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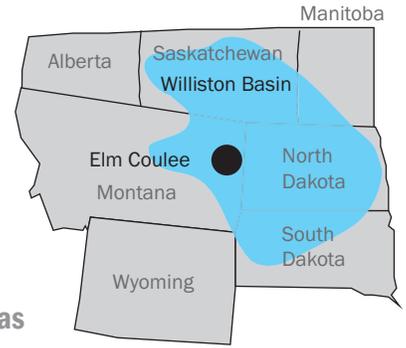
Seminar Program

7:45 – 8:00	Coffee and Registration
8:00 – 8:05	Introductions <i>Ian Marquand</i>
8:05 – 8:45	Keynote <i>Tom Richmond</i>
8:45 – 9:15	National and State Outlooks <i>Patrick Barkey</i>
9:15 – 9:30	Local Outlook <i>Paul Polzin</i>
9:30 – 9:40	Coffee Break
9:40 – 10:00	Nonresident Travel <i>Norma P. Nickerson</i>
10:00 – 10:20	Health Care <i>Gregg Davis</i>
10:20 – 10:40	Agriculture <i>George Haynes</i>
10:40 – 10:50	Coffee Break
10:50 – 11:10	Real Estate <i>Scott Rickard</i>
11:10 – 11:30	Manufacturing and Forest Products <i>Todd Morgan</i>
11:30 – 11:50	Local Expert Report
11:50 – 12:00	Break
Noon - 12:50	Luncheon Program <i>Panel discussion</i>
12:50	Closing Remarks

Montana's New Energy Frontier

What are the Prospects?

Tom Richmond, Administrator and Petroleum Engineer, Montana Board of Oil and Gas



Ranchers in Sidney, Montana, are receiving \$1 million royalty checks. Homeowners are renting unheated garages to oil workers for \$600 a month. And new technology has opened up billions of barrels of oil in the Bakken, arguably the largest inland oil find in the U.S. in the past 50 years. From 2000 to 2006, Montana's oil production more than doubled (Figure 1) as the oil industry developed and implemented a number of variations of the horizontal drilling technique in the development of the Elm Coulee Field in Richland County.

Science and technology have had a long history of influencing the development of Montana's oil and gas resources. The extraordinary and continuing interest in development of the Bakken formation in Montana and North Dakota is the product of two technologies, horizontal drilling and hydraulic fracturing. Both technologies

have been in use in Montana for several years: horizontal drilling since 1989 and hydraulic fracturing at least since the 1950s. Neither by itself would have made the long-known but marginally productive oil-bearing Bakken formation the target of so many drilling rigs and oil and gas developers.

Just east of the Montana border, North Dakota has become a magnet for investment dollars, creating new jobs and bringing revenues into the state. Energy development is going strong in eastern Montana, but does it have the potential of our North Dakota neighbors?

