was called the Rox.)

Today, the city and its surrounding communities compose an area of about 200,000 inhabitants, making it the fourth-largest metropolitan area in Minnesota (after the Twin Cities, Duluth and Rochester.) It has grown into a regional retail center for Central Minnesota, an education hub with over 20,000 students in colleges and universities, and a regional health care provider through the St. Cloud Hospital and its affiliated medical practices. It has a workforce over 100,000 and area personal income of \$6.12 billion in 2008.

Calling St. Cloud a “metropolitan area” carries a connotation that it has changed from its roots. Whereas nineteenth century St. Cloud had much of its trade oriented between St. Cloud and rural Minnesota, by the twentieth century it had started to think of itself as an exporter to the world. From the granite of its quarries to the catalogs and legal forms of its printing presses, St. Cloud imagines itself as engaged in world commerce. In the 1950s and 1960s, the area diversified its manufacturing base and embraced its location as a regional shopping hub by building Crossroads Mall, which spawned a host of other retail shops and restaurants.

The city estimates that shoppers from surrounding areas double St. Cloud's population on weekends.

This is thought to have changed the structure of St. Cloud's economy. By structural change we mean that the direction of trade has moved toward a more global orientation. The area has not just more diversification in businesses, but diversification in customers and suppliers. In addition, St. Cloud remains vulnerable to structural change in the allocation of employment opportunities between goods-producing and service-providing industries. St. Cloud has historically enjoyed a disproportionately large share of manufacturing employment. As economic trends have led to more job opportunities in service-providing industries, the share of jobs in the goods-producing sectors of the St. Cloud economy has declined. This change in structure is also apparent in many rural communities around the state.

Many rural communities are also being forced to confront the effects of an aging workforce. While St. Cloud is not immune to the change that results from an aging population, these demographic forces are tempered by the existence of several major institutions of higher education in the St. Cloud area (and the associated influx of young people). In this regard, St. Cloud benefits from a population mix in a way that many rural communities are unable to enjoy.

For the last 11 years, the St. Cloud Area Economic Development Partnership and St. Cloud State University have collaborated on a survey of area businesses regarding the level of economic activity, employment, wages and prices they have experienced and expect to face over the near future. These data are reported in the *St. Cloud Area Quarterly Business Report*, which we have both authored since 2003. The response rate is over 75% most quarters, providing us with a good sample of the experiences and attitudes of St. Cloud business leaders.

There has been no more exciting time to write the *Report* than in the recent period we call The Great Recession. It has led to reflection on what St. Cloud's role is in the larger economy. The area experienced the Great Recession through a collapse in construction, the loss of many jobs in manufacturing, and closing of many retail businesses and

restaurants. But parts of the economy remained strong, particularly those that symbolize areas of St. Cloud's historical roots. In a recent survey, we asked these business leaders where they did business. The results surprised us: The durability of those rural connections had survived for many firms still operating here. It is about those connections that we write in this article.

In the first section of this article, we give an overview of the Great Recession's impact on the state and on rural Minnesota. In the next section we outline the industrial history of the St. Cloud area. In the third section we look at the results of the recent survey of St. Cloud firms that show that business owners in St. Cloud recognize their rural connections. We then turn to the future of the rural Minnesota economy. A combination of demographics and medium-term financial challenges face the area and make the future difficult to forecast.

### *I. The Great Recession's impact on rural Minnesota: An overview*

For rural America, the Great Recession of 2008-10 was the deepest recession since the Great Depression on some measures, though not all. It began at the end of 2007 with a combination of declining employment and commodity price inflation. That inflation continued into the middle of 2008. The producer price index for industrial commodities rose more than 17 percent over twelve months to July of that year, led by oil and construction materials. Across all agricultural goods, prices rose dramatically for seven months after the recession began.

The decline thereafter was swift. As Figure 1 shows, 12 months later the decline in producer prices for industrial commodities was nearly as large as the increase in 2007-08. Prices have since rebounded, while the Minnesota economy's level of activity has just begun to recover in late spring. We could redraw this graph with foodstuffs, livestock, seed oils, or any other price index, and the picture would look no different.

