Economic Indicators

Economic Indicators: An Update for the 7 Rivers Region reports on a long-term study of regional economic indicators. The research is ongoing and spans a period of time to enable us to understand and report trends. This project is expected to continuously build on a base of economic information and provide decision makers with valuable tools for strategic planning. The information will also provide a basis for comparison with other regions and a measure of our progress.

State Bank Financial sponsors this research project in collaboration with the University of Wisconsin-La Crosse College of Business Administration and *The La Crosse Tribune*. These programs will continuously build on a base of information and provide decision makers like you with valuable tools for strategic planning.

Specific goals of this project are:

- Support business owners in their business decisions by gathering key local economic indicators and trend information.
- Develop specific economic indicators for this region that are not readily available to decision makers.
- Develop tools to assess our progress in economic growth, prepare baseline measures that will allow comparison with other regions, and measure future progress of the region.
- Track the region's participation in the "new economy" and development in the high tech arena.
- Bring professionals together with business owners for discussion about the local economy and related critical issues.
- Create a business recruitment and retention tool by publishing the information.

Core economic indicators cover the following areas:

- Employment
- Income
- Cost of Living
- Consumer Attitude and Behavior
- Real Estate and Housing
- Interest Rates
- Equity Performance

Economic Indicators and Trends

Taggert J. Brooks, Ph.D., UW-La Crosse Department of Economics

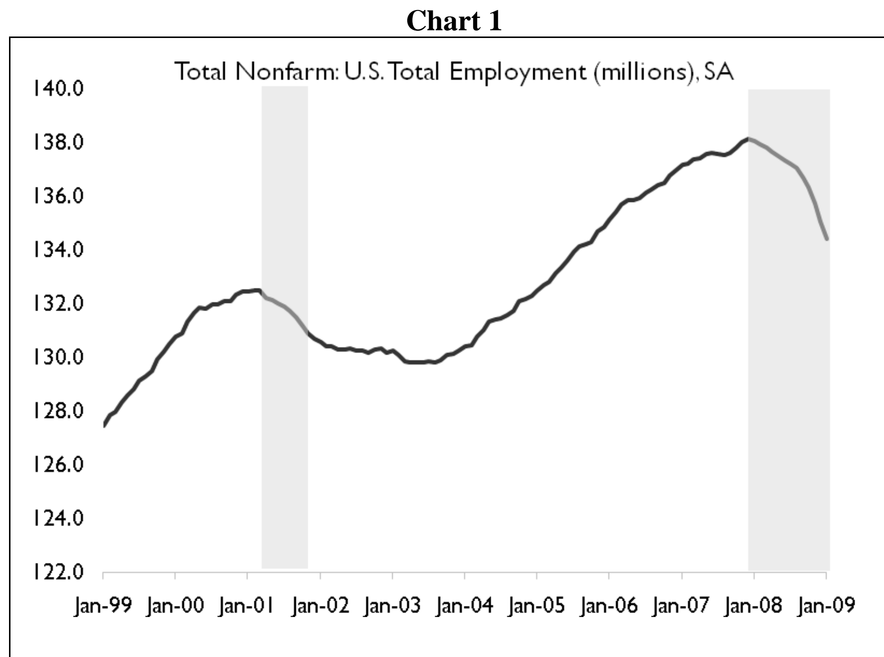
Core economic indicators have been tracked since 2001 to have objective measures for our 7 Rivers Region economy. The special focus of the spring meeting is finding creative problem-solving strategies for dealing with tough economic times. Dr. Brooks begins with some observations on the US economy and moves on to some regional comparisons.

Note: Dr. Brooks recently launched the 7 Rivers Region Economics blog, which will contain ideas and writings that might or might not be included in this publication provided at the Economic Indicators breakfast meeting. Dr. Brooks will use the blog to track different topics and collect ideas. The Web address is: http://sevenriversecon.blogspot.com/.

The Recession

On December 1, 2008 the National Bureau of Economic Research (NBER)[1] identified the peak of the latest expansion as occurring in December of 2007. As they did for the last recession, they identified the peak in the business cycle concurrent with the peak in employment. Chart 1 plots the non-farm payroll employment figures with the recessions shaded in grey. Chart 2 compares the current contraction in employment relative to the last two recessions in terms of cumulative job loss measured as a percentage of employment since the peak.

Chart 1



While media reports have claimed that this recession is the worst since the Great Depression, we need to be careful about identifying the appropriate metric for comparison. In terms of the number of job losses this is certainly a bad recession, but when measured as a percentage of

1. http://www.nber.org/cycles/dec2008.html

employment the current recession began much as the last two recessions began. The worrisome fact is that job losses appear to have accelerated relative to previous recessions, which by now would have subsided. Yet from Chart 2 we can see that the current recession does not appear to have hit the bottom.

Chart 2

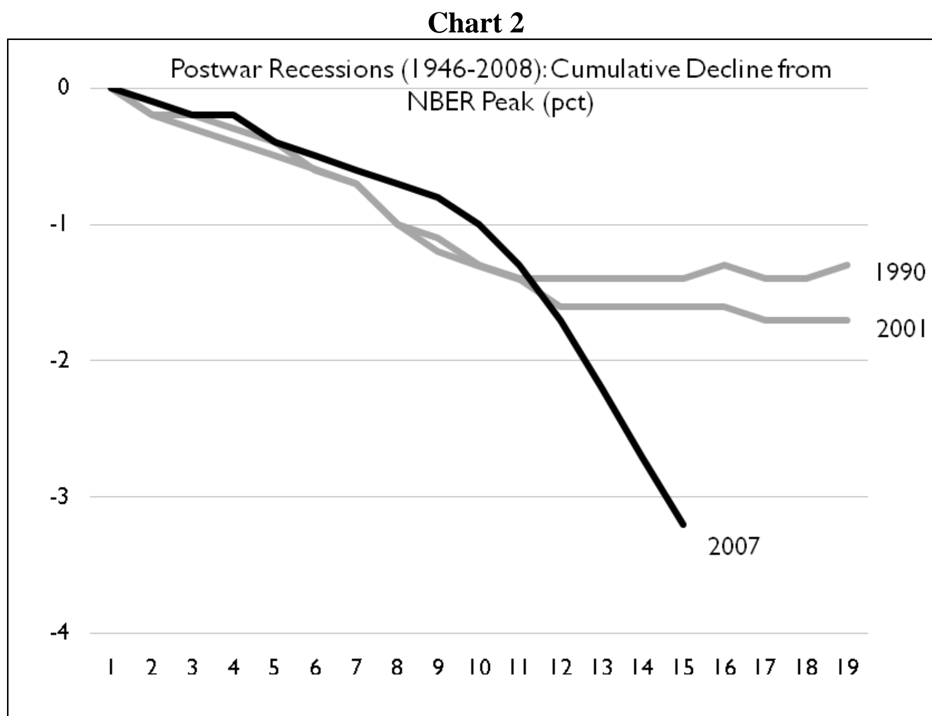


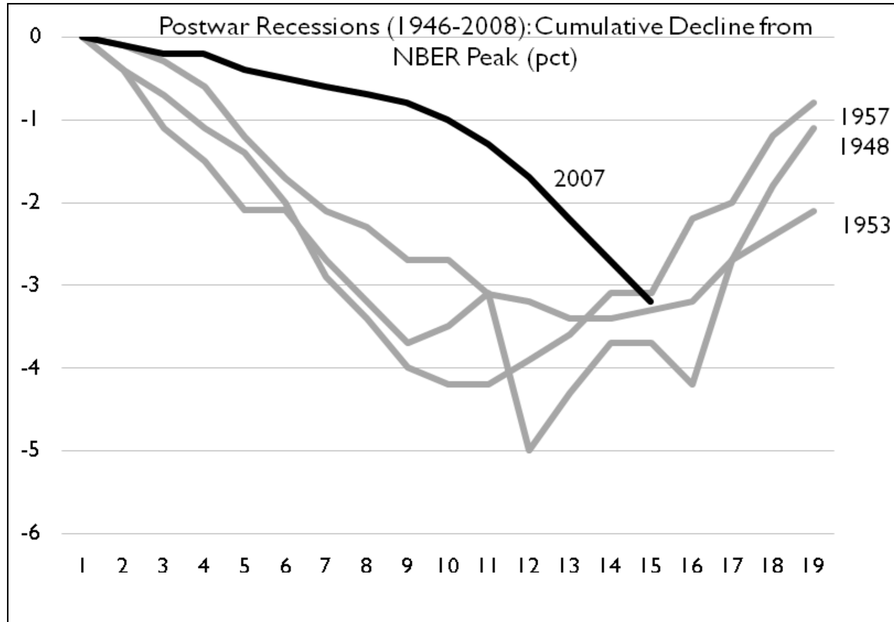
Chart 3 demonstrates the depth, in terms of employment losses, of the recessions following WWII. It's obvious from the chart those recessions were typified by much sharper contractions in employment and much sharper rebounds relative to both the current recession and the recessions of 1992 and 2001. The changing dynamics of the labor market is likely responsible for the changing nature of the employment response to business cycle contractions. Whereas the recessions immediately after WWII involved mainly layoffs due to depressed demand, modern recessions appear to involve permanent job loss from job restructuring.

For example, the 2001 recession did not return to the pre-recession level of employment until 48 months after it began, whereas the 1957 recession was back at pre-recession employment levels within 18 months.[2]

Eventually, the economy returns to the employment level that existed before the recession began, but it now appears to take much longer than it used to. That is because it takes workers longer to acquire the new skills needed in the new job market. It takes longer for them to find jobs for which they are well suited and the search process might also involve geographic relocation, which takes time.

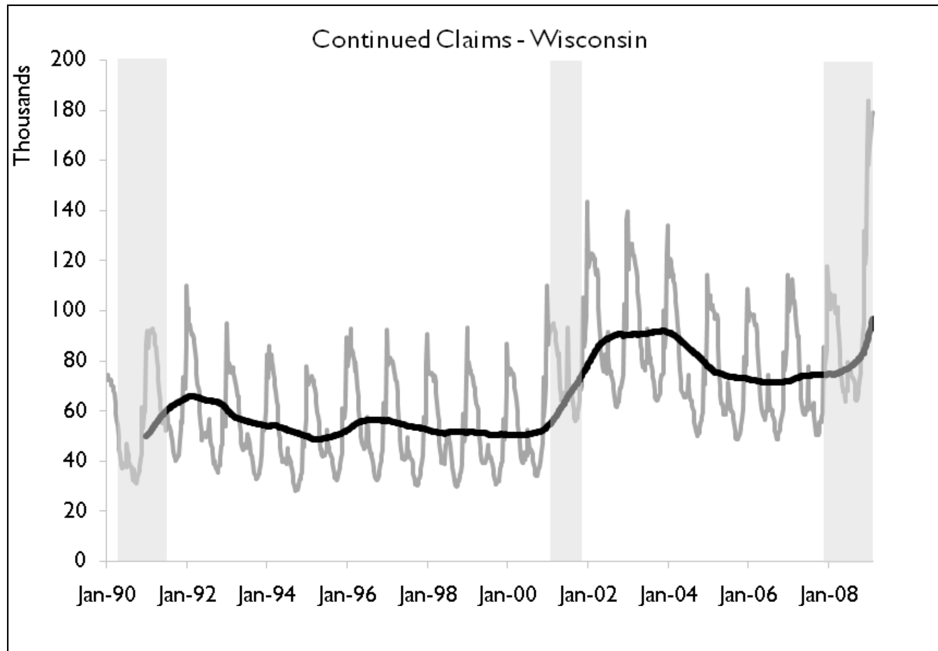
2. http://www.williampolley.com/blog/archives/2009/02/employment-loss.html

Chart 3



The regional labor market looks to be turning worse later than the rest of the country. Wisconsin and Minnesota are more heavily dependent on manufacturing than the rest of the country, and because durable goods orders have fallen so sharply, the manufacturing sector is starting to experience layoffs. Chart 4 shows the very recent uptick in continued unemployment claims for Wisconsin. This recession is likely to find us last in and last out.

Chart 4

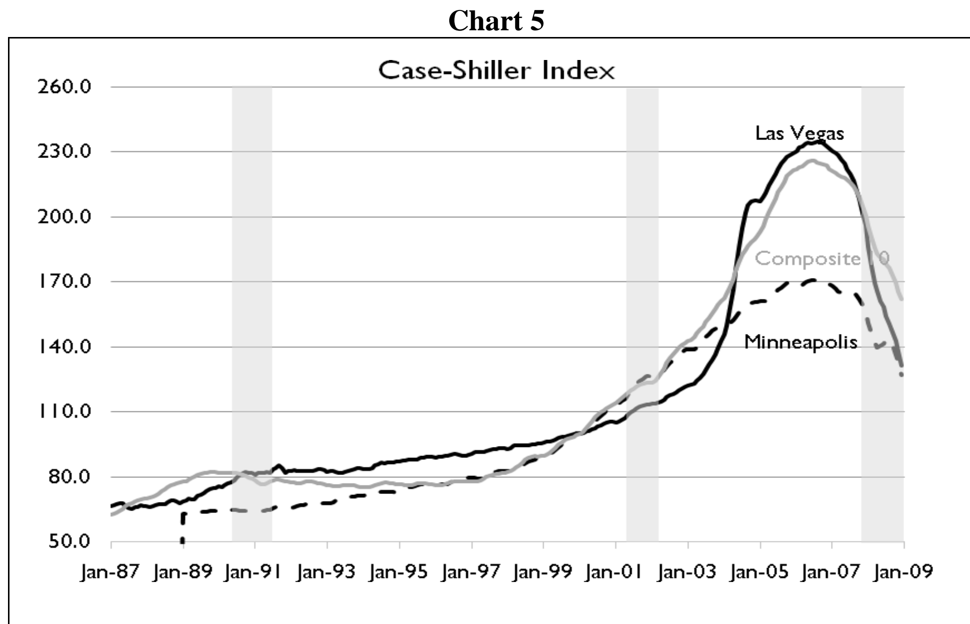


Housing Market

Nationally, the housing market contraction continues to dominate the headlines. Some markets, such as Las Vegas, are down as much as 43.8 percent from their peak. Chart 5 plots the Case-Shiller Composite 10, a collection of prices for 10 large cities, which has experienced about a 28.3 percent decrease since the peak. Minneapolis is down a bit less at a cumulative 25.8 percent from the peak in the summer of 2006. Given that the aggregate value of the US housing stock was around $22.4 trillion during the summer of 2006, a 25 percent decrease in prices implies about a $5.6 trillion loss in wealth.

Estimates of the effect of a change in wealth on consumption put the impact around 5.5¢ for every dollar lost. This implies a reduction in consumption of around $308 billion, or about 3 percent of annual personal consumption expenditures. This effect generally occurs pretty rapidly, with most of it occurring in the first year.[3]

Chart 5

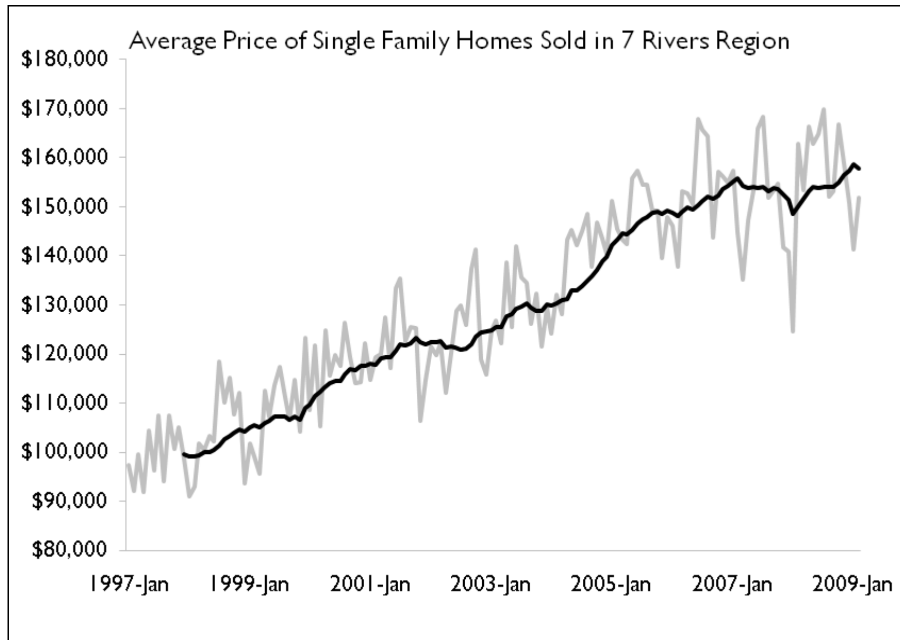


Locally we are in relatively great shape with housing prices continuing to hold up under the stress of increased foreclosures. There are, however, some signs of a slowdown in the local housing market. There were fewer houses sold, as measured by the decreased number of listings sold last year, which fell to 1505 from 1588. The average number of days on the market has risen to 99 from a low of 64 days in 1999.