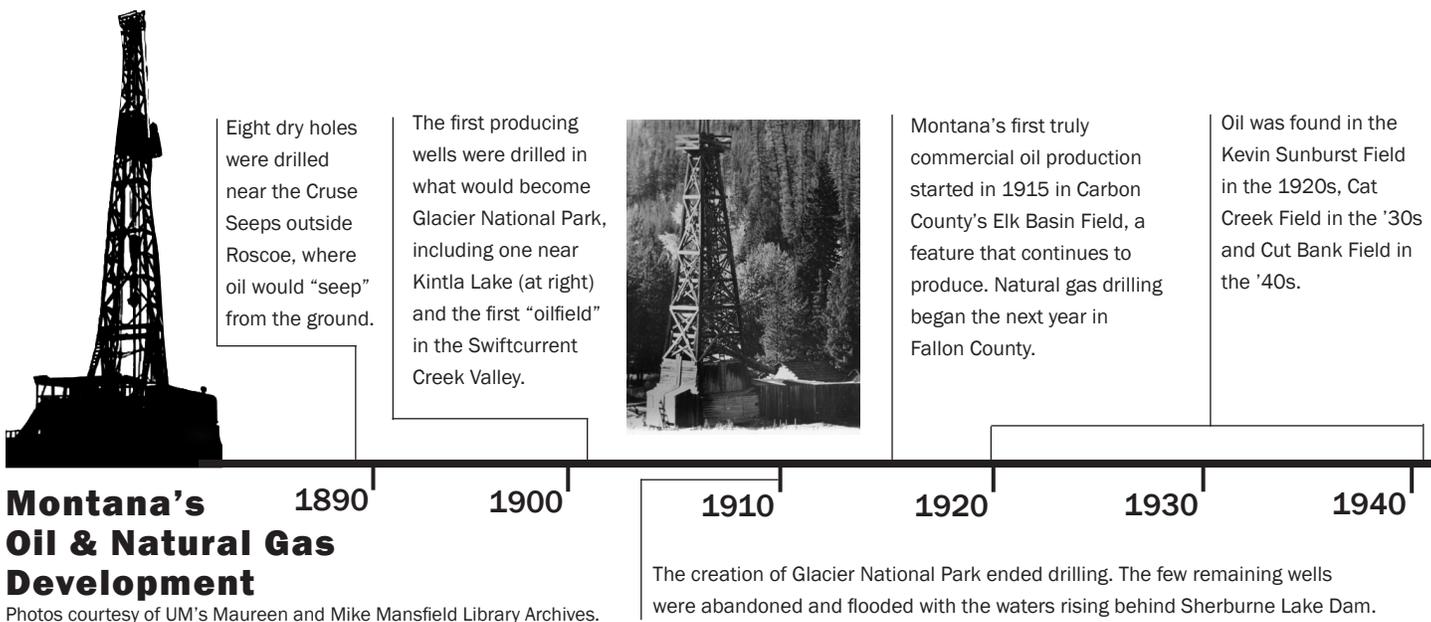
Science, Technology, and Exploration

Montana's complex and diverse geologic setting has long provided opportunities for successful exploration and development activities aided by science and technology advancements.

The oil and gas industry has explored virtually every geologic basin in the state over the last century; albeit, some have been only lightly explored. The traditional producing areas include the Montana portions of the Williston, Powder River in the southeastern part of the state, and the Big Horn Basins in south central Montana. The Sweet Grass Arch and other central Montana areas contribute to the state's production. Figure 2 shows oil production trends throughout the state.

The original oil-finding technology was applied in Montana as it was in many other places. In the late 1880s and early 1900s, oil developers looked for natural oil seeps as evidence of potential commercial production.

The science of oil finding progressed as geologists found and explored anticlines and domes throughout the state. Montana's first



commercial oil production occurred in 1915 (see timeline). From that time through the 1960s, advances in geologic exploration methods, along with the occasional success of random drilling, increased success rates.

By the 1970s, seismic exploration and the ability to use electronic processing to analyze great quantities of data, produced a rush to explore the deep geological features that trapped oil in the Red River formation in the Williston Basin. In the process of exploring for Red River oil, other oil-bearing formations were penetrated and successful wells developed. The recent development of three-dimensional seismic techniques and data processing advancements continues to improve the ability of geologists and geophysicists to successfully tap oil resources from features that would otherwise escape detection.

The Bakken: Promise and Reality

The Bakken development currently drawing so much attention honors a much more recently developed

Figure 1
Monthly Oil Production, Vertical vs. Horizontal Wells, Jan. 1986 - Aug. 2011

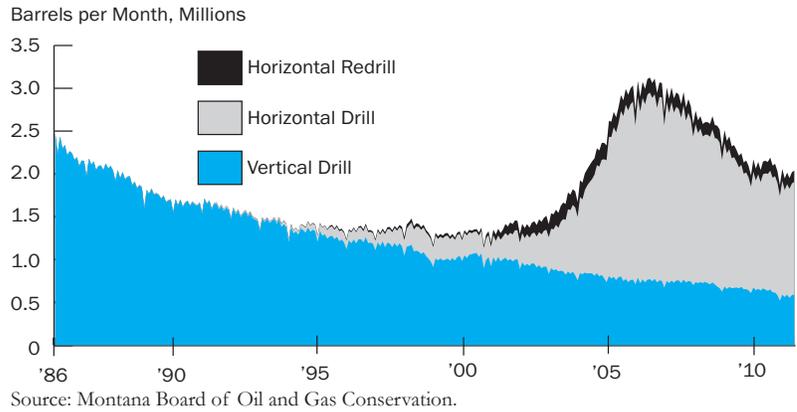
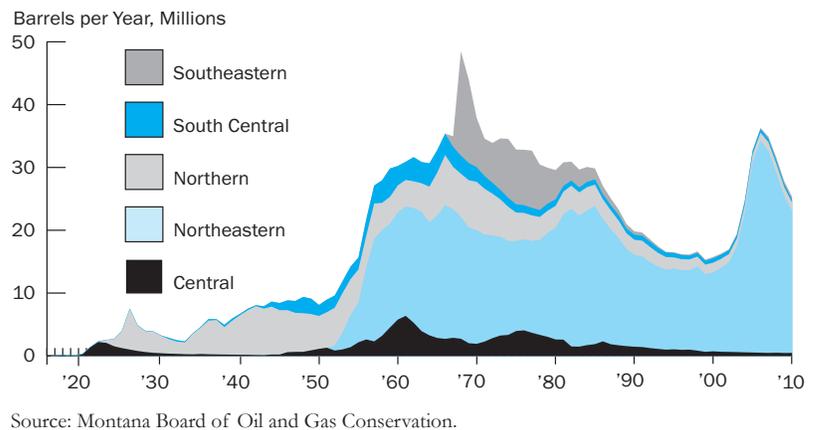


Figure 2
Statewide Oil Production History, 1916-2010



The "Montana Gusher" journal was created in 1920 in Lewistown to follow the booming industry.