Rising prices are good for rural economies, as a substantial part of their income depends on selling commodities. Even

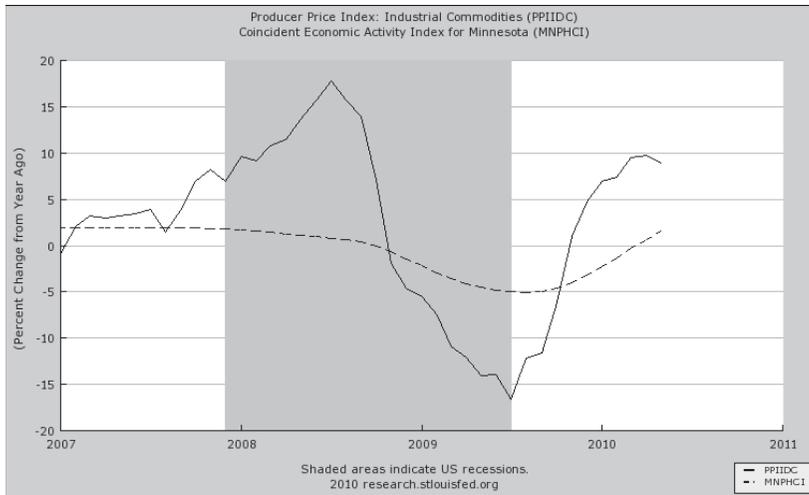


Figure 1: The Producer Price Index, 2007-2010.

though fuel and other input costs rose, farming profits were high in 2008. Combined with demand for corn as an input to ethanol, the return on an acre of land put into corn rose in 2008 to \$494 from \$402 in 2007.

But 2009 was a much worse year, as the recession deepened and demand for food fell worldwide. Declining prices led to a 10.6-percent decline in gross crop revenues in the United States. Jason Henderson of the Federal Reserve Bank of Kansas City writes that dairy and pork producers suffered the most in 2009, and cattle operators were below break-even levels by the end of the year.<sup>1</sup>

In the end, the rural economy suffered the same fate as metropolitan and suburban economies, but milder. While non-metro home prices never rose as much as those in cities, by the end of 2009 these prices were in decline as well, though by far smaller percentages. Agricultural land prices finally reversed their slide in the fourth quarter of 2009. And after three good years in 2006-08, the 2009 experience found rural economies with some cushion to absorb the recession.

The impact on St. Cloud has been to provide some cushion as well. Auto dealers reported as late as early 2008 that rural Minnesotans were buying trucks. St. Cloud's orientation toward rural Minnesota protected some sectors of its economy

from deeper declines, even though its manufacturing sector has been deeply cut in this recession (1,400 jobs in the sector were lost in 2009 in the St. Cloud area.)

## ***II. The history of St. Cloud and rural Minnesota***

Like many small rural cities on the American frontier, St. Cloud's early economy was based on the surrounding natural resources, and like many cities, it began as a port through which consumer goods for frontiersmen and farmers went west while timber, furs and agricultural goods went east. St. Cloud's birth was as a site for sawmills in the 1850s that sent logs down the Mississippi. The next generation brought granite quarries, and then printing and food processing. Each of the nineteenth-century industries has in one way or another survived to this day, with the exception of the sawmills.

St. Cloud is known as the Granite City. Early quarries on the east side of St. Cloud and near Lake George gave way to Rockville and the Cold Spring Granite Company (originally Rockville Granite Company). By 1920 there were 50 firms in the granite industry in the St. Cloud area. The number was only half that in 1997, but in the last ten years new firms have sprung up. Despite this growth, employment in non-ferrous mineral manufacturing in the St. Cloud area has fallen by almost a third since 1990. The industry has made significant investments in equipment that has increased productivity, however, so while employment is down, it appears output has expanded.

Similar stories can be told in other industries. Located near many rivers, the town became a trans-shipment point for logs to come to area sawmills, and sawmills soon led to paper mills such as the Hennepin Paper Company in Little Falls and Watab Paper Company in Sartell (one is gone and the other merged into a national firm). Lumber continued through places like Matthew Hall Lumber, a company begun in 1889.

Access to paper also provided a comparative advantage in the region for printing. Sentinel Printing, for example, was established in 1854 and continues to this day. Thirty-five printing firms employing nearly 2,600 workers continue in central Minnesota even though the peak of paper milling ended decades earlier.

The Heim Mill is another early St. Cloud firm, established in 1887, that continues to this day. First grinding wheat for flour and feed for animal husbandry, it now grinds more specialty grains. Nearby Pan-O-Gold has ground flour for baking since 1895. Some mills such as the Tileston Flour Mill have left the area, but food processing has remained strong in central Minnesota. Transportation was also a focus at various times as well. What was the Burbank Trading Company (using stage coaches and the river) became the Burlington Northern Railroad. The Pan Motor Company of 1917-22 gave way to International Harvester in the 1930s and to Arctic Cat today.