Fortunately, the continued resistance of local housing prices to the national trends helps to support local consumption. This helps to buffer the local economy from some of the negative effects of the current recession.

3. http://www.jchs.harvard.edu/publications/finance/w04-13.pdf

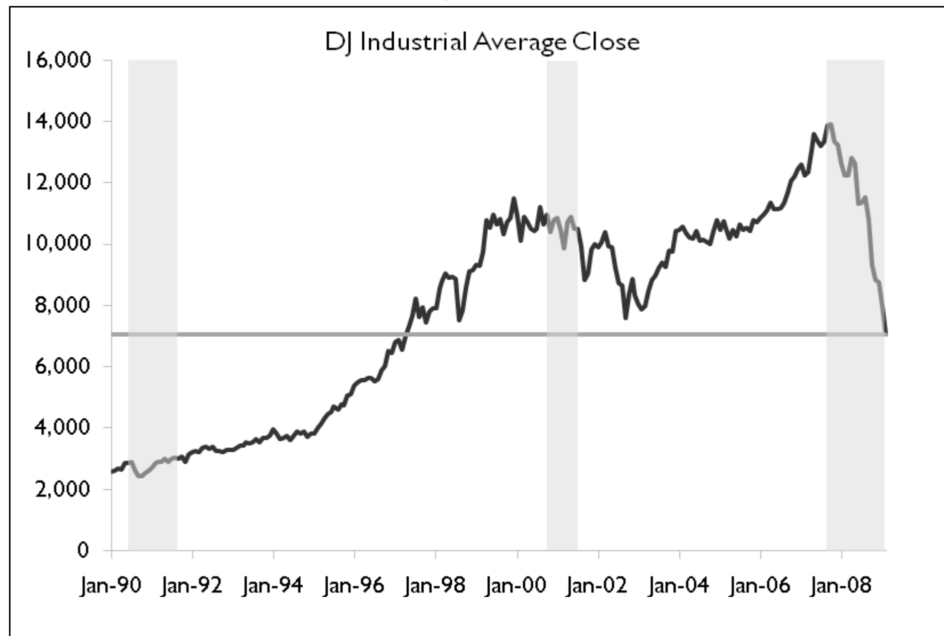
Chart 6



Another source of wealth, albeit a substantially less important source, that fuels consumer spending is the stock market. Most of the major indices are off 50 percent from their peaks. In fact, from the chart below you can see that the Dow Jones Industrial Average (DJIA) has now closed at levels not seen since 1997.

Chart 7 depicts the DJIA close. Chart 8 depicts the 7 Rivers Equity Index and the DJIA, along with the S&P 500.

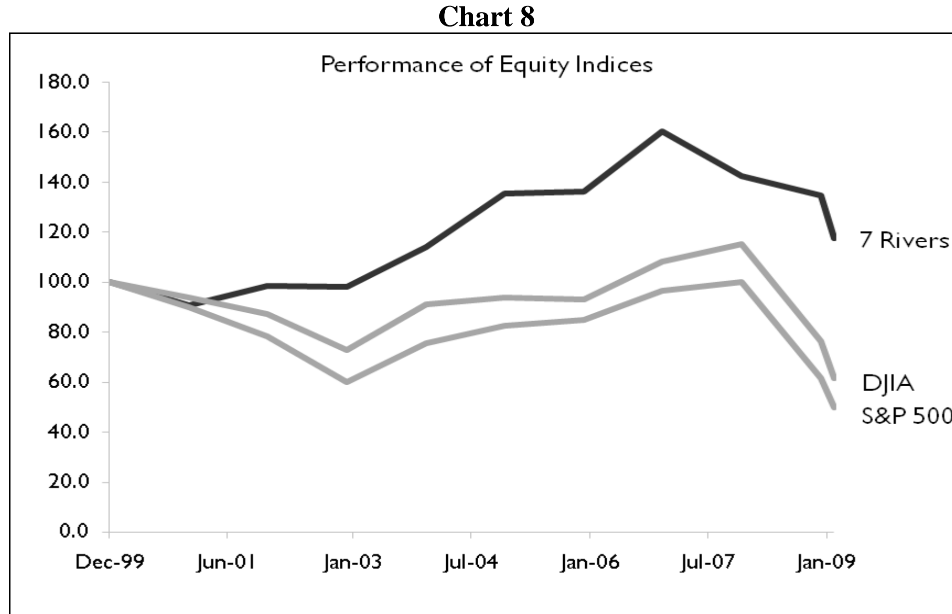
Chart 7



The estimated wealth effect from equity losses is much smaller than from housing. In fact, it is generally imprecisely estimated and some research puts it close to zero. However, this contraction in the equity indices can be expected to exacerbate the contraction in consumption.[4]

Regionally we are doing better than the rest of the nation, as evidenced by Chart 8. Professor Krueger's 7 Rivers Equity Index indicates that local publically traded firms have outperformed the broader market indices.

Chart 8

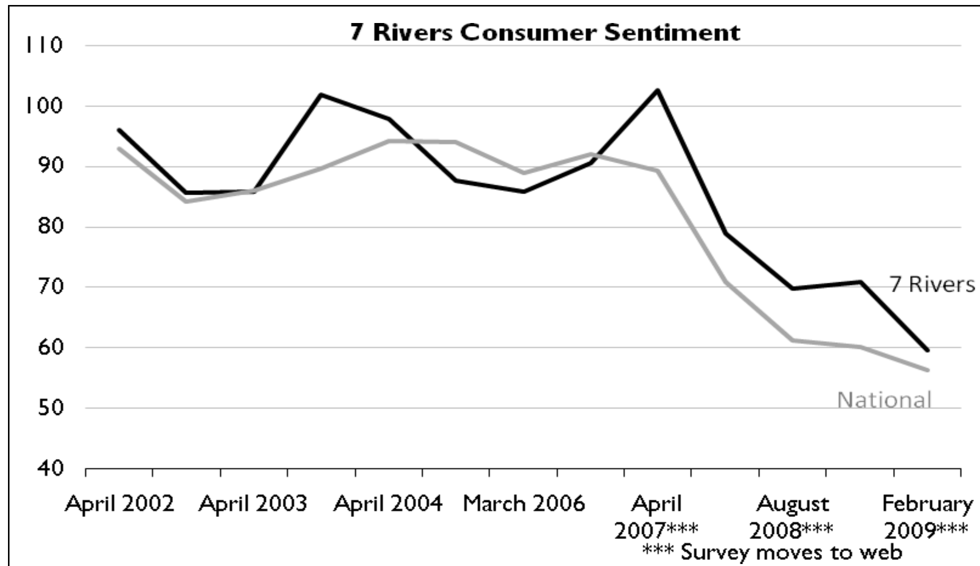


Consumer Sentiment

Given the rapidly changing economy and the ease of use of the new web survey, I conducted two consumer sentiment surveys since the last meeting. In December of 2008 and February of 2009, I conducted the semi-annual consumer sentiment survey for the 7 Rivers Region. Approximately 1,100 current and past participants in 7 Rivers Region events were e-mailed a link to the survey. 238 responses were received for the December survey and 343 were received for the February survey. Chart 9 depicts the overall index for consumer sentiment in the 7 Rivers Region. It generally tracked the national numbers, although it actually rose slightly in December 2008 to 70.9 from 69.9 in August 2008, and fell dramatically in February to 59.7. The rest of the nation experienced a steady decline in overall sentiment from 61.2 to 60.1 and then 56.3 in February.

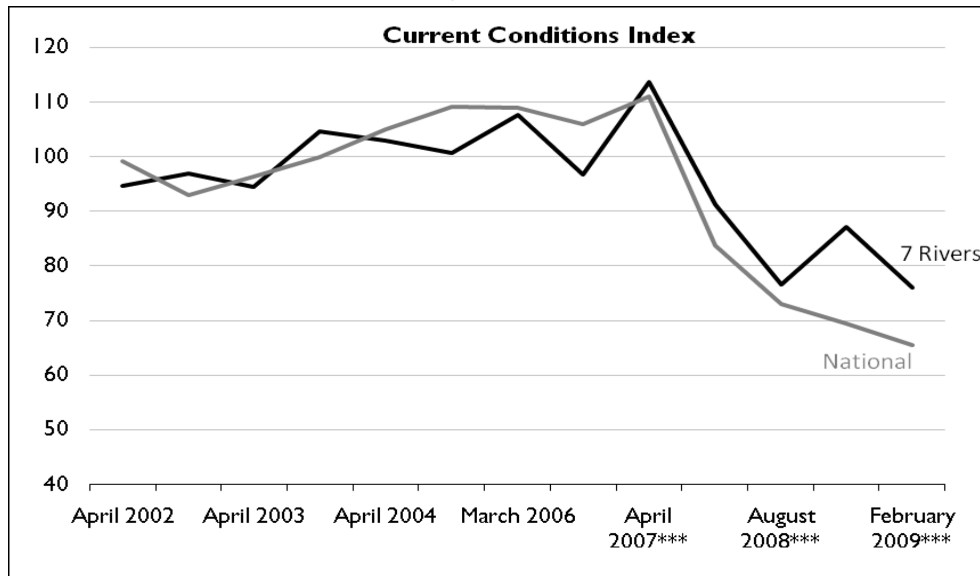
4. http://www.econ.yale.edu/~shiller/pubs/p1181.pdf

Chart 9



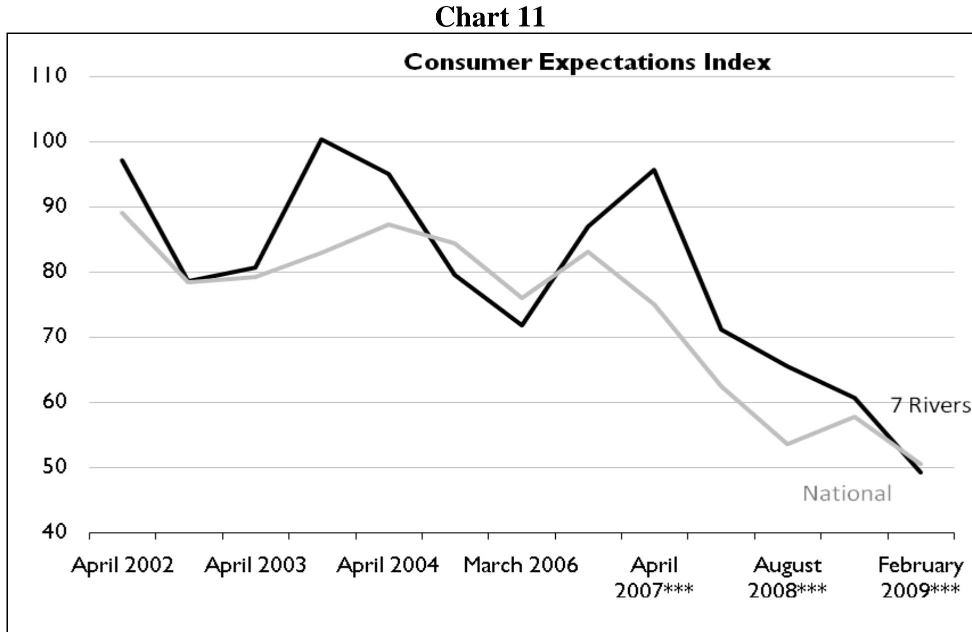
The current conditions index is based on a subset of questions that ask respondents how they are doing now and how they have been doing over the last year. In Chart 10 we see that the 7 Rivers Region appears to have done a bit better than the rest of the nation. The 7 Rivers Region current conditions index rose from 76.5 in August of 2008 to 87.0 in December of 2008 and fell to 75.9 in February. The national index fell from 73.1 to 69.5 in December, then to 65.5 in February.

Chart 10



Turn to future expectations, which are depicted in Chart 11. The local expectations index appears to have taken the biggest hit, with the index of future expectations falling from 65.6 to 60.6 in December and then further to 49.2 in February. The national numbers rose from 53.5 to 57.8 then back to 50.5 over the same time period.

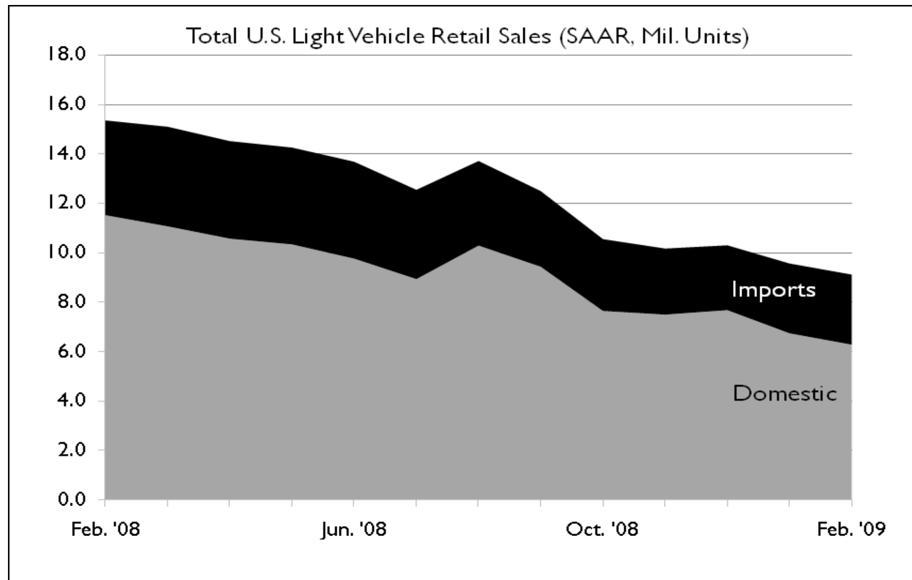
Chart 11



Nationally we've experienced a large drop in consumer's wealth and their confidence in the economy. Locally we've experienced both, but to a lesser degree. One of the obvious ways the loss in wealth has affected consumption is in the purchase of autos. The chart below demonstrates the contraction in auto sales over the last 12 months, which has fallen from a rate of nearly 16 million autos sold per year to less than 10 million sold per year. We've seen this locally with the recent announcement of the Onalaska Saturn dealership closing.[5]

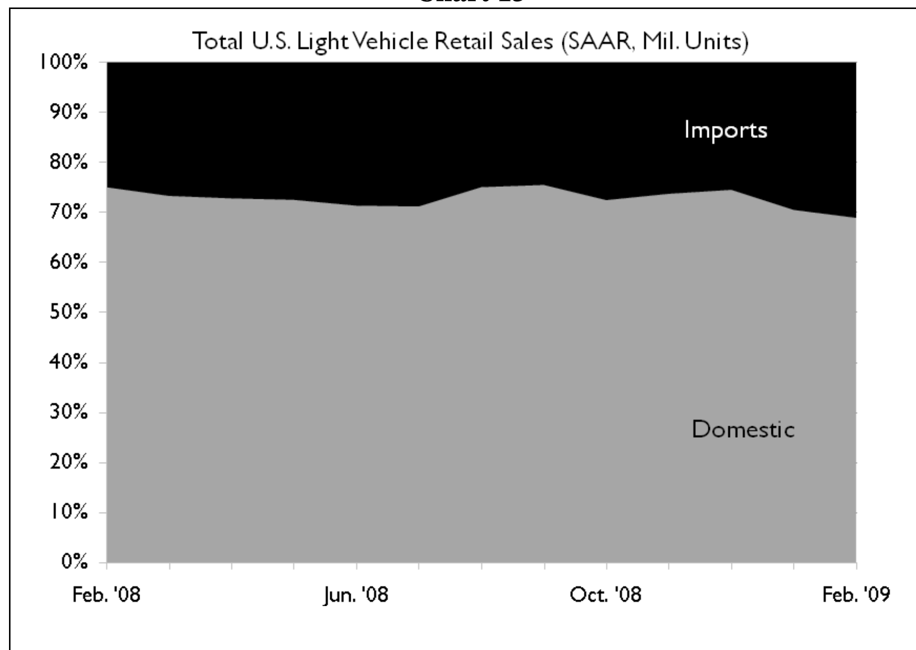
5. http://www.lacrossetribune.com/articles/2009/03/17/news/00lead.txt