The technique of hydraulic fracturing, nicknamed "fracking" today, was developed by the 1950s. At the same time, oil was discovered on the Cedar Creek Anticline, deep beneath the formations drilled for natural gas the previous 40 years.

The technique of horizontal drilling began.

From 2000 to 2006, Montana's oil production more than doubled as the oil industry developed and implemented variations of the horizontal drilling technique in Richland County's Elm Coulee Field.

1950 1960 1970 1980 1990 2000 2010

Bell Creek Field in Powder River County was discovered in 1967.

There was a rush to explore the deep geological features that trapped oil in the Red River formation in eastern Montana's Williston Basin, which is still a hot spot today.

Terms and Definitions

The **Bakken** is a subsurface rock formation with three layers: shale for the upper and lower with a varied composition in the middle. The Bakken lies between the overlying Lodgepole Formation and the underlying Three Forks Formation and occupies about 200,000 square miles of the subsurface of the Williston Basin. The formation was deposited approximately 360 million years ago.

Elm Coulee is an oilfield in Richland County, Montana, that is productive from the middle layer of the Bakken Formation. It was named shortly after the original Bakken horizontal well development started in 2000. The field currently produces about half of Montana's total oil production.

Williston Basin is an elliptical-shaped, sedimentary basin that extends from the northern Great Plains of the U.S. into Canada. The basin occupies most of North Dakota, northwestern South Dakota, eastern Montana, and a part of southern Manitoba and Saskatchewan in Canada. The U.S. part of the basin is a maximum sediment thickness of about 16,000 feet near Williston, North Dakota.

The **Nesson Anticline** in North Dakota and the **Cedar Creek Anticline** in Montana are the two prominent structural features in the Williston Basin. Oil production was discovered in both features in the early 1950s. An anticline is a convex upward fold in the earth's strata, or layers.

The term **Pay Zone** was probably borrowed from gold mining nomenclature. It is a permeable rock that contains oil or gas in sufficient quantity to produce and through which petroleum may migrate. It's also called the reservoir or reservoir rock.

Hydraulic Fracturing is stimulation treatment typically performed on low-permeability oil or gas reservoirs. Engineered fluids are pumped at high pressure, causing a fracture to open along the natural stresses in a formation. Proppant, such as grains of sand, is mixed with the fluid to keep the fracture open when the treatment is complete.

Horizontal Drilling is a subset of the more general term "directional drilling," used where the angle of the wellbore approaches 90 degrees away from vertical. Because a horizontal well typically penetrates a greater length of the reservoir, it can offer significant production improvement over a vertical well.

Play is a term used to refer to potential drilling areas whose boundaries are defined by their characteristics, such as varying degrees of hydrocarbon accumulation and other formation factors. A play (or a group of interrelated plays) generally occurs in a single petroleum system. They are used to model a region's prospects or plan for development.

exploration model, that of the "continuous resource" or "resource play." This concept suggests that organic rich shale formations like the Bakken or the Marcellus of the eastern U.S. and the Barnett of Texas are continuously productive over large areas. While the concept admits to significant variations in well-to-well productivity, the risk of dry holes is largely eliminated. Montana's Elm Coulee field currently has about 750 producing Bakken oil wells; during the process of development, only two dry

holes were drilled. It is this level of success that the continuous resource model predicts and delivers.

Bakken may be the magic name for oil resource plays in the northern plains, but the Bakken is not the same in all areas. Due in large part to the wide variation in reservoir properties, the technology used successfully in Montana's initial Bakken development was altered significantly in the North Dakota development.

The North Dakota Bakken development has been dependent on

technology changes that improved the efficiency of the drilling and completion practices to match the Bakken realities in that state. Those same technologies have returned to the Elm Coulee Field, bringing more effective completion techniques for in-fill and step out wells and the recovery of additional oil. Application of this "customized" technology to Bakken development in Richland, Roosevelt, and Sheridan counties holds great promise for migration of the very active development in North Dakota to this portion of eastern Montana.

However, the Williston Basin is asymmetrical and the center of Bakken deposition occurred in an area east of the Nesson anticline, well beyond the border into western North Dakota. The much thicker Bakken formation in this area and the additional pay zones found in the Sanish Sand and Three Forks formation have attracted many investors. This intense level of North Dakota activity changes the timing, but not the potential for significant Bakken development in eastern Montana.