Beyond its granite quarry roots, the waterways and proximity to agriculture gave much of St. Cloud manufacturing a rural tinge, and much of the employment in the manufacturing sector in St. Cloud turns out to depend on its proximity to the rural economy. Data on the manufacture of goods in the St. Cloud MSA is shown in Table 1, comparing Economic Census data for 1992 and 2007. While some of the production is driven by more short-run factors — wood products increased in demand when homebuilding boomed in the middle part of the 2000s — the steady growth of

*Table 1: Share of manufacturing employment in the St. Cloud Metropolitan Statistical Area, comparing 1992 and 2007.*

| <b>Share of manufacturing employment in:</b> | <b>1992</b> | <b>2007</b> |
|--|-------------|-------------|
| Food manufacturing                           | 17.2%       | 17.7%       |
| Wood products                                | 4.5%        | 5.8%        |
| Printing & related manufacturing             | 13.4%       | 15.7%       |
| Nonmetallic mineral manufacturing            | 11.2%       | 8.5%        |
| Fabricated metals                            | 9.0%        | 6.9%        |
| Machinery manufacturing                      | 5.2%        | 6.9%        |
| Transportation equipment                     | 3.0%        | 7.1%        |
| Medical/ophthalmic equipment                 | 11.2%       | 4.6%        |
| Other  | 25.4%       | 23.6%       |
| Note: Total manufacturing employment         | 13,400      | 17,503      |

food products and printing indicate a consolidation of manufacturing in areas of traditional St. Cloud industry. Food and wood are both tied directly to rural economy output. And much of the machinery manufacturing comes from connections to the rural economy with machines built for farm use at firms such as DCI.

Productivity has grown over this period. Value added per worker in manufacturing rose an average of 4.6 percent between 1992 and 1997, 5.1 percent from 1997 to 2002, and 6.2 percent from 2002 to 2007.

This increase has led to additional hiring in certain fields, assisted by public policy. The increase in transportation equipment employment can be directly tied to tax policies such as JOBZ, which led to the building of Arctic Cat. Such stories can be found historically as well. The Great Depression did not hurt the granite industry or the railcar shops of the Great Northern Railroad, and in fact employment expanded when federal works programs bought granite to build Selke Field on the campus of what is now St. Cloud State University (the field's cornerstone bears the WPA marker, as does a wall that still stands at the corner of Northway Drive and Ninth Avenue).<sup>2</sup>

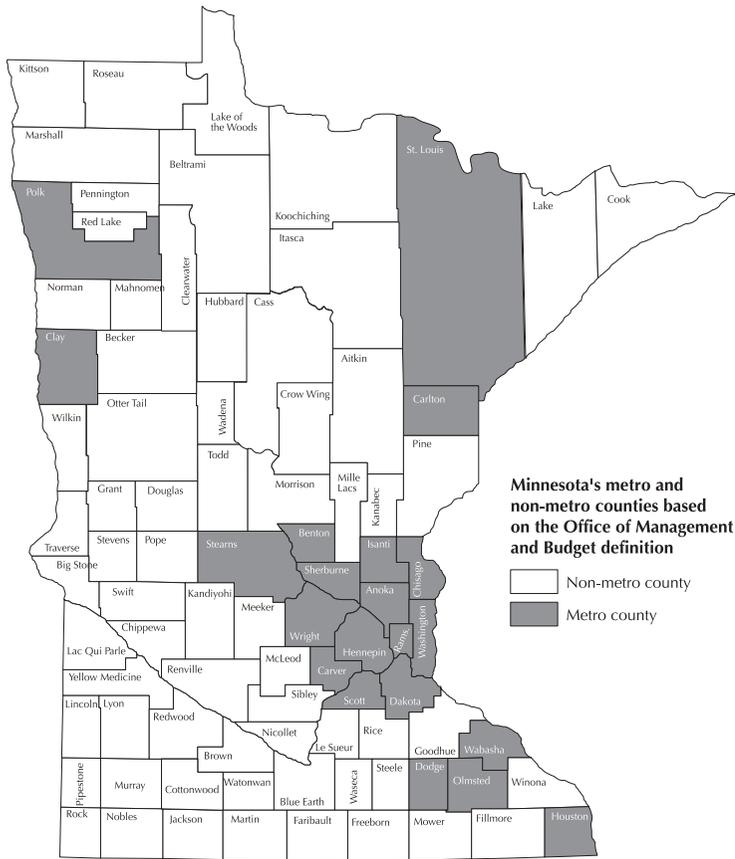
But most businesses that have survived in St. Cloud through the years have also diversified. Cold Spring Granite moved from lower-value-added stone walls to memorials, which sustained them through the Depression. Food processing has also evolved, as mills that used to grind wheat to flour now produce specialty products used in agriculture as well as higher-end foods. Firms that grew around the west-side industrial area in 1959 grew if they were related to these areas (Dairy Craft, now DCI, e.g.), but the ophthalmic and nondurable manufacturing firms (e.g., Fingerhut) did not fare as well. The diversification of the 1950s and 1960s passed into the current period of consolidation.