Chart 12



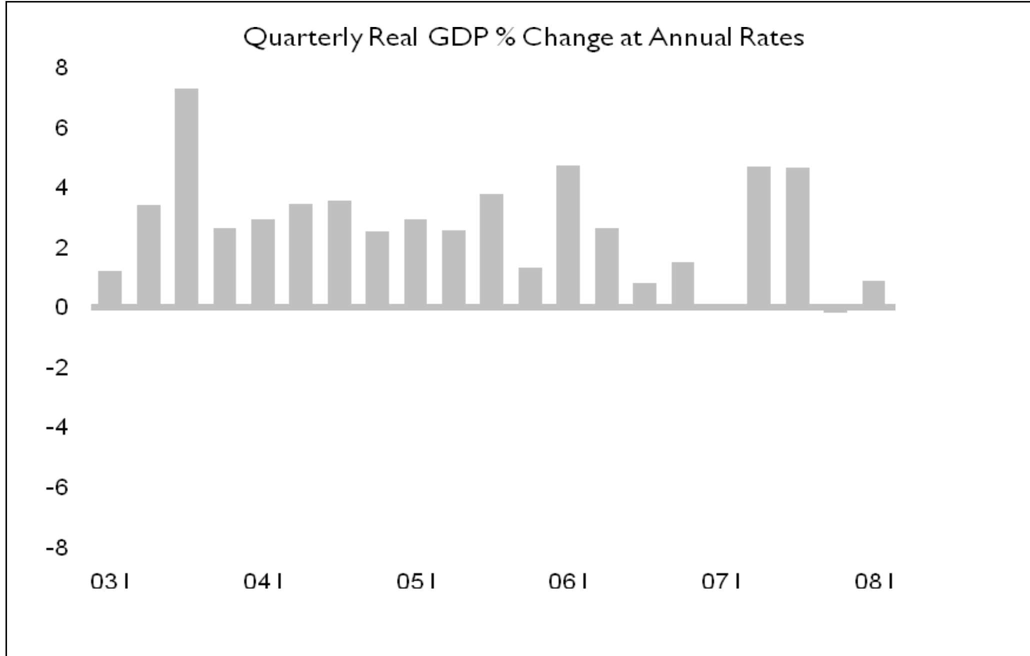
Interestingly, while imports have fallen as well, they have fallen by less than the sales for domestic manufacturers. The following chart shows the increased market share that imports have garnered. The important lesson is that recessions often offer opportunities to grab market share. Obviously, part of the transition to imports in the last year is due to the high gas prices experienced a year ago. People began purchasing smaller more fuel efficient vehicles, which are disproportionately imports.