Montana's Energy Future

Although the Bakken formation is present in other areas of the state, the dispositional environment and subsequent geologic history may not be identical to that of the Williston Basin. Recent exploration indicates that oil is present in the Bakken as far west as Glacier County. It remains to be determined if technology developed in the Williston Basin will be effective in the shallower, less pressured areas of Bakken occurrence. However, exploratory interest in other areas remains high. ¹²

U.S. Economic Outlook

How Slow Can We Grow?

Patrick M. Barkey, Director, Bureau of Business and Economic Research

The U.S. continues to flirt with the “stall speed” lower limit of growth that the economy can sustain without nose diving into a second recession. And as difficult as it has been to keep the spark of growth alive here, there is ample evidence that Europe has already entered a mild recession. Can the U.S. avoid this fate and at least keep its agonizingly slow recovery intact? It will take a bit of luck and some sound policy decisions, but thus far the road to recovery looks to remain open for next year and beyond.

The following are the top ten economic predictions for 2012, courtesy of IHS Global Insight, Inc.:

1. The United States will probably avoid a recession. The good news is that U.S. domestic risks have diminished somewhat, and growth momentum has picked up modestly. Consumers seem willing to spend, and businesses are more disposed to hire. This means that over the next year, U.S. growth will average between 1.5 percent and 2.0 percent.

2. The Eurozone is headed for a second dip. All indications are that the Eurozone will suffer through a recession in 2012 – a mild one if the region’s sovereign-debt problems are resolved, or a deep one if they are not.

3. Asia will continue to outpace the rest of the world. While Asia will not be immune to a recession in the Eurozone, growth in the region will remain resilient and will continue to be the strongest in the world (around 5.5 percent).

4. Growth in other emerging markets will hold up, for the most part. The Eurozone crisis and

Table 1
Actual and Forecasted Values for Key U.S. Economic Variables

	2011 Q3	2011 Q4	2012 Q1	2012 Q2	2010	2011	2012	2013	2014
Real GDP (percent change)	1.8	3.4	2.0	1.2	3.0	1.8	2.0	2.4	3.4
Consumer Price Index (% change year-to-year)	3.8	3.3	2.3	1.3	1.6	3.1	1.5	1.8	2.0
Ten-Year Treasury Yield (Percent)	2.43	2.05	2.10	2.26	3.21	2.79	2.33	2.84	3.58
Mortgage Rates, 30 year (Percent)	4.31	4.01	3.92	4.01	4.69	4.46	4.08	4.48	5.12
Oil Prices, Refiner Acquisition Cost (Dollars per barrel)	101	102	97	98	77	101	98	106	109
Housing Starts (Millions)	0.62	0.67	0.70	0.72	0.59	0.61	0.73	0.97	1.34
Unemployment Rate (Percent)	9.1	8.8	8.7	8.8	9.6	9.0	8.8	8.6	7.9

* Forecasts as of Jan. 2012.

Source: IHS Global Insight, Inc.

recession will have a differential impact on the rest of the emerging world. Hardest hit will be Emerging Europe (the former Soviet Bloc countries). Latin America and Africa should hold up fairly well.

5. Commodity prices will (mostly) move sideways. During the coming year, commodity prices are likely to get pulled down by weaker global demand – and pushed up by limited excess capacity and continuing robust growth in key economies, such as China and India.

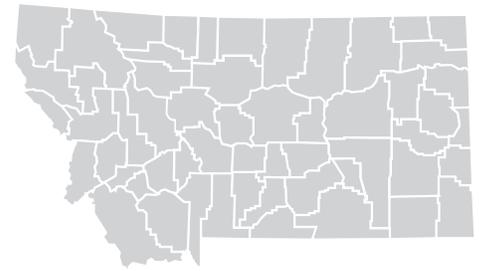
6. Inflation will diminish almost everywhere. With world growth softening and commodity prices off their peaks, inflation in every region of the world will decline in 2012.

7. Monetary policy will either be on hold or ease further. Easing inflationary pressures and increasing anxiety about the growth outlook have changed the priorities of central banks worldwide.

8. Fiscal policy is set to become even tighter in the United States and Europe. Notwithstanding the standoff over deficit reduction in the U.S. Congress, fiscal policy in the U.S. is already tightening. Federal government purchases will contract over the next several years, acting as a major drag on growth. State and local spending is also expected to fall for at least another year.

9. With the exception of the euro, the dollar will keep sliding. Economic fundamentals, alone, would suggest that the dollar should keep sliding against most currencies, especially those of emerging markets.