### ***III. How important is the rural economy to the state economy? A special case: The importance of the rural economy to firms in the St. Cloud area***

The U.S. Census Bureau, the USDA Economic Research Service, and the Office of Management and Budget (OMB)

each have alternative measures seeking to define what is meant by the term “rural.” It is not our intention to address any controversies surrounding which definition of rural should be used, so we take a practical approach to defining this term — we make use of the term that helps us best organize available data during the most recent recessionary period. We use the non-metro counties found in the OMB’s approach to defining rural as a way to construct rural economic performance data. In particular, we use the State of Minnesota Quarterly Census of Employment and Wages

Figure 2: Metro and non-metro counties in Minnesota.

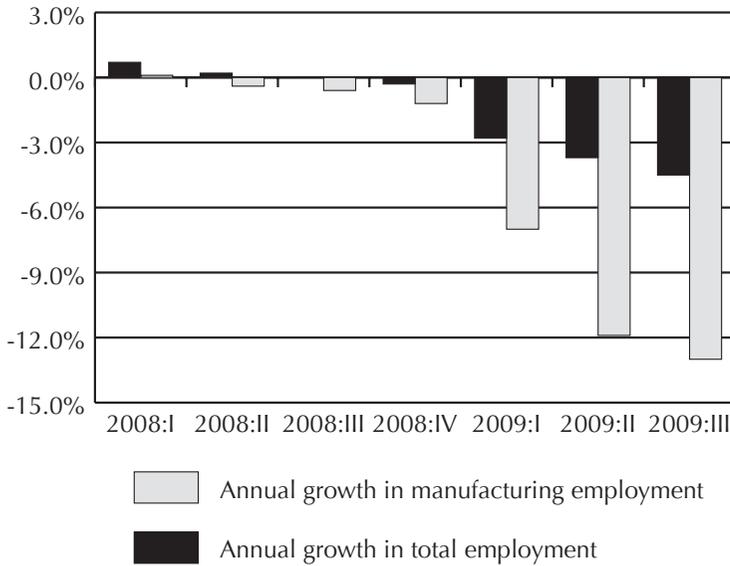


Source: [www.ers.usda.gov](http://www.ers.usda.gov)

(QCEW) data to aggregate employment (see Figure 2) in these non-metro counties for 2007, 2008, and 2009 (available through Quarter 3, 2009).

The 66 counties for which the data are available in this sample had total employment of 562,975 in the third quarter of 2009, representing 22 percent of employment in the state of Minnesota. Agriculture and manufacturing, of course, play a large role in rural employment. For example, these non-metro counties account for 30 percent of total manufacturing employment in Minnesota. Rural counties are particularly vulnerable to economic weakness given their relative dependence on these types of sectors: the employment data bear out the extent to which the goods-producing sector of the economy has been disproportionately affected by recessionary conditions. The Minnesota manufacturing sector has been particularly hard hit in this downturn, and non-metro counties certainly found 2009 to be a tough year in manufacturing. Year-over-year job losses in rural manufacturing continued to pile up through the third quarter of 2009. For example, the third-quarter 2009 loss of jobs in Minnesota rural manufacturing was 13 percent relative to the prior year. This is much weaker than overall rural job loss of 4.5 percent over the same period. These numbers are also similar to those observed for the state of Minnesota as a whole. Rural Minnesota has therefore not been able to avoid the weakness found in the entire state. Over this same period, overall Minnesota employment declined 5 percent and the Minnesota manufacturing sector shed 12.1 percent of its jobs (Figure 3). It remains to be seen if these manufacturing jobs will return when the overall economy returns to its long-term potential growth trend.