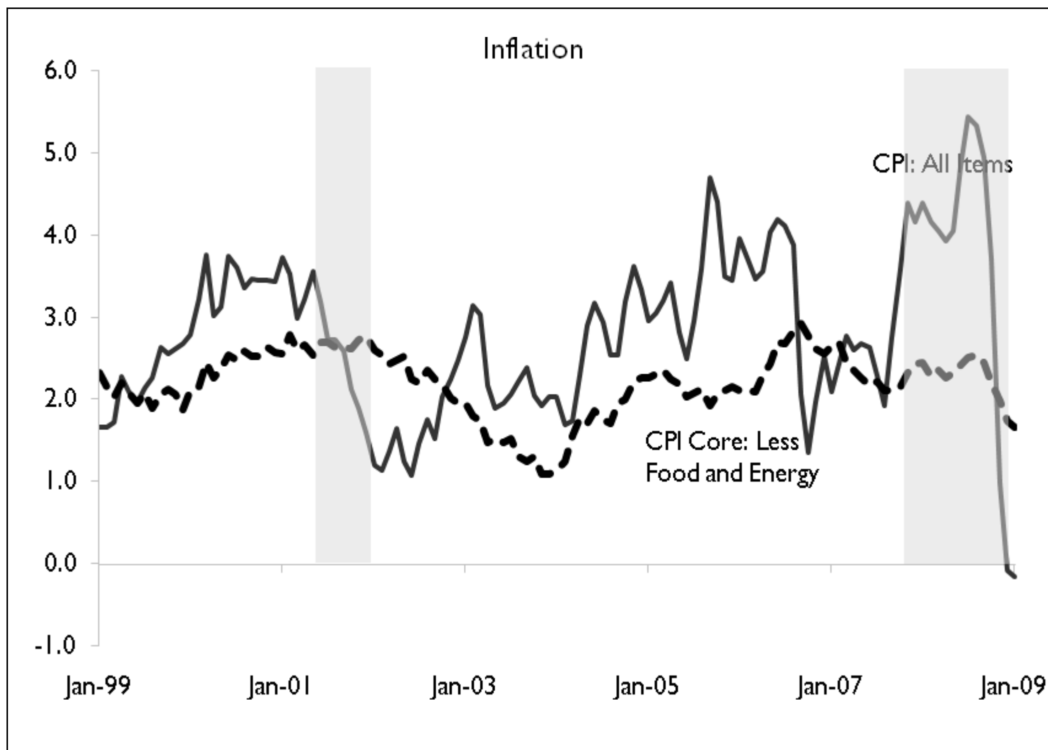
Chart 13



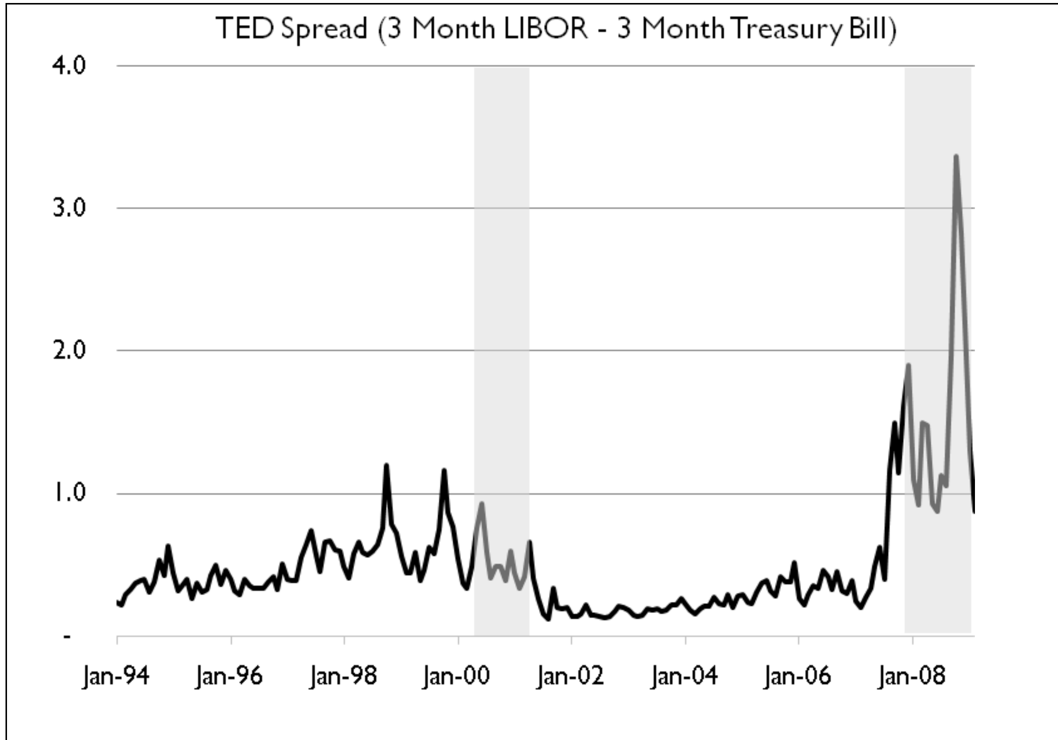
Appendix: Additional Charts

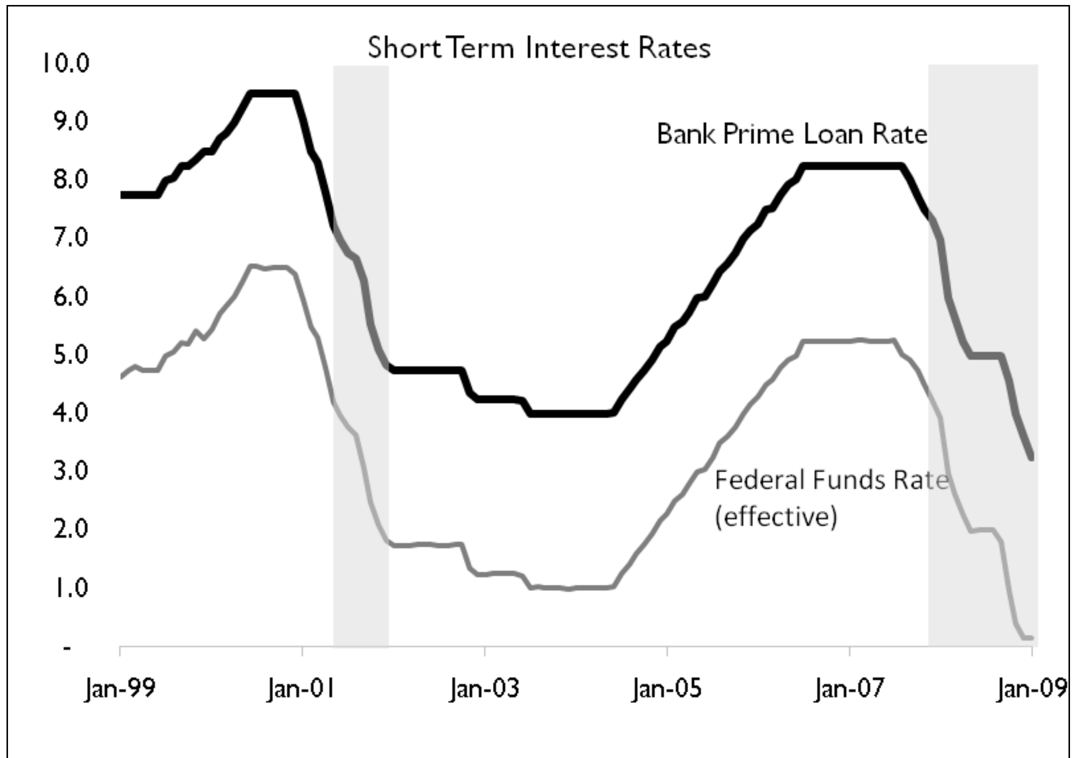
Macroeconomic Indicators

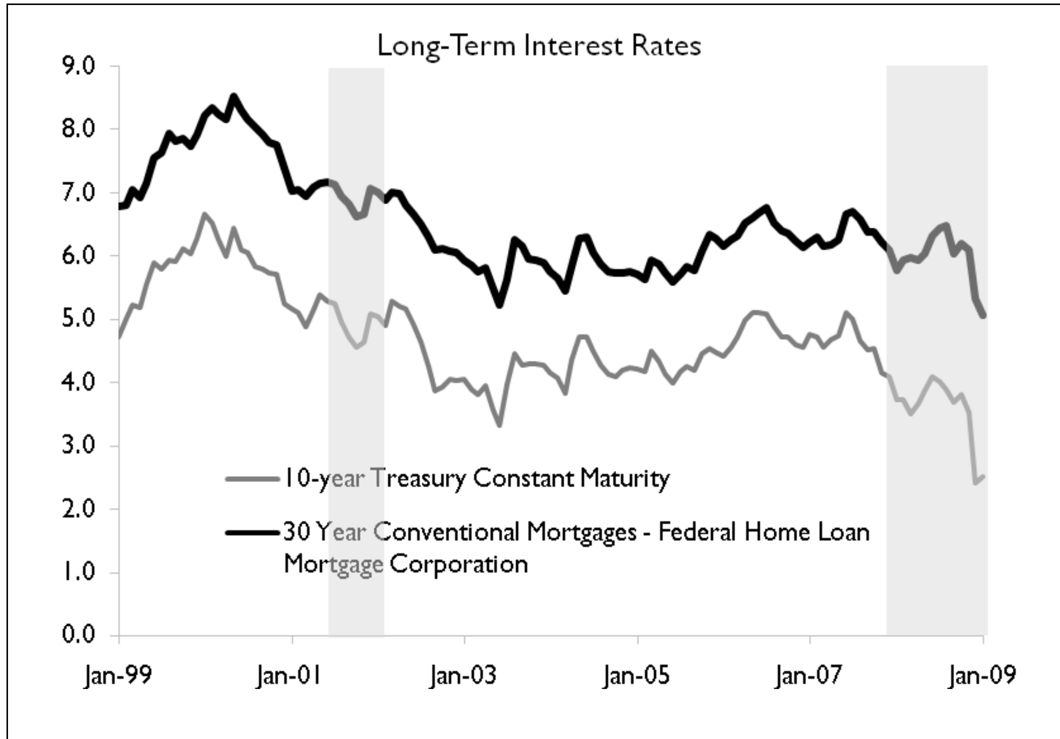


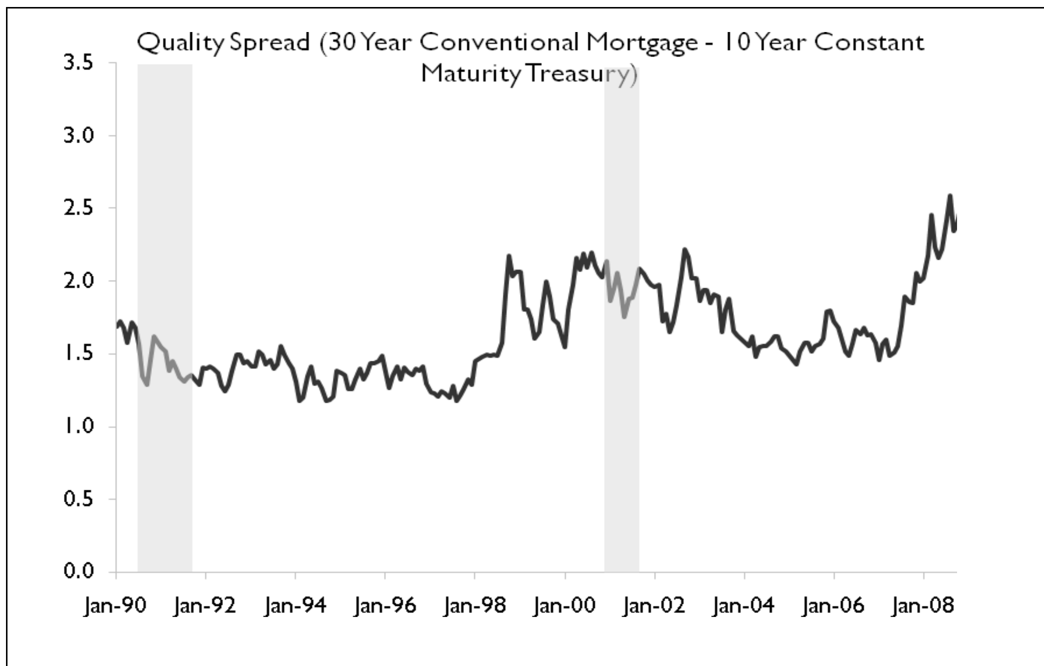


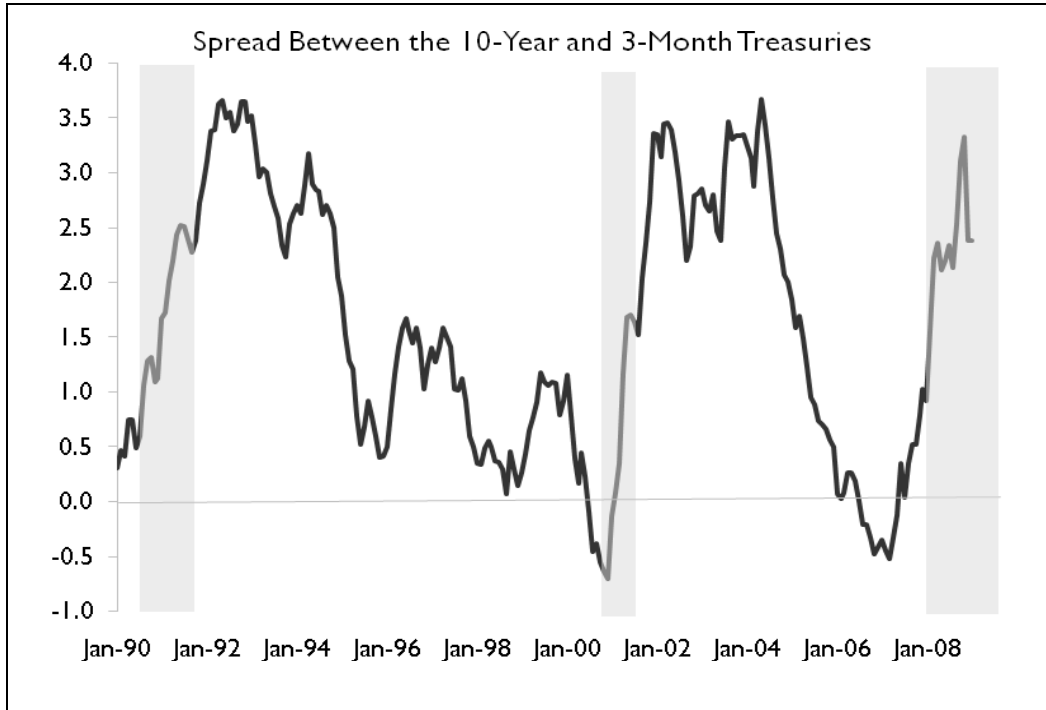
Interest Rate Indicators



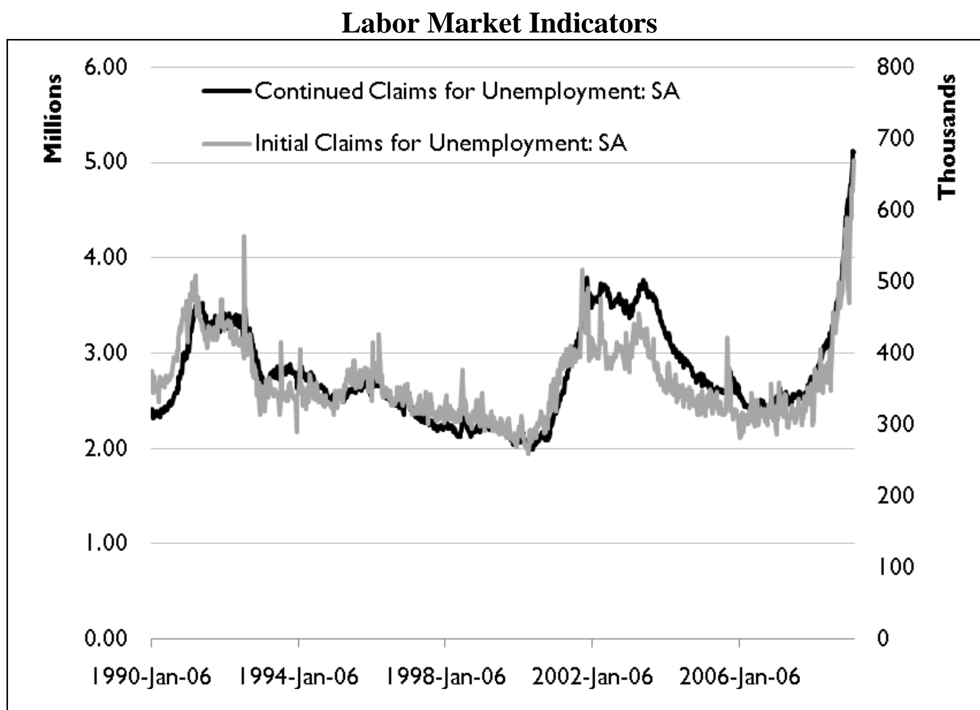


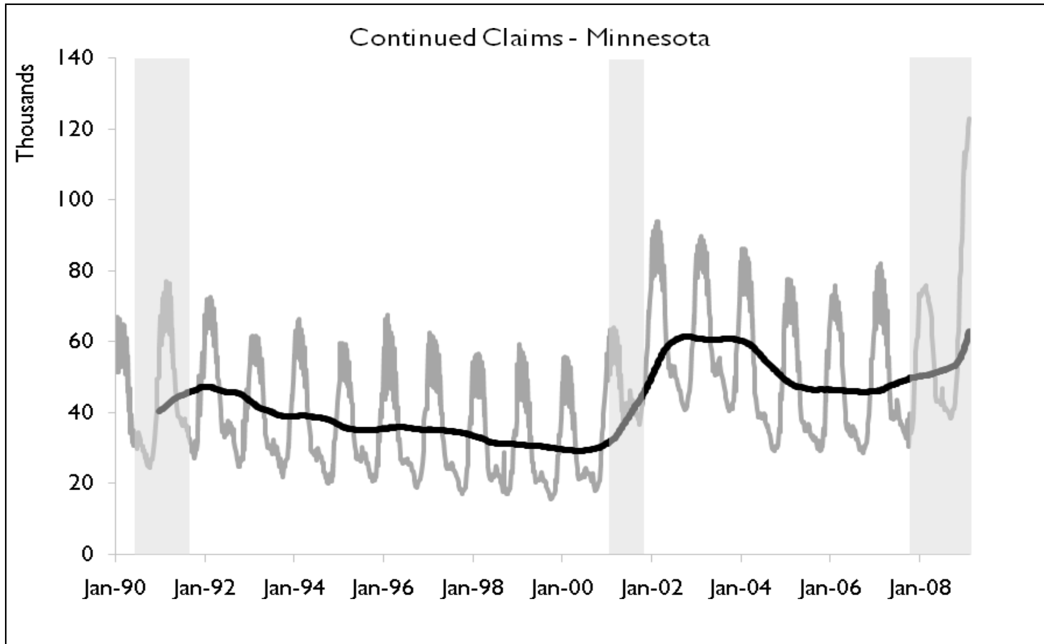

Long-Term Interest Rates
9.0
8.0
7.0
6.0
5.0
4.0
3.0
2.0
1.0
0.0
Jan-99
Jan-01
Jan-03
Jan-05
Jan-07
Jan-09
10-year Treasury Constant Maturity
30 Year Conventional Mortgages - Federal Home Loan Mortgage Corporation

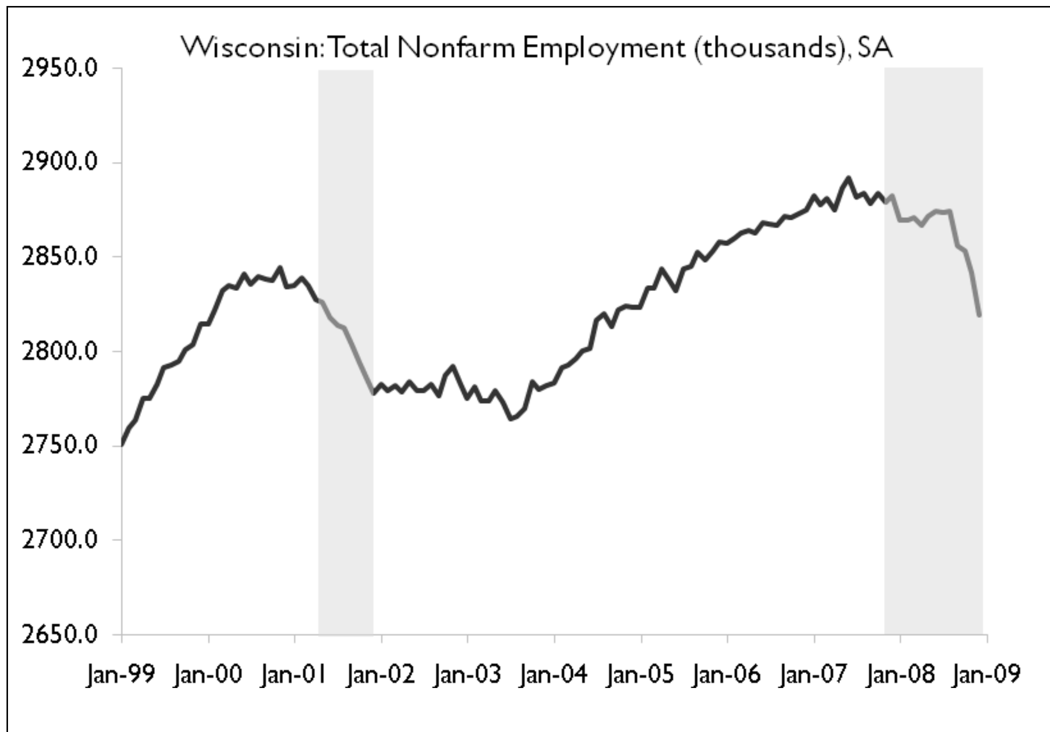

Quality Spread (30 Year Conventional Mortgage - 10 Year Constant Maturity Treasury)
3.5
3.0
2.5
2.0
1.5
1.0
0.5
0.0
Jan-90
Jan-92
Jan-94
Jan-96
Jan-98
Jan-00
Jan-02
Jan-04
Jan-06
Jan-08