10. Most of the risks to the outlook are on the downside. Two risks look particularly threatening over the next year. The first is the possibility of a financial meltdown in the Eurozone, with some countries exiting, and/or a messy default by one or more of the large Eurozone countries, especially Italy or Spain. The second big risk is a sharp slowdown in China’s growth (say to 5 percent) triggered by a bursting of its real estate bubble. **12**



Montana Economic Outlook

Recovery Still Stuck in the Starting Gate

Patrick M. Barkey, Director, Bureau of Business and Economic Research

In the information age, it is impossible to avoid learning of every surprise and disappointment in the national economy. Yet if we could somehow forget about the episodes of turbulence in stock markets, the downgrades in both national forecasts and government debt, and the fall in consumer and business confidence expressed in national surveys, we might feel much better about the economy around us. In fact, there are positive signals in the Montana economy.

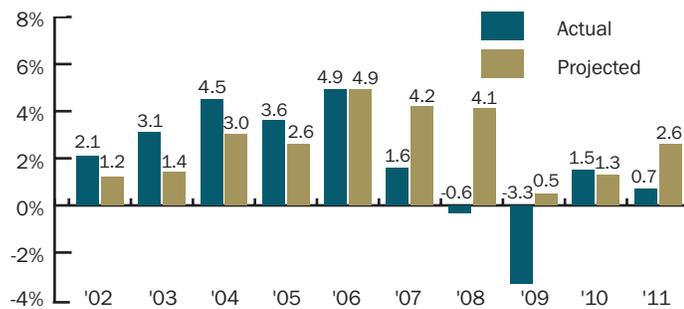
Perhaps the most heartening has been the improvement in state tax revenues. After experiencing the deepest two-year decline in revenue in postwar history, Montana general fund revenues enjoyed growth of just over 10 percent in fiscal year 2011. These were led by increased collections for both the personal and corporate income taxes. There also was an encouraging uptick in payroll employment.

While the 2011 data show some gains, statewide growth in real nonfarm earnings has fallen considerably short of the 2.6 percent increase we foresaw happening a year ago (Figure 1). As judged by this comprehensive measure, the Montana economic recovery thus far remains stuck in the starting gate – actually slowing down from the 1.5 percent growth rate of 2010 to register a disappointing 0.7 percent growth in inflation-corrected nonfarm earnings.

There are at least three factors that led to this less than expected rate of overall growth:

Inflation. After being largely dormant since 2008, spikes in food and energy prices propelled prices ahead at a much

Figure 1
Actual and Projected Change in Nonfarm Earnings, Montana, 2002-2011



Sources: Bureau of Business and Economic Research, The University of Montana; Bureau of Economic Analysis, U.S. Department of Commerce.

Montana Profile

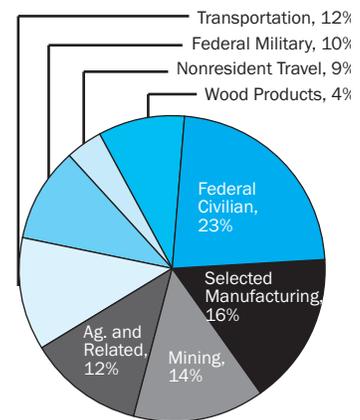
Total Population, 2010	989,415
Percent Change in Population, 2000-2010	9.7%
Median Age, 2010	39.8
Percent 65 or Older, 2010	14.8%
Percent of Population with Bachelor's Degree or Higher, 2010	28.2%
Median Household Income, 2010	\$43,335
Percent of Population without Health Insurance Coverage, 2010	17%
Unemployment Rate, October 2011	6.9%

Sources: American Community Survey, U.S. Census Bureau; Research and Analysis Bureau, Montana Department of Labor and Industry.

faster than anticipated rate in 2011. If price growth had been as originally forecasted, actual growth in 2011 would have been almost a percentage point higher.

Weak Individual Sector Performances. Several sectors of the state economy performed much more weakly than we anticipated in 2011. There were larger than anticipated declines in earnings of federal government workers due to the wind down of the Census and

Figure 2
Earnings in Basic Industries, Montana, 2009-2011 (Percent of Total)

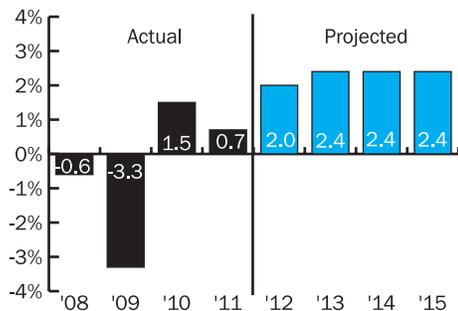


Sources: Bureau of Business and Economic Research, The University of Montana; Bureau of Economic Analysis, U.S. Department of Commerce.

the less active fire season. Health care earnings growth also has been much more sluggish than expected, as health providers deal with higher regulatory compliance costs and lower demand for elective procedures.