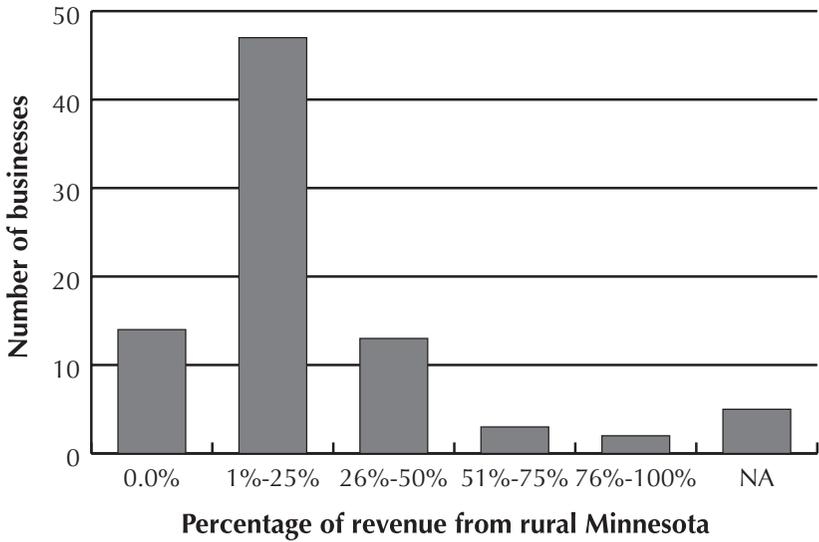
We have been studying the St. Cloud area economy for many years. The St. Cloud area has some resemblance to non-metro counties to the extent that St. Cloud has long had a disproportionately large share of its workers employed in manufacturing. It is also located in a county that is in close proximity to numerous non-metro counties. We have therefore had a special interest in the impact of the rural economy on the St. Cloud area.



**Figure 3:** Growth in manufacturing employment has declined much faster than in overall employment since Q1 2008.

For the past eleven years, we have been surveying St. Cloud area business leaders each quarter on key business conditions that are affecting their company as well as their future outlook. We also ask them special questions designed to address timely issues. We believe the sample of survey respondents is representative of overall business conditions in the St. Cloud area. Survey results have consistently and reliably tracked the performance of the state and national economy. (While the identities of the St. Cloud area firms responding to the survey have always been kept confidential, key characteristics of those firms surveyed can be found at [http://www.scapartnership.com/files/file/reports/qr\\_oct\\_2006.pdf](http://www.scapartnership.com/files/file/reports/qr_oct_2006.pdf).) In February 2010, we surveyed 84 St. Cloud area business leaders about the importance of the rural economy to their firms. (The survey response rate was 79 percent, out of a total of 106 firms that were mailed the survey.) We asked firms the following question:

Approximately what percentage of your company's total revenues comes from each of the following areas?



**Figure 4:** The percentage of revenue St. Cloud businesses derive from rural customers.

- St. Cloud Area
- Twin Cities Metro
- Twin Cities-St. Cloud Corridor
- Other Minnesota Metropolitan Areas
- Rural Minnesota
- States in the U.S. other than Minnesota
- Foreign Countries

While a full analysis of these results can be found at <http://www.scapartnership.com/files/file/Winter%202010QBR.pdf>, it is interesting to note how important sales in rural Minnesota are in St. Cloud (Figure 4). Only 14 of the 84 surveyed firms indicate they receive no revenues from rural areas. Forty-seven firms receive between 1 percent and 25 percent of their revenues from rural Minnesota, and 13 firms receive between 26 percent and 50 percent of their revenues from rural sources. Five surveyed firms receive more than half of their revenues from rural Minnesota. It should be noted that 41 of the 84 surveyed firms receive *at least* 10 percent of their revenues from rural sales.