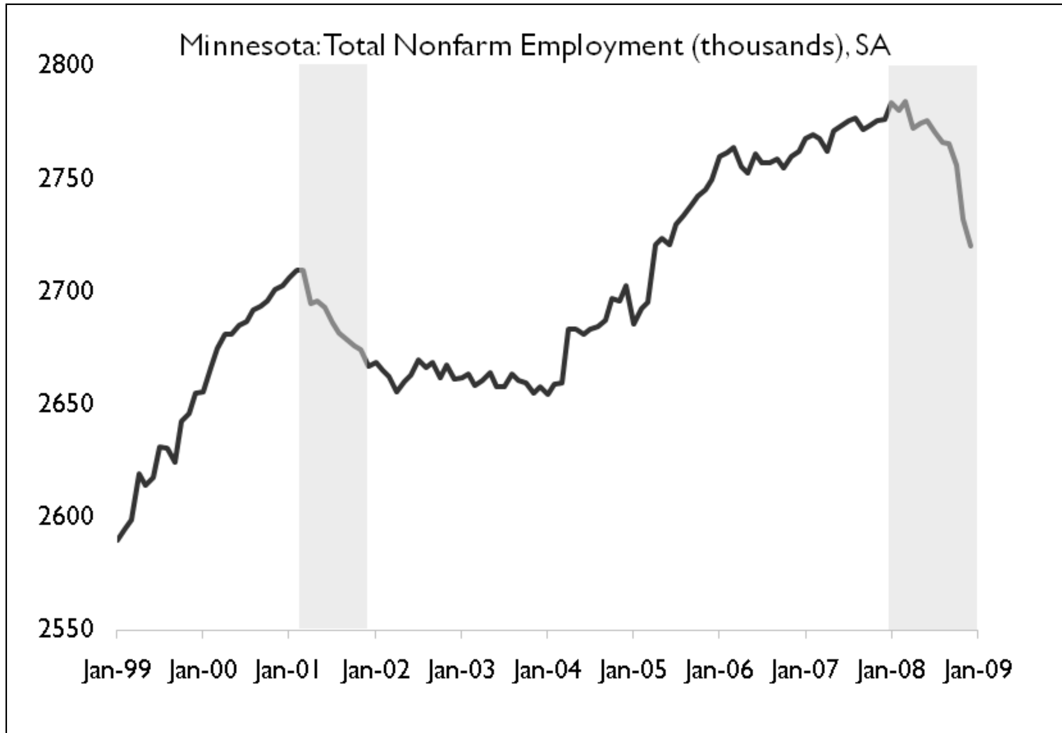


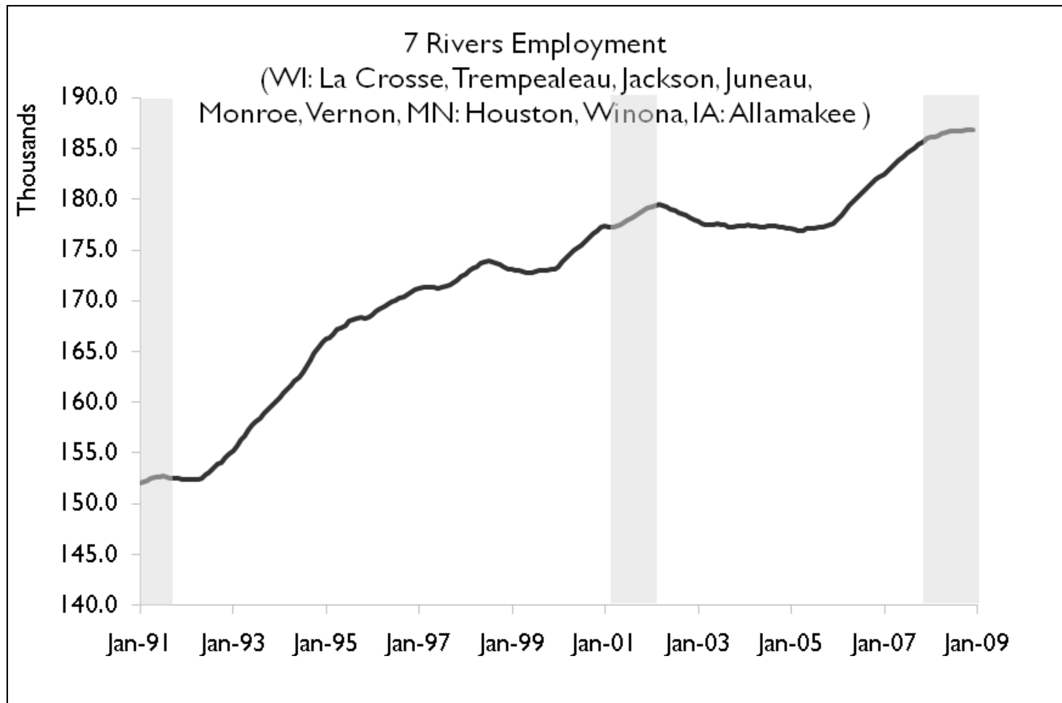
Labor Market Indicators

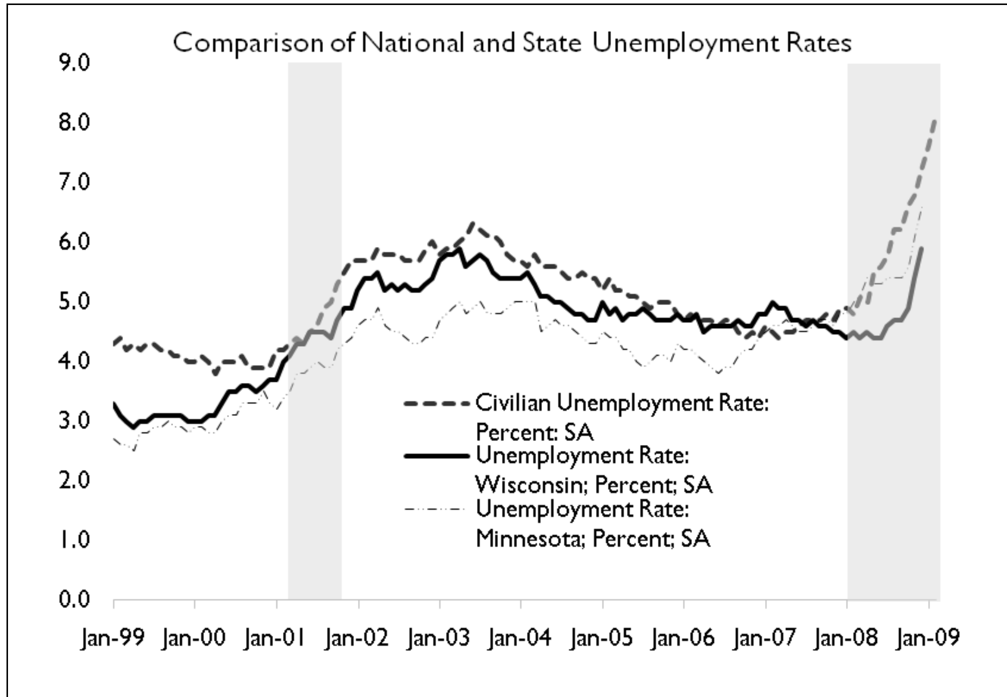


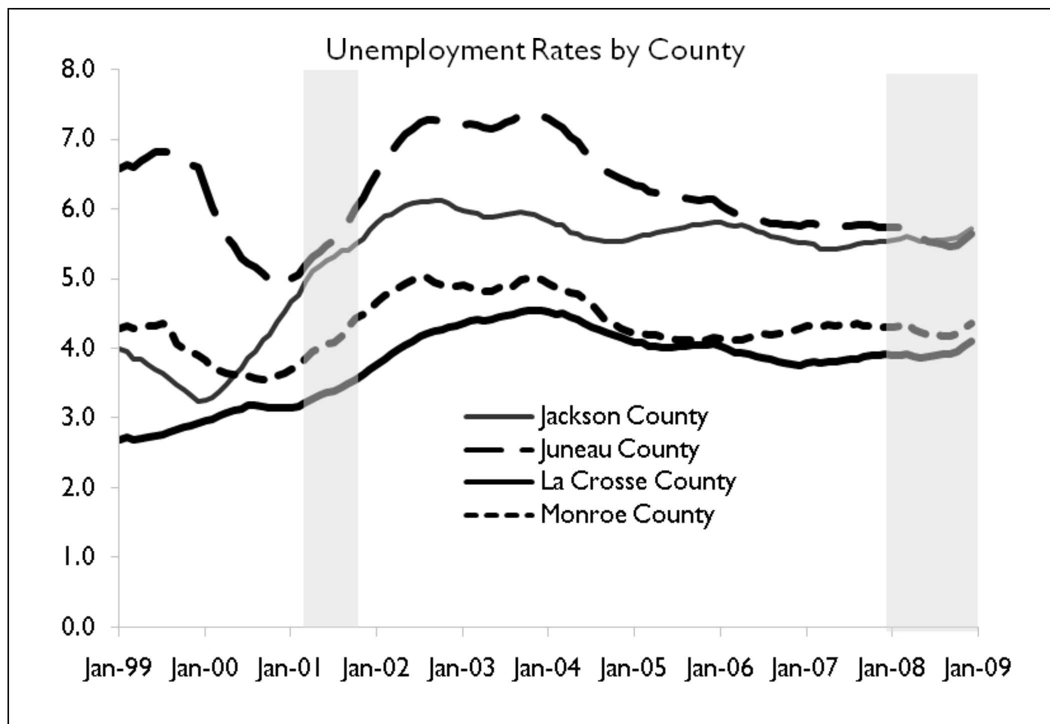

Continued Claims - Minnesota
Thousands
140
120
100
80
60
40
20
0
Jan-90
Jan-92
Jan-94
Jan-96
Jan-98
Jan-00
Jan-02
Jan-04
Jan-06
Jan-08

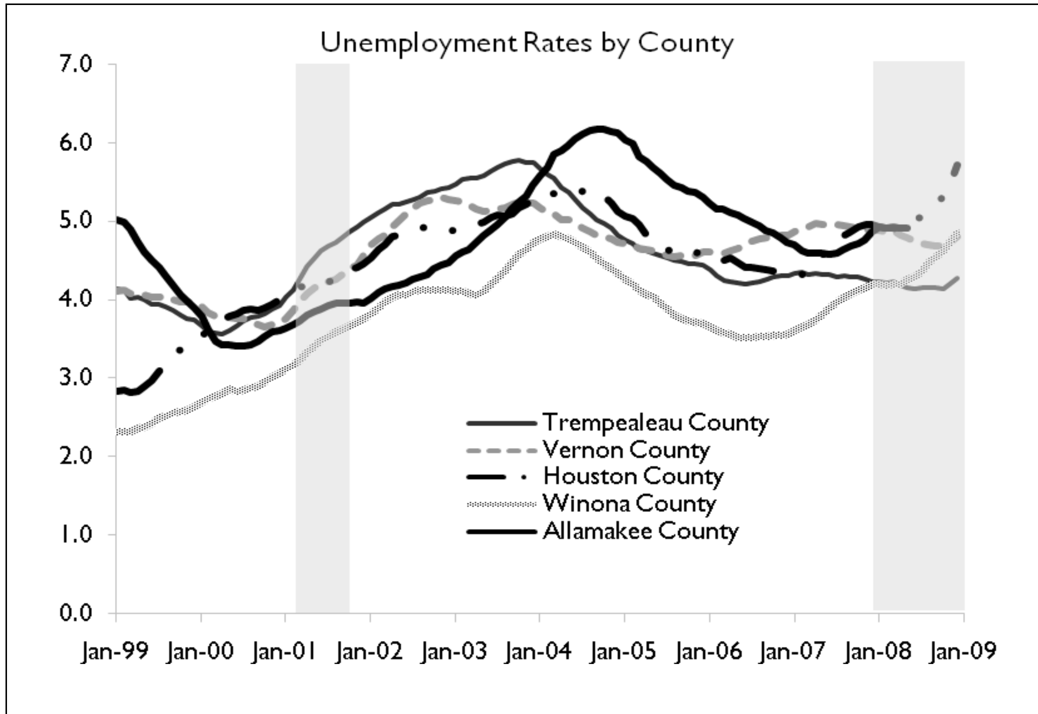

Wisconsin: Total Nonfarm Employment (thousands), SA
2950.0
2900.0
2850.0
2800.0
2750.0
2700.0
2650.0
Jan-99
Jan-00
Jan-01
Jan-02
Jan-03
Jan-04
Jan-05
Jan-06
Jan-07
Jan-08
Jan-09


Minnesota: Total Nonfarm Employment (thousands), SA
2800
2750
2700
2650
2600
2550
Jan-99
Jan-00
Jan-01
Jan-02
Jan-03
Jan-04
Jan-05
Jan-06
Jan-07
Jan-08
Jan-09

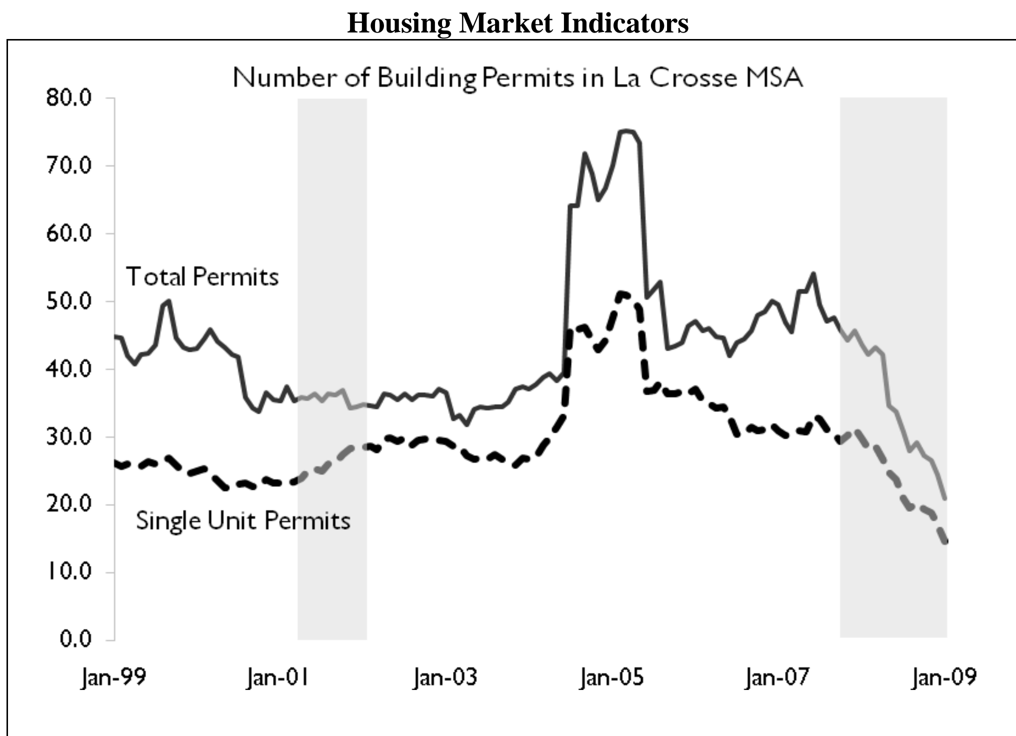

7 Rivers Employment
(WI: La Crosse, Trempealeau, Jackson, Juneau,
Monroe, Vernon, MN: Houston, Winona, IA: Allamakee)
Thousands
190.0
185.0
180.0
175.0
170.0
165.0
160.0
155.0
150.0
145.0
140.0
Jan-91
Jan-93
Jan-95
Jan-97
Jan-99
Jan-01
Jan-03
Jan-05
Jan-07
Jan-09

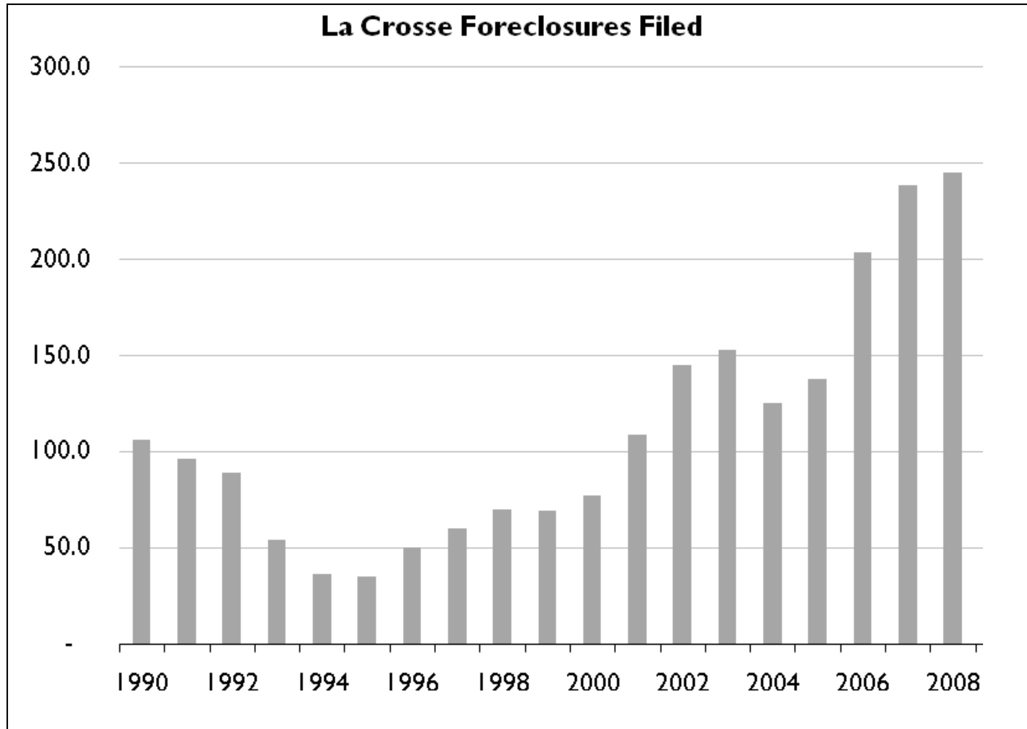

Comparison of National and State Unemployment Rates
9.0
8.0
7.0
6.0
5.0
4.0
3.0
2.0
1.0
0.0
Jan-99
Jan-00
Jan-01
Jan-02
Jan-03
Jan-04
Jan-05
Jan-06
Jan-07
Jan-08
Jan-09
Civilian Unemployment Rate: Percent: SA
Unemployment Rate: Wisconsin; Percent; SA
Unemployment Rate: Minnesota; Percent; SA

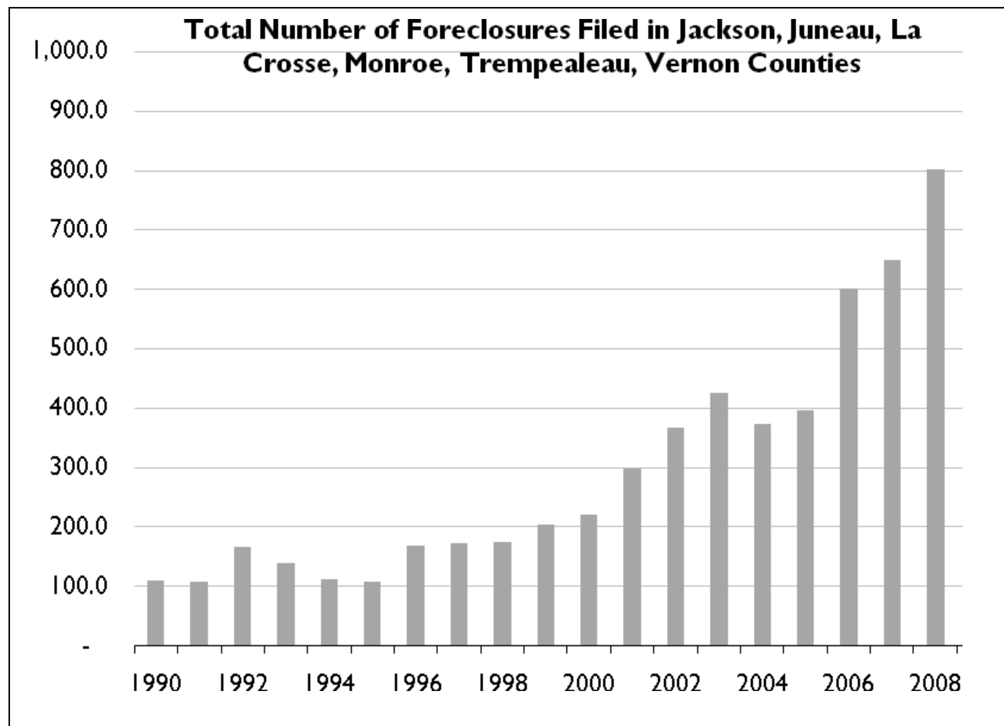

Unemployment Rates by County
8.0
7.0
6.0
5.0
4.0
3.0
2.0
1.0
0.0
Jan-99
Jan-00
Jan-01
Jan-02
Jan-03
Jan-04
Jan-05
Jan-06
Jan-07
Jan-08
Jan-09
Jackson County
Juneau County
La Crosse County
Monroe County