U.S. Economic Growth. Growth in the national economy was revised down

Figure 3
Actual and Projected Change in
Nonfarm Earnings, Montana,
2008-2015



Sources: Bureau of Business and Economic Research, The University of Montana; Bureau of Economic Analysis, U.S. Department of Commerce.

sharply for the first half of the year, with overall economic growth just fractionally above zero. Although job growth has continued, discretionary consumer spending remains weak, and with it, the prospects for spending by nonresident visitors to Montana remain cloudy as well.

The exceptions to these developments have been agriculture and, especially, natural resources and energy. Because of oil-related fabrication, repair, engineering, and other development activity, rural eastern Montana's growth has been much stronger than elsewhere in the state. And reasonably strong prices for wheat and calves have helped farmers and ranchers realize another good season for their gross receipts.

In preparing this outlook, we have attempted to strike a balance between the recent performance of the state economy, which outside of housing has been reasonably good, and the climate for future growth, which has become increasingly cloudy. While as of this writing the U.S. economic expansion looks a bit more secure, the prospects for Asia and especially Europe have worsened considerably. A recession in Europe appears more and more certain, with the only question being how severe

Table 1
Population, Montana and Regions, 1990-2010

	Thousands of Persons			Percent Change	
	1990	2000	2010	1990-2000	2000-2010
Montana	800	902	989	12.9%	9.7%
West	287	329	367	14.6%	11.6%
Missoula	79	96	109	21.8%	14.1%
Flathead	60	74	91	25.8%	22.2%
Silver Bow	34	35	34	2.0%	-1.2%
Ravalli	25	36	40	44.2%	11.5%
Rest of West	89	88	93	-1.1%	5.7%
North Central	229	259	266	13.1%	2.7%
Cascade	78	80	81	3.4%	1.2%
Lewis & Clark	48	56	63	17.3%	13.8%
Hill	18	17	16	-5.6%	-3.5%
Fergus	12	12	12	0.0%	0.0%
Rest of North Central	73	94	94	28.8%	0.0%
Southeast	284	314	356	10.6%	13.4%
Yellowstone	114	129	148	14.0%	14.4%
Gallatin	51	68	90	34.4%	32.0%
Richland	11	10	10	-9.8%	0.0%
Custer	12	12	12	0.0%	0.0%
Rest of Southeast	96	95	96	-1.0%	1.1%

Sources: U.S. Census Bureau.

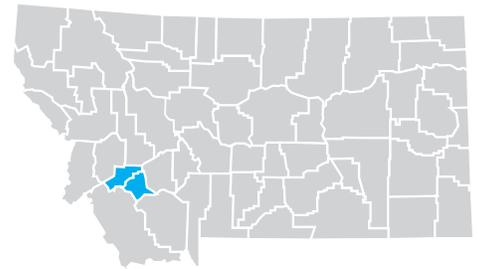
and whether it will be accompanied by a banking crisis.

In this environment, especially with housing and construction still ailing, the prospects of a swift return to faster growth are small. Our baseline forecast calls for growth of between 2.0 percent and 2.5 percent in nonfarm earnings over the next four years, substantially less than the growth that prevailed before the recession. This outlook assumes that:

- The U.S. economy will avoid recession but continue to operate well below its potential for at least the next two years, as spending and savings adjustments in the wake of the 2009 financial crisis continue to be worked out;
- The housing price declines end in 2012, with a modest recovery in construction under way by 2013;
- Global prices for commodities, energy, and food will remain high by historical standards;

- Spending growth will remain severely restrained by revenue shortfalls due to the recession, especially at the state and local levels; and
- Energy and natural resource developments will tilt faster growth toward the eastern part of the state.

The main risk to the forecast is of a new global recession that causes prices of energy and natural resource commodities to fall sharply, as occurred in 2008-09. Such an event is possible, especially if political leaders in Europe allow problems there to snowball to produce an unmanageable situation. On the other side, if construction comes back more quickly than predicted, or business and consumer confidence bounces back sharply, our forecast of near-term growth could be too low. **12**