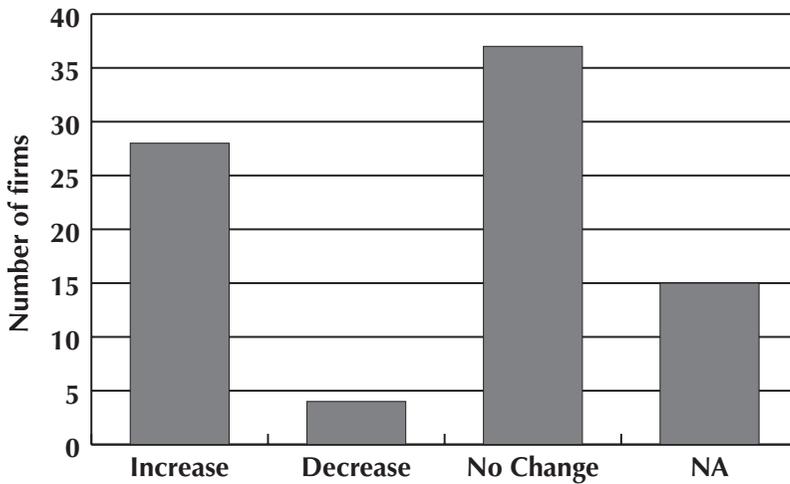


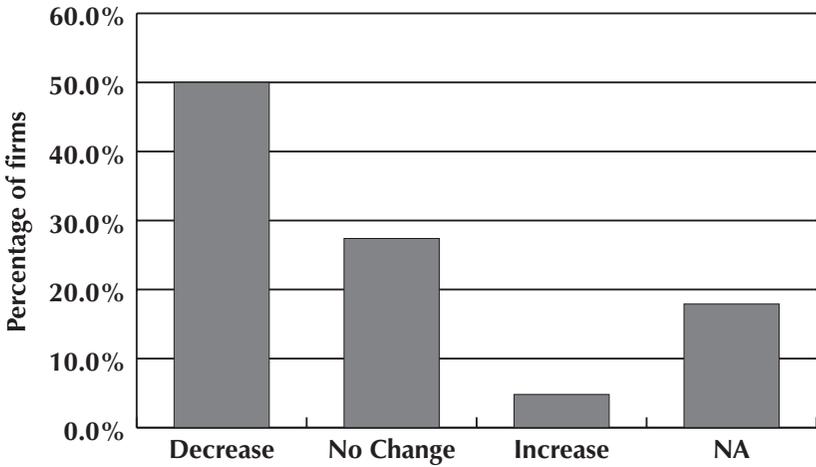
Figure 5: St. Cloud firms' expectations for revenue from rural customers over the next five years.

Clearly, most St. Cloud area businesses are highly dependent on rural customers, and this tendency is expected to grow in importance over the next several years. We asked firms:

“Over the next five years, how do you expect your company’s share of total revenues to change [in each of the areas asked about in the prior question]?” Twenty-eight (33%) St. Cloud area firms expect an increase in the share of revenues coming from rural areas, while only four firms expect a decrease in revenue share from rural customers (Figure 5). While we have no evidence to suggest that the St. Cloud area results can be generalized to include other areas of the state, we suspect similar results would be found in locations like Mankato, Duluth, Fargo-Moorhead, Grand Forks, and Rochester.

To the extent that these results do apply to other areas in Greater Minnesota, it is interesting to look at how the recession has impacted St. Cloud area firms’ sales in rural Minnesota (Figure 6). In the February 2010 survey, we asked St. Cloud area firms:

“To what extent has the recession impacted your company’s sales in rural Minnesota?”



*Figure 6: How the recession has affected St. Cloud businesses' sales from rural customers.*

Fifty percent of surveyed firms report a decrease in their sales to rural areas, while 27 percent of firms report no change. Five percent of firms actually reported an increase in rural sales. The recession and the associated weakness in manufacturing and agriculture has no doubt damaged incomes of rural residents. This shows up in spending in every sector of the area economy — from retail sales to business services.

St. Cloud area firms had some interesting comments regarding the impact of the recession on their rural sales. By and large, most survey respondents report that sales to *all* customers have declined. So, while any firms that are exposed to weakness in rural manufacturing and agriculture are likely to have been disproportionately harmed by a decline in the rural economy, the impact of this weakness has been nearly universally felt. Some firms submitted written comments that are interesting. These comments include:

- From an engineering firm: “We do work for many municipalities. They are doing less.”
- From a real estate firm: “Lake shore real estate sales (are) down.”
- From a construction firm: “There are fewer construction

- projects in general, which causes the decrease.”
- From a commercial real estate firm: “Real estate sales volume is down.”
- From a firm that relies on advertising sales: “Slight decrease (in rural areas). Sales have decreased faster in our urban markets.”
- From a landscaping firm: “I have learned that 25 landscape companies within 50 miles of St. Cloud have gone out of business and that will double if no money or work comes available.”
- From a manufacturing firm: “The recession has caused an overall downturn in business. For us, rural Minnesota has followed the trend.”
- From a building supply company: “The housing market in rural areas doesn’t seem to be hit as hard as metro areas.”
- From a professional services firm: “Rural school districts and cities and counties don’t have the funds to purchase (our services).”
- From a roofing firm: “More activity from other contractors that didn’t work in these areas before.”
- From an automobile dealership: “Farm economy seems poor.”
- From a public utility: “Decrease in farm prices has reduced sales. Capital investment in agricultural sector is down. Housing-related manufacturing (is) hurting.”