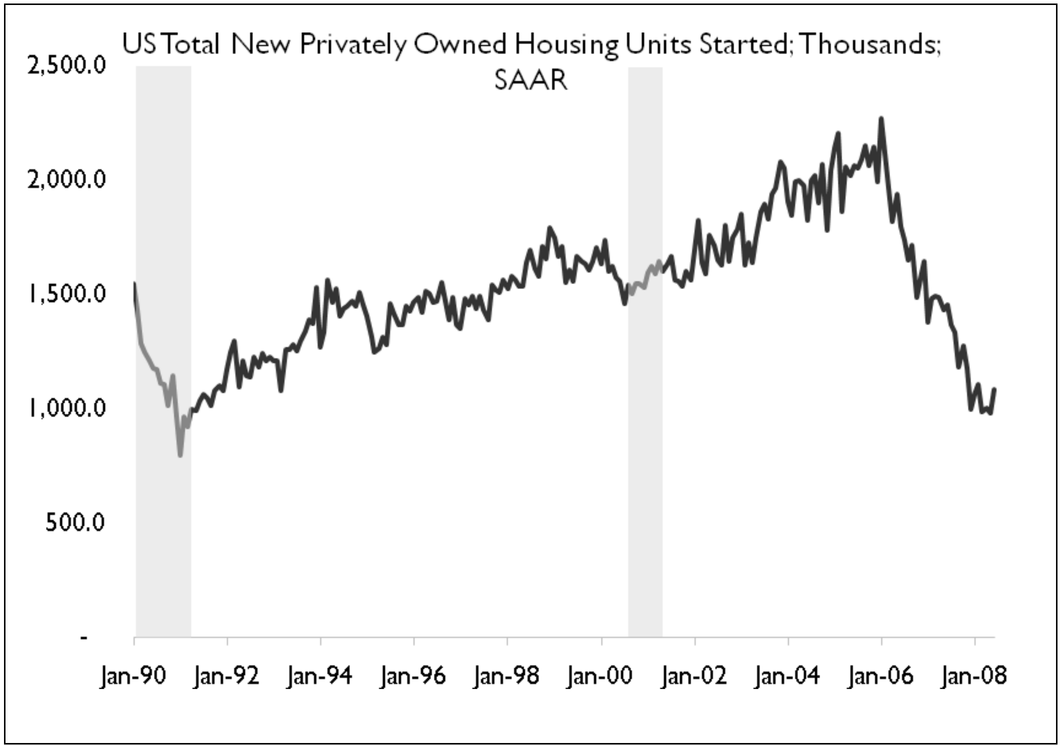


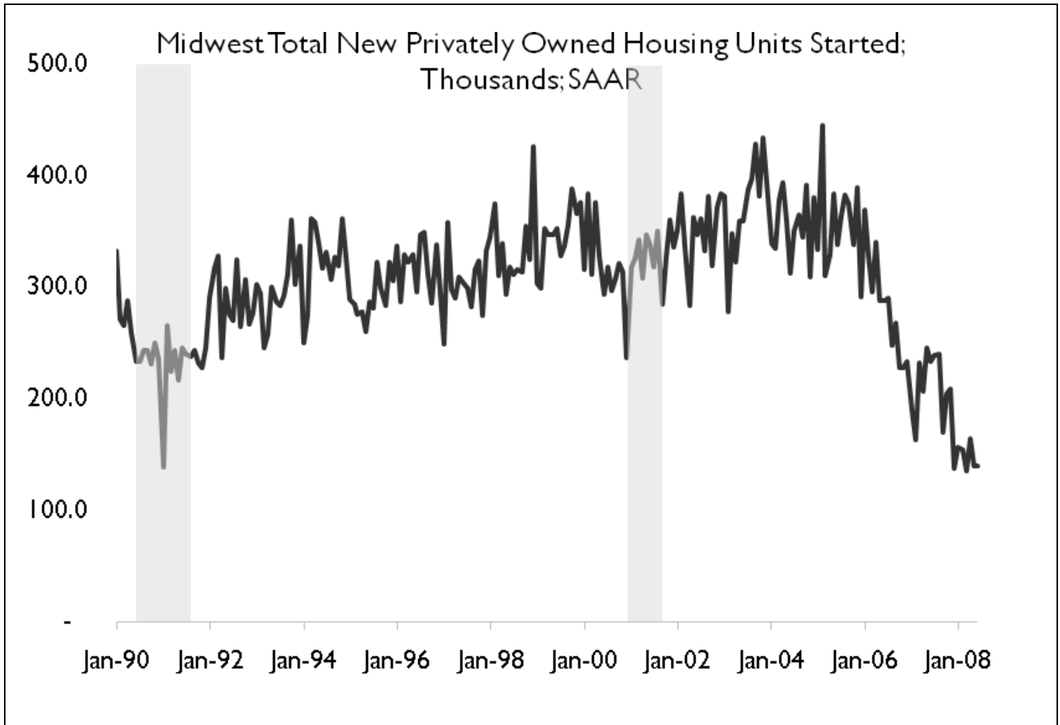
Housing Market Indicators

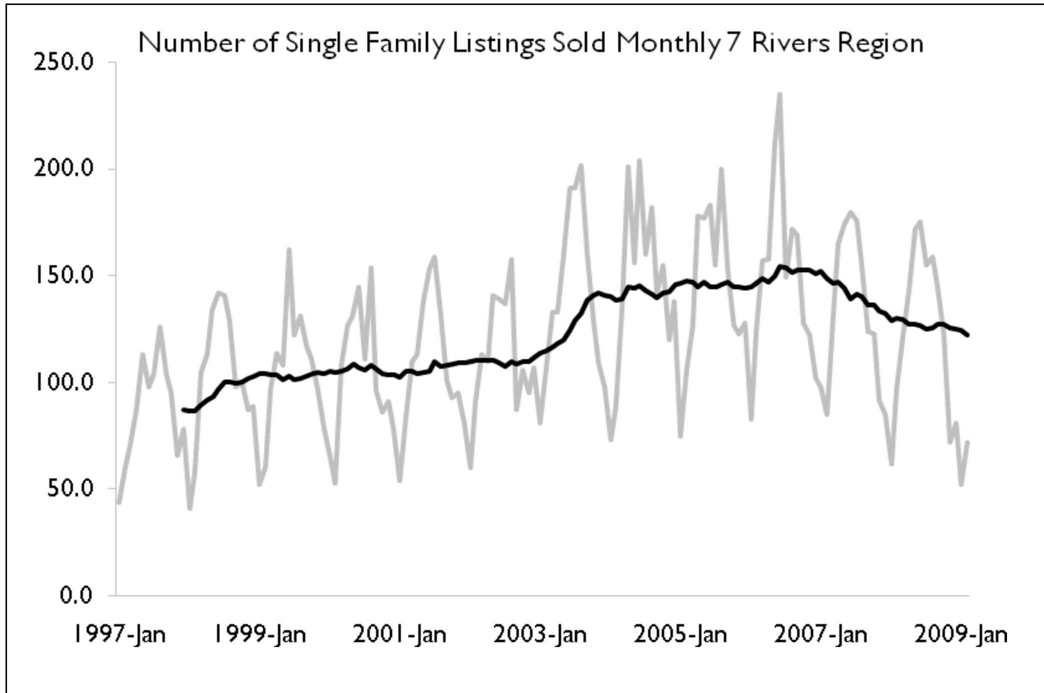


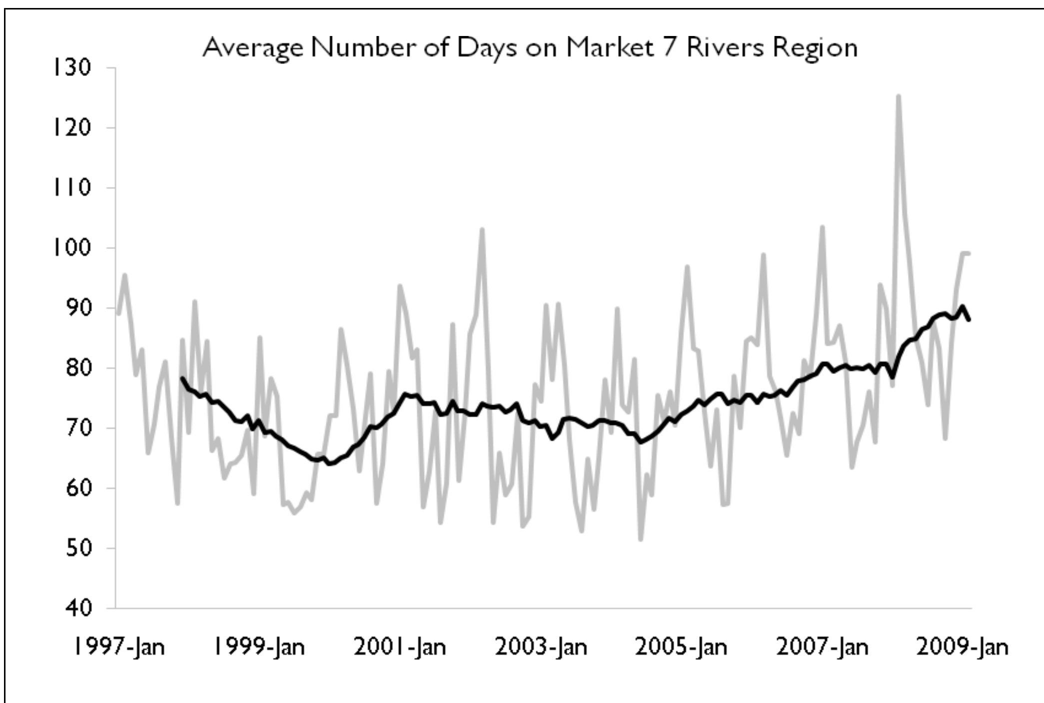

La Crosse Foreclosures Filed
300.0
250.0
200.0
150.0
100.0
50.0
-
1990
1992
1994
1996
1998
2000
2002
2004
2006
2008


Total Number of Foreclosures Filed in Jackson, Juneau, La Crosse, Monroe, Trempealeau, Vernon Counties
1,000.0
900.0
800.0
700.0
600.0
500.0
400.0
300.0
200.0
100.0
-
1990
1992
1994
1996
1998
2000
2002
2004
2006
2008

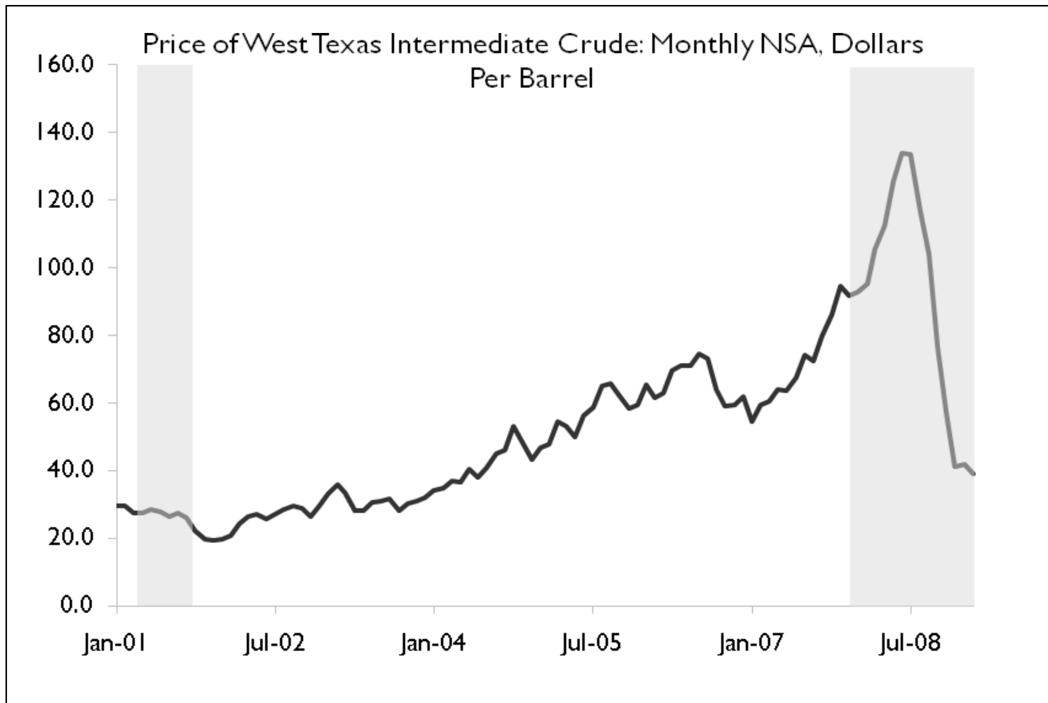

US Total New Privately Owned Housing Units Started; Thousands; SAAR
2,500.0
2,000.0
1,500.0
1,000.0
500.0
-
Jan-90 Jan-92 Jan-94 Jan-96 Jan-98 Jan-00 Jan-02 Jan-04 Jan-06 Jan-08

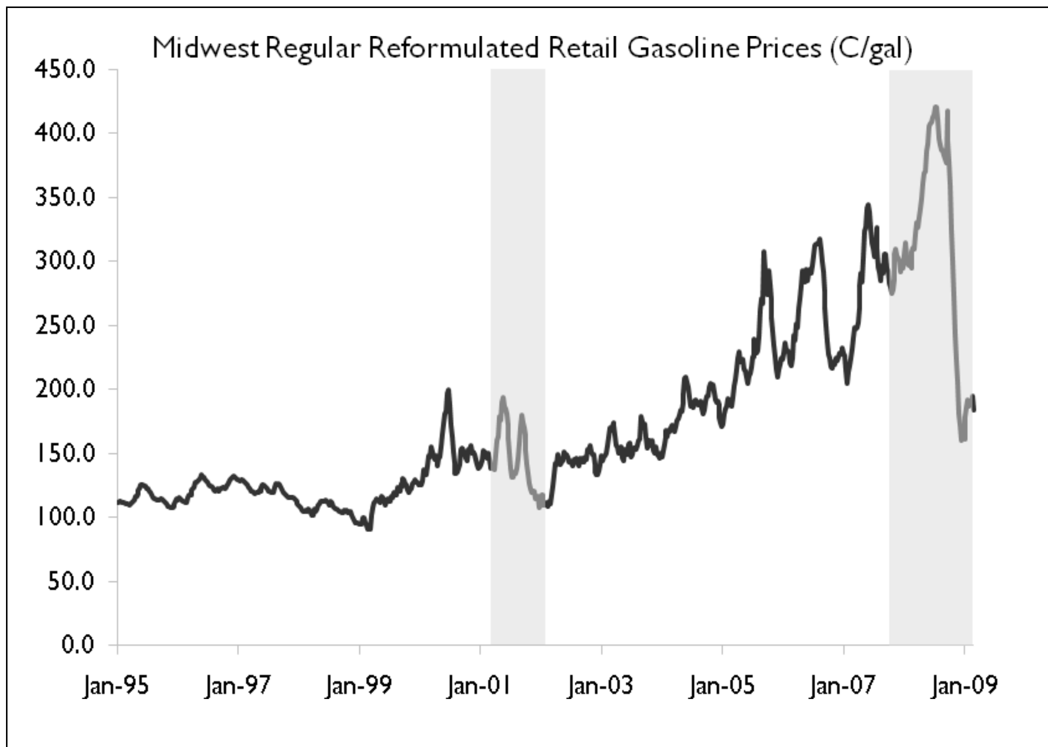

Midwest Total New Privately Owned Housing Units Started; Thousands; SAAR
500.0
400.0
300.0
200.0
100.0
-
Jan-90 Jan-92 Jan-94 Jan-96 Jan-98 Jan-00 Jan-02 Jan-04 Jan-06 Jan-08