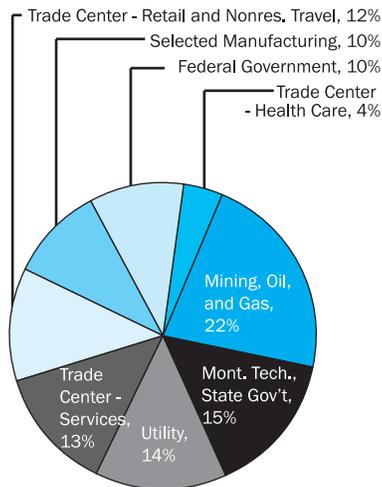


Butte-Anaconda

Serving the World's Economy

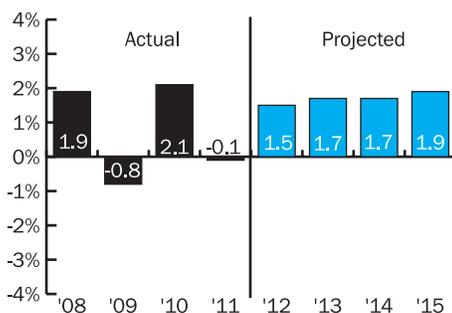
Paul E. Polzin, Director Emeritus, Bureau of Business and Economic Research

Figure 1
Earnings in Basic Industries,
Butte-Anaconda, 2009-2011
(Percent of Total)



Sources: Bureau of Business and Economic Research, The University of Montana; Bureau of Economic Analysis, U.S. Department of Commerce.

Figure 2
Actual and Projected Change in
Nonfarm Earnings,
Butte-Anaconda, 2008-2015



Sources: Bureau of Business and Economic Research, The University of Montana; Bureau of Economic Analysis, U.S. Department of Commerce.

The Great Recession was relatively mild for the Butte-area economy. The modest 2008-09 decline includes smaller bonuses at Montana Resources – an open pit copper and molybdenum mine in Butte – due to temporary softness in copper prices as well as some employment declines and cutbacks in other industries.

The mining and manufacturing industries in the Butte-area economy are closely tied to the global economy and are strongly influenced by international trends. The rapid growth in developing countries during the mid-2000s caused rising commodity and metal prices – including copper. This led to sizable increases in Montana Resources' employment and the return of mining as a major component of the Butte-Anaconda area economic base. This company now employs approximately 350 workers. Overall, the mining industry (which includes other companies) accounts for about 22 percent of the economic base in Butte-Anaconda.

Another company, Renewable Energy Corporation (known as REC Silicon), has positively influenced Butte's economy. The manufacturing plant near Butte was formerly known as Advanced Silicon Materials before REC Silicon – a Norwegian company – bought it in the last decade. The continued operation and stability of this facility, which specializes in renewable energy and has facilities worldwide, provides a good example of benefits of an ownership

Butte-Anaconda Profile

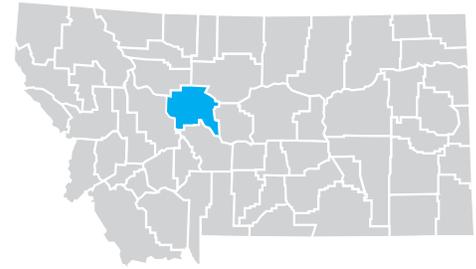
Total Population, 2010	34,200
Percent Change in Population, 2000-2010	-1.2%
Median Age, 2010	41.3
Percent 65 or Older, 2010	16.4%
Percent of Population with Bachelor's Degree or Higher, 2010	22.2%
Median Household Income, 2010	\$38,440
Percent of Population without Health Insurance Coverage, 2010	12.8%
Unemployment Rate, November 2011	6.1%

Sources: American Community Survey, U.S. Census Bureau; Research and Analysis Bureau, Montana Department of Labor and Industry.

change. REC Silicon announced in late 2011 that it would close several of its older European plants but that the U.S. facilities would be unaffected. All of the Butte-area manufacturing facilities together account for about 10 percent of the local economic base.

The mild local recession impacts also can be attributed to other noncyclic components of the economic base. These include the federal government (10 percent), Montana Tech and other state government (15 percent), and the headquarters of NorthWestern Energy (14 percent).

The Butte-area economy is projected to grow about 1.7 percent per year from 2012 to 2015. This projected growth rate is slightly less than the 2.4 percent statewide average and down almost a full percentage point from the pre-recession figures for the Butte-area economy. The major uncertainties concern worldwide economic trends and their influence on commodity prices. ¹²



Cascade County

Malmstrom is a Two-Edged Sword

Paul E. Polzin, Director Emeritus, Bureau of Business and Economic Research

The Cascade County economy has largely escaped the effects of the Great Recession due to its dependence on noncyclical Malmstrom Airforce Base (AFB) and the health care industry. The short-term benefits of relying on the military should be balanced against the longer term risks of significant cutbacks on the base resulting from federal budget concerns and possible changes in defense priorities.

The Great Falls-area economy was one of two urban areas in Montana that did not experience declines sometime during the recent recession. Home construction did sputter to a snail's pace, and some retail sectors were affected, but the impacts were nowhere near those felt in other parts of the state.