Prior to the recession, St. Cloud area firms were benefiting from strong sales to agricultural interests who were enjoying high farm prices. For example, milk prices have only recently started to rebound from a precipitous decline that dates back to the beginning of the national recession in December 2007 (Figure 7). At a current price of \$15 per hundredweight, milk prices are still well below the peak price of \$22 in late 2007. Wheat and corn prices trade at about half their peaks in the summer of 2008 (Figures 8 & 9). Global recovery and an increase in energy prices can be expected to have a favorable effect on Minnesota agriculture. Corn prices in particular will benefit from an improved economic outlook and the accompanying revival in ethanol demand.

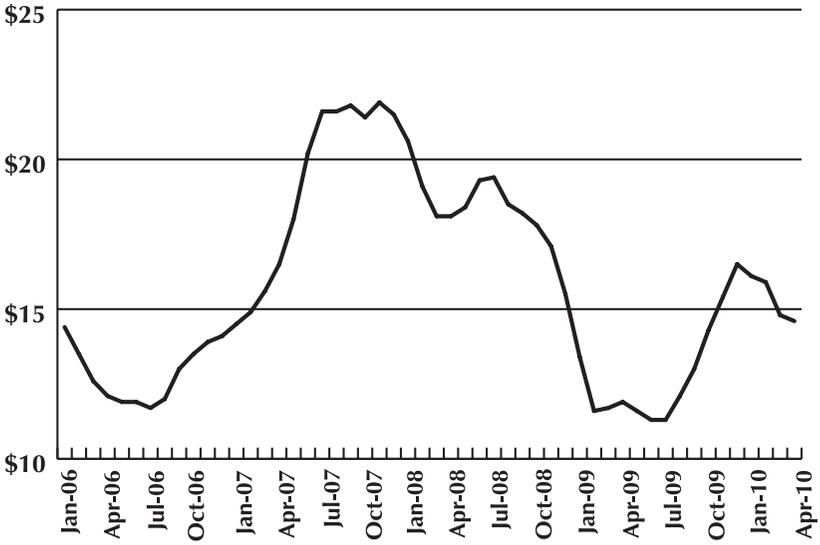


Figure 7: Milk prices, 2006 to today.

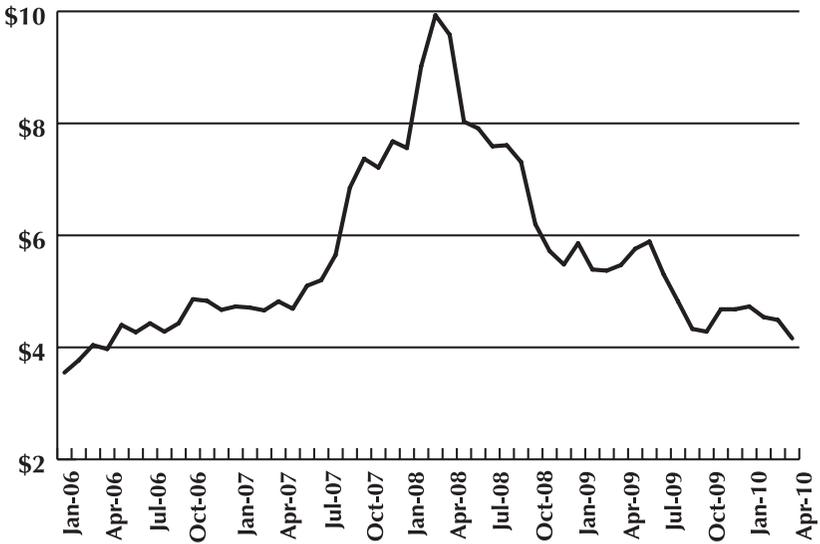


Figure 8: Wheat prices, 2006 to today.