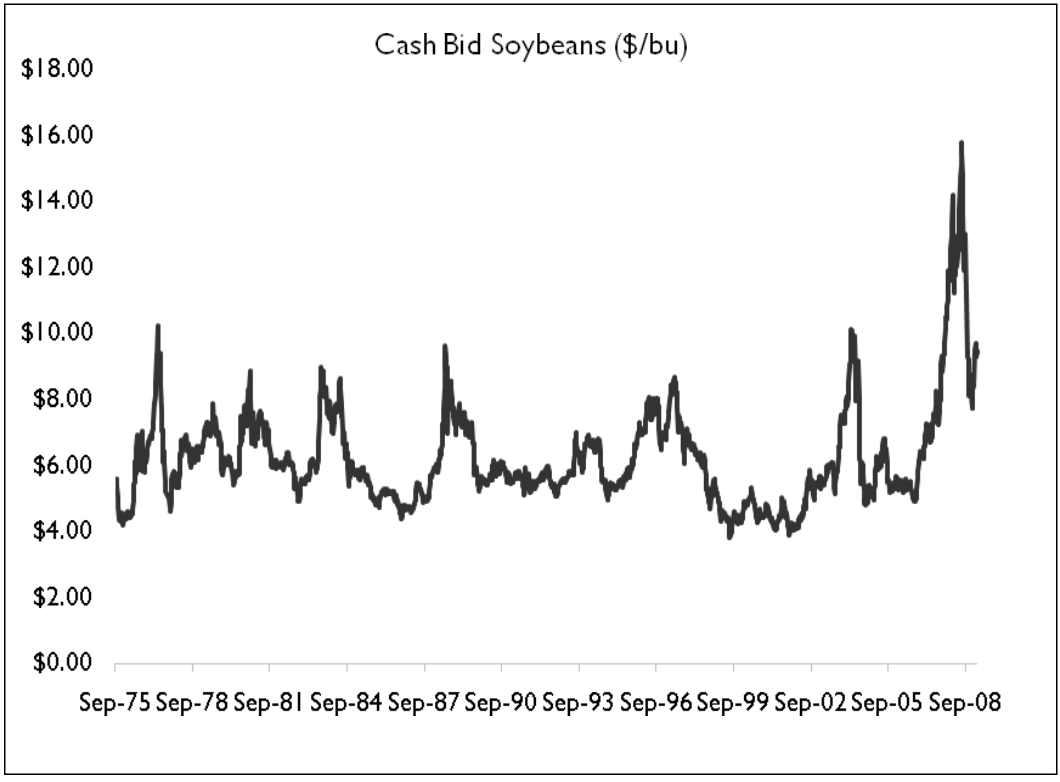


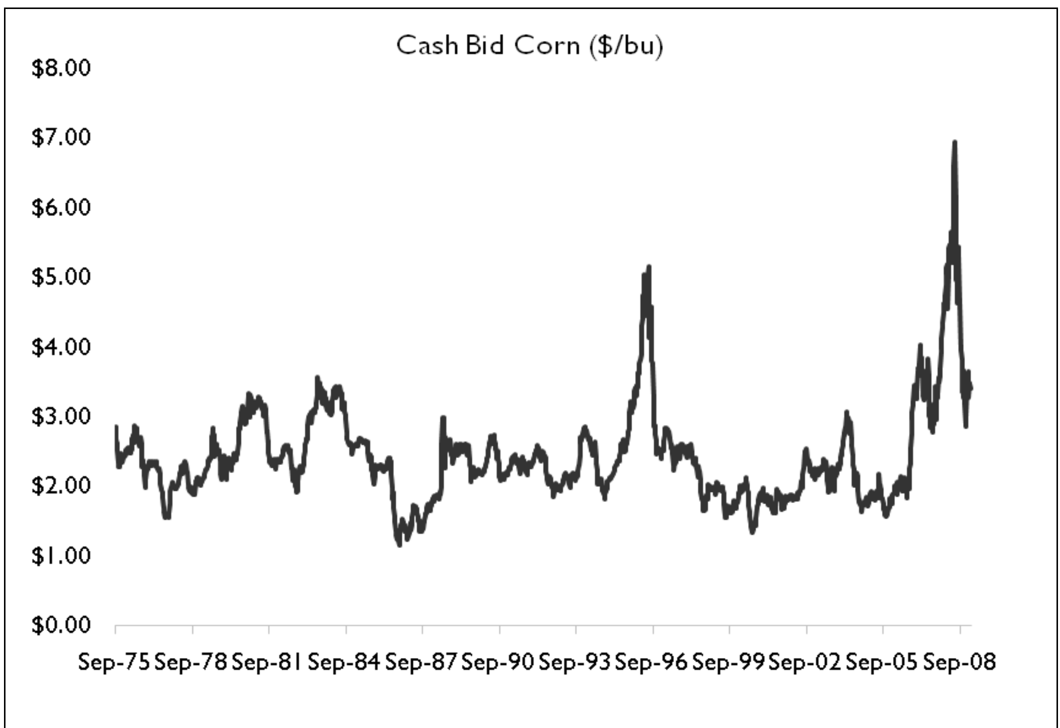


Commodity Market Indicators


Price of West Texas Intermediate Crude: Monthly NSA, Dollars Per Barrel
160.0
140.0
120.0
100.0
80.0
60.0
40.0
20.0
0.0
Jan-01
Jul-02
Jan-04
Jul-05
Jan-07
Jul-08


Midwest Regular Reformulated Retail Gasoline Prices (C/gal)
450.0
400.0
350.0
300.0
250.0
200.0
150.0
100.0
50.0
0.0
Jan-95
Jan-97
Jan-99
Jan-01
Jan-03
Jan-05
Jan-07
Jan-09


Cash Bid Soybeans ($/bu)
$18.00
$16.00
$14.00
$12.00
$10.00
$8.00
$6.00
$4.00
$2.00
$0.00
Sep-75 Sep-78 Sep-81 Sep-84 Sep-87 Sep-90 Sep-93 Sep-96 Sep-99 Sep-02 Sep-05 Sep-08


Cash Bid Corn ($/bu)
$8.00
$7.00
$6.00
$5.00
$4.00
$3.00
$2.00
$1.00
$0.00
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The 7 Rivers Equity Index:
Varying Fundamental Local Firm Strength in the Midst of a Depression

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Introduction

This report covers the share price performance and provides a fundamental financial analysis of companies headquartered in the 7 Rivers Region over the seven-month period from August 2008 through February 2009. If you were to look back at the reports over the past two years you would observe an amazing change in tone. The spring 2007 report referred to stocks as "the new holy grail of investing … [because]…the [stock] markets had not dropped by over 2 percent from a previous high, and had not fallen by over ten percent for almost four years!" The spring 2008 report stated that "investors are trying to [figure] out whether this correction is a much-overdue, short term pullback or a sign of a weaker stock market and economy ahead."

In retrospect, we now know that the current financial crisis began in July 2007, when a loss of confidence by investors in the value of securitized mortgages resulted in a liquidity crisis that prompted a substantial injection of capital into financial markets by the governments around the world. Perceived credit risk spiked in July 2007, remained volatile for a year, and then spiked even higher in September 2008. In September 2008, as the U.S. Presidential race entered the home stretch, the crisis deepened as stock markets world-wide crashed and entered a period of high volatility, and a considerable number of banks, mortgage lenders, and insurance companies failed in the following weeks. Although America's housing collapse is often cited as having caused the crisis, the financial system was vulnerable because of intricate and highly-leveraged financial contracts and operations; a U.S. monetary policy that made the cost of credit negligible, therefore encouraging such high levels of debt; and greed by financial markets.

Looking at the past year, on March 14, 2008, the U.S. government guaranteed assets arising from the Bear Sterns bailout, and with it capitalism changed. As the year unfolded, there were similar bailouts, most notably in the financial and auto industries. Before the year was out, "tarp" no longer referred solely to a canvas sheet protecting items from rain, but to the Troubled Asset Relief Program. Despite the election of a new President promising change, things looked grim. The Grinch stole Christmas, resulting in retailers rolling out deeper and broader price cuts than ever before to liquidate inventories. In the midst of its busiest time of the year, FedEx reported falling shipping volumes, cut its payrolls, and eliminated retirement contributions to those still employed.

Those looking for a turnaround in 2009 have been sorely mistaken. The fear gripping the stock market in early 2009, which resulted in an 18 percent drop during the first two months, has caused some abrupt changes on Main Street, too. U.S. airlines slashed prices to fill empty seats. More companies cut dividends in the first two months of 2009 than in all of 2008, with even General Electric reducing its dividend payment by 68 percent to retain cash. Even heavy sales incentives, reaching $5,566 for every vehicle sold by Chrysler, were insufficient to keep auto sales from plunging 41 percent in February. One of the most abrupt changes on Main Street was the $100 plunge in crude oil prices.

The list of financial challenges on the national scale could go on for pages. To provide some focus, let's look solely at the 7 Rivers area unemployment rates. La Crosse's unemployment rate at first seemed to be holding its own, rising from 4.3 percent in January 2008 to 5.1 percent in December 2008. However, it rose quickly to 6.6 percent in the first month of January 2009. Ironically, job satisfaction rose during the period from 28 percent in December 2007 to 38 percent in December 2008, according to Yahoo! HotJobs, in a sign *The Wall Street Journal* (March 4, p. D1) referred to as a "sign people are grateful they're still employed."

When it comes to purchases, while the $9.8 million that was raised in 2008 did exceed the previous year by about $100,000, sales tax revenues took a plunge in December in La Crosse County compared with the same month in 2007. The December 2008 total was $823,010, down from $990,386 in 2007. The shortfall could signal the start of an impact arising from the recession. A similar delayed impact has been experienced in local stocks. While the value of the 7 Rivers Equity Index held up remarkably well in 2008, it has sunk faster than the Dow Jones Industrial Average or S&P 500 in 2009.

The next section of this report will examine the investment returns of the 7 Rivers Equity Index compared to national stock market performance. As this article is being written in early March, fearful investors are wondering how low the stock market will sink. The remainder of this report helps provide an answer to this concern by providing a synopsis of managerial performance at local companies based on nine financial ratios. Three popular ratios are taken from each of their most recent income statements, balance sheets, and statements of cash flows. (For the most recent analysis of security prices and local firm return forecasts, please refer to the September 2008 edition of *7 Rivers Region: An Economic Update*.)

The 7 Rivers Equity Index

Two criteria must be met for inclusion in the 7 Rivers Equity Index. One, the firm must be publicly held with share price data available from the financial press or Internet sources. Two, the company's headquarters must be within 100 miles of La Crosse, which includes the 7 Rivers Region. A listing of such companies is generated with the assistance of *Reference*USA, a data service allowing one to screen public corporations within a given state. The thirteen companies currently in the 7 Rivers Equity Index set are identified in Table 1.

In prior years, a map and ruler were used to draw a 100 mile radius from downtown La Crosse. *Reference*USA has recently increased its services and now provides a listing of all public companies within a given distance of a location. By their measurement, all companies included in Table 1 are within 102 miles of La Crosse.

Given the stock market's meltdown, it seems as though the first concern of many would be the financial fortitude of local companies. Consequently, Table 1 has been revised to show the performance of local companies during 2008 and the first two months of 2009. A surprisingly high five out of thirteen firms actually registered a gain in 2008, with the price of National Presto rising 46.2 percent! Mirroring the nationwide decline in financial stocks, HMN Financial dropped 83 percent! Baraboo Bancorp dropped 38 percent and Eau Claire's Citizens Bank dropped 26 percent. Even Flexsteel gave up 44 percent of its value.

During the first two months of 2009, only two companies, Citizens Bank and Hormel, have seen their share prices rise, with the largest increase being only 6 percent. Neither of these firms had experienced a stock price increase in 2008. The demise of valuation of financial companies is borne out by the 46 percent and 45 percent stock price declines at HMN Financial and Heartland Financial, respectively. Wausau Paper's drop of 51 percent, however, was larger. The generally larger stock price drops in 2009 than in all of 2008 might be reflecting the delayed impact of the general economic contraction and investor conclusion that the decline would be significant and drastic enough to hurt the local companies.

Table 1: 7 Rivers Equity Index

The headquarters of each of these public firms is within 100 miles of La Crosse.

State / Company	2008 Price Change	January/February 2009 Price Change
Wisconsin		
Baraboo Bancorporation (BAOB)	-38%	-19%
Baraboo; Retail banking		
Citizens Community Bank (CZWI)	-26%	6%
Eau Claire; Retail banking		
Marten Transportation (MRTN)	36%	-13%
Mondovi; Trucking		
National Presto (NPK)	46%	-21%
Eau Claire; Cookware		
Renaissance Learning (RLRN)	-36%	-21%
Wisconsin Rapids; Educational software		
Wausau-Mosinee Paper (WPP)	27%	-51%
Mosinee; Paper products		
Minnesota		
Fastenal (FAST)	-14%	-13%
Winona; Threaded fasteners		
HMN Financial (HMNF)	-83%	-46%
Spring Valley; Savings & loan		
Hormel (HRL)	-23%	2%
Austin; Pork and turkey processing		
Merchants Financial Group(MFGI)	-16%	0%
Winona; Retail banking		
Rochester Medical (ROCM)	38%	-32%
Stewartville; Urinary treatment products		
Iowa		
Flexsteel Industries (F LXS)	-44%	-10%
Dubuque; Home furnishings		
Heartland Financial USA (HTLF)	11%	-45%
Dubuque; Retail banking		

Firms included in the 7 Rivers Equity Index that are no longer publicly held:
Ag Services of America – acquired by Rabobank (1/2004)
Bone Care International – acquired by Genzyme Corporation (6/2005)

Table 1: 7 Rivers Equity Index - Continued

Featherlite – acquired by Universal Trailer Holdings (10/06)
First Federal Capital Corporation – acquired by Associated Banc-Corp (10/04)
La Crosse Footwear – relocated to Oregon (3/2001)
Land's End – acquired by Sears (6/2002)
Northland Cranberries – privatized (11/2005)
Pemstar – acquired by Benchmark Electronics (1/07)
Sheldahl – bankrupt (4/2002)
State Bank La Crosse – privatized (2/2003)
TenderCare International – acquired by Hain Celestial (12/07)

Performance of the 7 Rivers Equity Index, an equally-weighted index of local companies, is presented in the first column of Table 2. Current stock prices, adjusted for stock splits and dividends are divided by the first stock price on or after 12/31/1999. Companies that go out of existence are assumed to have been sold at their final share price, with a rate of return calculated from the first time these shares were available on or after 12/31/1999. Total returns are divided by the number of companies available (which is 24) and multiplied by 100 to estimate the 7 Rivers Equity Index. In this way, all firms are equally weighted. The 7 Rivers Equity Index, like the comparison benchmarks described below, excludes dividends.

Share prices were obtained from Yahoo! Finance. Since 1999, eleven 7 Rivers Region firms have been acquired or went bankrupt, and they are listed at the bottom of Table 1. The performance of these firms is included in the calculation of the 7 Rivers Equity Index for the period in which they met the 7 Rivers Equity Index's criteria.

The values in Table 2 represent the value of $100 invested in local shares on 12/31/1999. For instance, in 2000, the value of 7 Rivers Equity Index dropped 9.3 percent to 90.7, meaning that a $100 investment would have lost $9.30. Over the first seven years, through December 2006, 7 Rivers Equity Index rose 60.6 percent to 160.6, which is the highest year-end close of the 7 Rivers Equity Index. This value would equate to a rise of about 7 percent per year. Meanwhile, between 2000 and 2006, $1000 invested in the Dow Jones Industrial Average rose to only $108.40 and the Standard and Poor's 500 fell to $96.50, as exhibited in the center and right hand columns of Table 2.

The all-time high for the 7 Rivers Equity Index was reached in April 2007, when the index climbed to 167.6. From that point, however, the 7 Rivers Equity Index dropped significantly, falling 8.5 percent for the year. By contrast, during 2007, the Dow Jones Industrial Average rose 6.5 percent and the Standard & Poor's 500 rose 3.3 percent. In 2008, the 7 Rivers Equity Index held up very well, dropping to a slight loss in June but then recovering and staying in positive territory until October.

The resilience of local stocks appears to have melted away in early 2009. Consistent with the individual company returns presented in Table 1, the 7 Rivers Equity Index sunk 13 percent. However, major stock market index declined to a greater extent, averaging a 19 percent decline. As of February, $100 dollars invested in local shares would still have earned $117.5, or an annualized rate of return of 1.8 percent. At the other extreme, investment in the Standard & Poor's 500 would have resulted in a loss of exactly half of one's money, which equates to an

annual rate of 7.3 percent. Although relatively good, the 7 Rivers Equity Index declined by 27 percent over the past 26 months.

Table 2: Comparative Index Performance

Since 12/31/1999 Index Value of 100
(Year-to-Year Change in Parentheses)
[12/2006-to-Month Change in Brackets]

	7 Rivers Equity Index		Dow Jones Industrial Average		Standard & Poor's 500	
12/1999	100.0	(n/a)	100.0	(n/a)	100.0	(n/a)
12/2000	90.7	(-9.3%)	93.8	(-6.2%)	89.9	(-10.1%)
12/2001	98.6	(+8.7%)	87.2	(-7.0%)	78.2	(-13.0%)
12/2002	98.1	(-0.4%)	72.6	(-16.7%)	59.9	(-23.4%)
12/2003	114.0	(+16.2%)	91.0	(+25.3%)	75.7	(+26.4%)
12/2004	135.8	(+19.2%)	93.8	(+3.1%)	82.5	(+9.0%)
12/2005	136.5	(+0.5%)	93.2	(-0.8%)	85.0	(+3.0%)
12/2006	160.6	(17.7%)	108.4	(16.3%)	96.5	(+13.5%)
12/2007	142.8	(-8.5%)	115.4	(6.5%)	99.9	(+3.3%)
January 2008	147.3	[3.1%]	110.3	[-4.6%]	93.9	[-6.1%]
February 2008	144.5	[1.1%]	106.7	[-7.5%]	90.5	[-9.5%]
March 2008	144.7	[1.3%]	106.6	[-7.6%]	90.1	[-9.9%]
April 2008	147.5	[3.3%]	111.5	[-3.4%]	94.3	[-5.7%]
May 2008	148.4	[3.9%]	109.9	[-4.7%]	95.3	[-4.7%]
June 2008	137.0	[-4.1%]	98.7	[-14.4%]	87.1	[-12.9%]
July 2008	144.4	[1.1%]	99.9	[-14.2%]	86.2	[-13.8%]
August 2008	147.6	[3.4%]	100.4	[-13.0%]	87.3	[-12.7%]
September 2008	146.5	[2.6%]	94.4	[-18.2%]	79.3	[-20.7%]
October 2008	134.8	[-5.5%]	81.1	[-29.7%]	65.9	[-34.1%]
November 2008	129.5	[-9.3%]	76.8	[-33.4%]	61.0	[-39.0%]
December 2008	134.9	[-5.5%]	76.3	[-33.8%]	61.5	[-38.5%]
January 2009	123.2	[-13.7%]	69.6	[-40.7%]	56.2	[-43.8%]
February 2009	117.5	[-17.7%]	61.4	[-46.8%]	50.0	[-50.0%]

Fundamental Characteristics of Local Firms

Forecasting whether 7 Rivers firms will continue to outperform national averages or whether the current downward trend will continue is difficult. To gain insight, the remainder of this report studies the local firms' financial health. Following past precedent, this spring report studies fundamental financial characteristics of the firms in the 7 Rivers Equity Index. Morningstar.com

and Yahoo! Finance were the sources of financial ratios and income statements, balance sheets, and statements of cash flows (when ratios were not available), respectively, for 2004-2008. In most instances the 2008 information covers all of 2008. In the three instances where information was not available for the last quarter of 2008, the final quarter of 2007 was included so that all ratios are based on twelve months of data. The 2004-2007 averages reported below are based on an average of individual calendar years in the 2004-2007 period. Due to their unique characteristics, the averages of the three financial companies covered by Morningstar.com and Yahoo! Finance are reported separately. Neither reporting agency tracks the small Baraboo Bancorporation or Merchants Financial Group.

Income Statement Insights

Gross profit margins (Gross profit/Sales) represent the percentage of revenues not consumed by the cost of producing products and services. As shown in the first 2008 column of Table 3, the gross profit margin of non-financial local companies is 34 percent, which implies that 66¢ of every dollar of revenue is used to produce the goods being sold. At the high extreme, the gross profit margins of Renaissance Learning and Fastenal are 75 percent and 53 percent, respectively. Wausau-Mosinee Paper's gross profit margin is only 8 percent, leaving little room to pay sales and administrative expenses. Fastenal (+13 percent) also posts greatest improvement in gross margin from the 2004-2007 average, while Marten Transportation (-8 percent) had the largest drop.

The comparable ratio for financial concerns is net interest margin. As one can see on the bottom panel in the first column, net profit margins are virtually identical and average 53 percent in the local financial firms with date available. Given the stock price drop reported in Table 1, it is not surprising to see that HMN Financial (-3 percent) experienced the largest drop in net interest margin.

Net profit margins (Net income/Sales) represent the percentage of revenue remaining after paying all expenses, including interest and taxes. As shown on the Non-Financial Average line on Table 3's middle column for 2008, 5 percent (or 6¢ per dollar) of revenue is normally available for retained earnings and dividend payment. Among non-financial firms, Fastenal (12 percent) is on the high end for the third year in a row. Wausau Paper lost 1¢ per dollar of sales. Both Renaissance Learning and Rochester Medical experienced a 6 percent drop in profit margins, while none rose by over 1 percent.

Perhaps the biggest news of the year was the incredible drop in profit margins! HMN Financial saw its profit margin drop from 24 percent to -25 percent, a 49 percent swing! Heartland Financial's profit margin also dropped by 9 percent, though Citizens Community Bank eked out a 3 percent gain. On average, local banks lost 3¢ per dollar of revenue.

Return on equity (Net income/Total stockholders equity) reflects the amount of return earned per dollar invested by shareholders. As shown in the right 2008 column of Table 3, 10 percent (or 10¢ per dollar invested by shareholders in non-financial firms) is returned to them in the form of dividends or retained earnings on an annual basis. Debt financing helped Fastenal (26 percent) to leverage up its net profit margin. The additional financing costs at Wausau Paper (-6 percent) made the loss per dollar invested 5¢ worse than the net profit margin alone. Although Fastenal (26 percent) leads in this category, Hormel's return on equity is 14 percent.

The worst return on equity took place at HMN Financial, whose loss amounted to 11¢ per dollar invested. This represents a decline of 22 percent from the average of the prior two years. All of the banks reported a drop in return on equity, with the average dropping from a positive 9¢ to a loss of 1¢ per dollar invested.

Table 3: Analysis of Income Statements Information

Non-Financial Firms	Gross Profit Margin (% of Sales)		Net Profit Margin (% of Total Revenue)		Return on Equity (% of Equity)	
	2008	2004-07 Average	2008	2004-07 Average	2008	2004–07 Average
Fastenal	53%	40%	12%	11%	26%	20%
Flexsteel	19%	19%	0%	2%	1%	7%
Hormel	20%	23%	6%	5%	14%	17%
Marten Transportation	29%	37%	4%	4%	7%	11%
National Presto	18%	18%	10%	9%	16%	7%
Renaissance Learning	75%	81%	10%	16%	19%	21%
Rochester Medical	47%	40%	2%	8%	1%	5%
Wausau-Mosinee Paper	8%	8%	-1%	1%	-6%	1%
Non-Financial Average	34%	33%	5%	6%	10%	11%

Financial Firms	Net Interest Margin (% of Interest Income)		Net Profit Margin (% of Total Revenue)		Return on Equity (% of Equity)	
	2008	2004-07 Average	2008	2004-07 Average	2008	2004–07 Average
Citizens Community Bank	52%	54%	9%	6%	2%	3%
HMN Financial	51%	54%	-25%	18%	-11%	11%
Heartland Financial	57%	53%	8%	17%	5%	12%
Financial Firm Average	53%	54%	-3%	14%	-1%	9%

Balance Sheet Insights

Current ratios (Current assets/Current liabilities) provide insight to firm liquidity. As shown in the first 2008 column in Table 4, on average non-financial firms had 4.1 times as many dollars in cash, accounts receivable, and inventory as they had in accounts payable and accruals. Rochester Medical's current assets were over eleven times the size of current liabilities. At the other extreme, Renaissance Learning, with a current ratio of 1.0, would have to sell all of its inventory and collect all of its accounts receivable to pay its suppliers, employees, and the government what was owed them. Actually, this is an improvement in Renaissance Learning's 2007 position, when its current ratio was 0.08.

The comparable figure among financial firms is financial leverage, which compares a bank's total assets to equity. A comparison across time reveals that all three banks experienced a decrease in assets per dollar of equity. The largest percentage decline occurred at Heartland Financial, although it still had the most assets in place per dollar invested by shareholders.

Long-term debt ratios (Long-term debt/Total assets) indicate the amount of long-term borrowing used to acquire assets. Perhaps in anticipation of looming recession, and aware of the challenges arising from paying interest expense when revenues are shrinking, all local non-financial firms shrunk their long-term debt ratio. In fact, at the end of 2008, Fastenal, National Presto, and Renaissance Learning had eliminated all long-term debt. The greatest decrease occurred at Marten Transportation, where the long-term debt financing of assets dropped from 30.6 percent to 2.4 percent.

In contrast, local financial companies actually increased their financial risk. HMN Financial saw its long-term debt ratio rise from 90.9 percent to 92.3 percent. With so much financial risk, it is not surprising that the price of HMN Financial has dropped over 90 percent in fourteen months.

Careful management of assets has helped local firms maintain their asset turnover ratios despite the recession. Aided by increased sales the asset turnover ratio increased by 85 percent at National Presto, generating sales that were 1.3 times its ratios instead of only 0.7 times its assets. The demand for appliances, as individuals cook at home instead of eating out, has helped National Presto buck the trend and register a 15 percent stock price increase over the past fourteen months.

Since many of the financial firms assets can be withdrawn or paid off at a moment's notice, the comparative measure among financial firms is the fixed asset turnover. Think of this as the banks revenues relative to the money it has invested in headquarters and branch locations. A shrinking revenue stream caused their average fixed asset turnover ratio to drop by almost 20 percent. Most of this drop can be attributed to Citizens Community Bank, where revenues dropped from 4.8 times to 3.2 times fixed assets.

Table 4: Analysis of Balance Sheet Information

Non-Financial Firms	Current Ratio (Times Current Liabilities)		Long-term Debt Ratio (% of Total Assets)		Total Asset Turnover (Revenue/Total Assets)	
	2008	2004-07 Average	2008	2004-07 Average	2008	2004–07 Average
Fastenal	6.6	7.0	0.0	1.5	1.9	1.7
Flexsteel	3.5	2.8	8.2	13.8	2.1	2.4
Hormel	2.0	1.7	9.7	24.2	1.9	1.9
Marten Transportation	1.4	1.6	2.4	30.6	1.5	1.4
National Presto	5.2	4.8	0.0	5.0	1.3	0.7
Renaissance Learning	1.0	1.6	0.0	3.6	0.9	1.3
Rochester Medical	11.6	8.0	4.9	10.2	0.5	0.7
Wausau-Mosinee Paper	1.8	2.0	21.7	44.1	1.6	1.3
Non-Financial Average	4.1	3.7	5.7	16.7	1.5	1.4

Financial Firms	Financial Leverage (Total Assets/Equity)		Long-Term Debt (% of Total Assets)		Fixed Asset Turnover (Revenue/Fixed Assets)	
	2008	2004-07 Average	2008	2004-07 Average	2008	2004–07 Average
Citizens Community	7.0	7.8	86.6	85.7	3.2	4.8
HMN Financial	10.2	11.2	92.3	90.9	3.0	3.2
Heartland Financial	11.9	14.7	93.5	93.0	1.2	1.2
Financial Firm Average	9.7	11.2	90.8	89.9	2.5	3.1

Cash Flow Statement Insights

Cash is the monetary lubricant that permits a business to operate. Cash is also required to pay dividends and expand operations. Consequently, the statement of cash flows is another important financial statement. These statements describe the change in cash in terms of a firm's operations, investing (in fixed assets) activities, and financing (with stocks and long-term bonds) activities. Each of these activities will be examined below. To adjust for firm size, each cash flow amount is divided by the firm's total assets value reported on the balance sheet.

Cash from operations starts with net income, adds back the noncash depreciation charge, and makes adjustments for changes in current asset and current liability accounts. Operations at the average non-financial firm took in 17¢ per dollar of assets during 2008, as exhibited in the first 2008 column of Table 5. This is a penny better than 2007 and a nickel better than the 2004-2007 average. Renaissance Learning brought in 38¢ per dollar of assets, which was more than 50 percent the 2004-2007 average. The largest drop occurred at Rochester Medical, which saw its cash flow from operations drop from 47¢ to 4¢, a 91 percent drop. A similar fall was registered at HMN Financial, where cash flow from operations fell from 11¢ to 2¢. This decline explains the average drop in cash flow from operations at local financial institutions.

Cash flow from investing activities was negative in eleven of the thirteen instances, as companies bought fixed assets to replace those worn out or to expand operations. However, only four companies spent more on additional assets than was depreciated or sold. Looking at the nonfinancial averages, one can see that while companies replaced 7 percent of assets in the 2004-2007 period, that percentage replaced in 2008 dropped to 2 percent. Pressured by the recession, it appears as though Renaissance Learning and Rochester Medical sold off non-business investment assets, resulting in a reduction in the number of total assets owned by the business. The amount of investing in new assets per dollar of total assets also dropped among local financial firms. However, Citizens Community Bank spent 15¢ more per dollar of assets, while HMN Financial spent 32¢ less per dollar of assets.

Cash flow from financing is typically positive when firms issue new stocks and bonds, but negative otherwise as firms pay dividends or retire stocks and bonds. For the second year in a row, only the rapidly expanding Rochester Medical took in more money through security sales than it paid out in dividends or security purchases in 2008. In early 2009, Rochester Medical announced a share repurchase program, so it is likely that the cash flow from financing activities in the future will be negative. National Presto, which has seen its sales double since 2005, and Renaissance Learning, which was selling off investments, both paid 32¢ out of their total assets to creditors and shareholders. Looking at the decreasing long-term debt numbers found in Table 4, it is likely that much of the money went to reduce long term debt.

Comparing local banks, cash flow from financing would be positive in instances where deposits grow. Looking at the bottom right rows of Table 5, one can see that Citizens Community Bank expanded by 23¢ per dollar of total assets. Although HMN Financial grew, its growth dropped from 26¢ to 4¢ per dollar of assets. Heartland Financial also registered a slight decline in its rate of growth.

A company's change in cash, as a function of assets, can be determined by adding together the three types of cash flow. For instance, Fastenal took in 20¢ through operations, but put 7¢ into fixed assets, and spent another 11¢ on financing, netting a gain of 2¢. Taking all of the average numbers together, cash on the balance sheets rose by an average of 2¢ (17¢ - 2¢ -13¢). This is exactly the same cash flow per dollar of assets as local companies had in 2007, though there was much more investing and less financing. Among local financial companies, there was a gain of a penny from operations because investing and financing activities offset each other.

Table 5: Analysis of Cash Flow Statements Information

Non-Financial Firms	Cash Flow From Operations ($/Total Assets)		Cash Flow From Investing Activities ($/Total Assets)		Cash Flow From Financing Activities ($/Total Assets)	
	2008	2004-07 Average	2008	2004-07 Average	2008	2004–07 Average
Fastenal	0.20	0.12	-0.07	-0.05	-0.11	-0.08
Flexsteel	0.19	0.12	-0.00	-0.16	-0.18	-0.08
Hormel	0.08	0.12	-0.04	-0.06	-0.03	-0.04
Marten Transportation	0.16	0.19	-0.12	-0.22	-0.04	0.04
National Presto	0.20	0.12	-0.08	-0.05	-0.32	-0.06
Renaissance Learning	0.38	0.24	0.11	0.09	-0.32	-0.38
Rochester Medical	0.04	0.19	0.07	-0.21	0.01	0.06
Wausau-Mosinee Paper	0.09	0.06	-0.06	-0.02	-0.07	-0.06
Non-Financial Average	0.17	0.12	-0.02	-0.07	-0.13	-0.06
Financial Firms						
Citizens Community Bank	0.01	0.01	-0.35	-0.16	0.40	0.17
HMN Financial	0.02	0.11	-0.06	-0.38	0.04	0.26
Heartland Financial	0.01	0.01	-0.06	-0.08	0.05	0.06
Financial Firm Average	0.01	0.04	-0.16	-0.22	0.16	0.16

Summary

As of February 2008, there are thirteen publicly-held firms in the 7 Rivers Region. Although the value of national equity indexes are half of what they were when we began this century, investment in 7 Rivers firms has earned a positive rate of return over the last eight years. However, the current level of the 7 Rivers Equity Index is down 30 percent from its all-time high.

It appears as though national economic conditions, instead of firm fundamentals, explain the reason for the sell-off of local non-financial company shares. Gross margin, net profit margins, and return on equity were similar in 2008 to their 2004-2007 averages. Current ratios are higher, financial leverage is lower, and total asset turnover is higher. Meanwhile, cash flows from operations were over forty percent higher, offsetting much higher financing expenses.

Strong fundamental strength is not prevalent among local financial companies, whose interest margins, profit margins, and return on equity eroded in 2008. Debt rose as financial firms saw their fixed asset turnover fall. Finally, their cash flow per dollar of assets was only half that of local non-financial firms. Consequently, these three companies have dropped 54 percent in the fourteen months, explaining 70 percent of the decline in the 7 Rivers Equity Index.