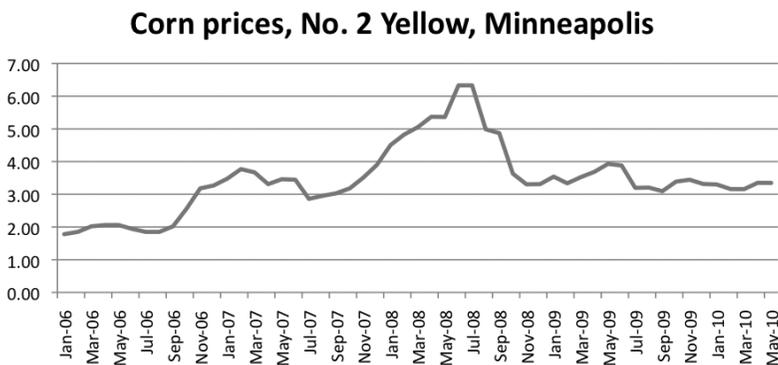


Figure 9: Corn prices, 2006 to today.

#### IV. What does the future look like in the Minnesota rural economy? Some concluding remarks.

We now know that the most recent recession was the worst that the U.S. has experienced since the Great Depression. Indeed, commentators have aptly named it the Great Recession. As we write this article, U.S. unemployment rates are at 9.7 percent, federal budget deficits are more than 10 percent of GDP, the Federal Reserve’s balance sheet has expanded by \$1.4 trillion from pre-crisis levels as they have become the *buyers of last resort* of varied debt instruments in financial markets, uncertainties in Europe threaten recovery in that part of the world, and a host of other factors make it quite possible that it will be some time before U.S. economic performance returns to what is considered normal. All of these factors make it very hard to figure out what a *cyclical* recovery will look like. Combine this uncertainty with the *structural* change that is also going on in rural Minnesota’s demography, and you have a recipe for a very uncertain outlook. Policymakers have been curiously quiet on how to shape public policy when cyclical events collide with structural/ demographic events.

At the same time that rural Minnesota is trying to recover from the Great Recession, it will be experiencing some unpleasant trends. Dependence on agriculture and manufacturing makes rural Minnesota highly vulnerable

to conditions that are beyond its control. While the long-term outlook for agricultural commodities seems reasonably favorable, this doesn't always translate into jobs. Combine this with the historical variation in farm prices (and profit margins), and it is easy to see why many young workers flock to urban areas and the relatively abundant service-providing jobs found there. The outlook for manufacturing is decidedly worse. If rural Minnesota continues to hold a 30-percent share of overall Minnesota manufacturing employment, it will only be because other areas are experiencing declines at the same pace or greater.

This reality needs to be translated into rural economic development policy. The economic development literature is full of pleas to pursue more enlightened 21st Century economic development policy, so we will simply add our concerns to those that have already been voiced. There really isn't much we can add to this, other than to simply remind people that if public officials feel the need to direct resources to targeted economic development uses, it will be essential in the coming years to take a regional approach to resource allocation. The traditional approach to using local tax incentives to attract manufacturers (in a heated competition with other localities) is simply too costly relative to any potential benefits it confers. A regional approach will necessarily have to work to a region's strengths—its natural resources, human capital, institutions of higher education, K-12 school systems, successful businesses, nonprofit organizations, transportation infrastructure, etc. — in order to leverage the shared interests of a region.

The federal government will soon need to begin to work down its massive budget deficits. This will happen at the same time that the share of federal spending on entitlement programs (many of which are designed to serve an aging population that accounts for a growing share of the overall population) is increasing. Simply put, governments at all levels are going to be working with very limited budgets. Rural regions are likely to prosper only to the extent that regional cooperation can achieve valued economic development objectives. Unfortunately, these structural/

demographic events are occurring at the same time that the rural economy is trying to recover from a worldwide recession. The temptation will be for public officials to explain weak employment conditions on the slow recovery from the Great Recession. While some of this will no doubt be true, it will be a good idea for these public officials to also keep in mind that they are also battling structural/demographic change. Policy designed to confront this structural/demographic change requires an entirely different arsenal of tools and we cannot expect adverse outcomes to be remedied over a short time horizon.

### **Endnotes**

<sup>1</sup> "Will the Rural Economy Rebound in 2010?" Federal Reserve Bank of Kansas City *Economic Review*, First Quarter 2010, pp. 95-119.

<sup>2</sup> John J. Dominik, *St. Cloud, the Triplet City*. (Woodland Hills, CA: Windsor Publications, 1983) p. 75.