Military personnel and civilian contractors account for approximately 46 percent of basic industry earnings in Cascade County. This figure probably slightly overestimates the importance of Malmstrom AFB for two reasons. First of all, this figure includes the Montana Air National Guard, which is located at the Great Falls International Airport. Secondly, military establishments usually have smaller impacts on the local economy (i.e. have smaller multipliers) because servicemen do some shopping at the base exchange rather than at nearby stores. Nevertheless, the base continues to be the largest single component of the economic base in Cascade County.

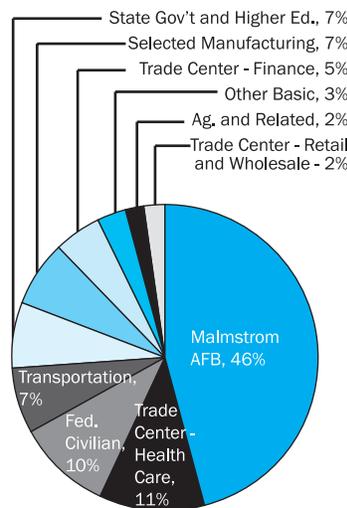
The next Base Realignment and Closing (BRAC) round is not scheduled until 2015. But the current emphasis on major spending cuts means there is the potential for significant reductions in all

Cascade County Profile

Total Population, 2010	81,327
Percent Change in Population, 2000-2010	1.2%
Median Age, 2010	38.9
Percent 65 or Older, 2010	15.6%
Percent of Population with Bachelor's Degree or Higher, 2010	23.9%
Median Household Income, 2010	\$41,828
Percent of Population without Health Insurance Coverage, 2010	14.8%
Unemployment Rate, November 2011	5.6%

Sources: American Community Survey, U.S. Census Bureau; Research and Analysis Bureau, Montana Department of Labor and Industry.

Figure 1
Earnings in Basic Industries, Cascade County, 2009-2011 (Percent of Total)

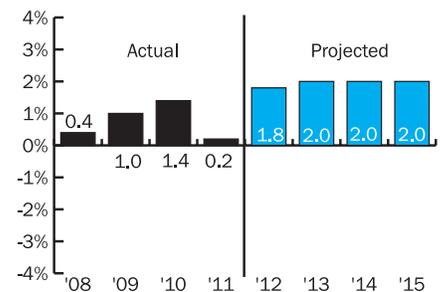


Sources: Bureau of Business and Economic Research, The University of Montana; Bureau of Economic Analysis, U.S. Department of Commerce.

components of the federal government.

Great Falls is the major regional health care center serving central and northern Montana. Nonresidents receiving treatment at local facilities accounted for about 11 percent of the economic base. The medical service area includes Blaine,

Figure 2
Actual and Projected Change in Nonfarm Earnings, Cascade County, 2008-2015

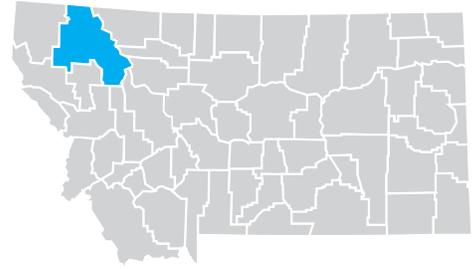


Sources: Bureau of Business and Economic Research, The University of Montana; Bureau of Economic Analysis, U.S. Department of Commerce.

Chouteau, Fergus, Glacier, Hill, Liberty, Phillips, Pondera, Teton, and Toole counties. During the recession years of 2008 and 2009, total employment in health care grew 6 percent and 4 percent, respectively. A recent study conducted for Benefis, the major health care provider in Great Falls, concluded that in addition to its 2,700 jobs, there were an additional 2,100 jobs elsewhere in the local economy indirectly attributable to health care.

Other Great Falls merchants serve customers in surrounding rural areas. This is especially true for businesses in retail, wholesale, and farm implement sales industries. The relatively prosperous conditions on farms and ranches and other areas in north central Montana are quickly transferred to the Great Falls-area economy.

The Great Falls-area economy is projected to grow about 2 percent per year from 2012 to 2015. This is approximately the same average growth rate as before the recession. 12



Flathead County

The Economic Rebound: Three Business Perspectives

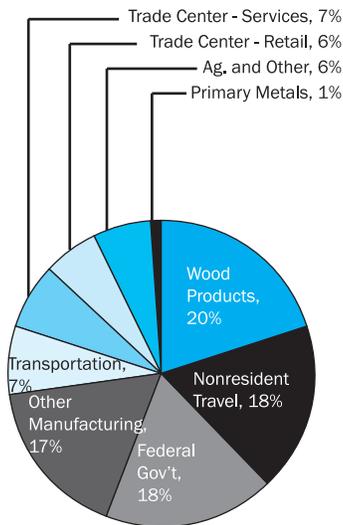
Gregg Davis, Health Care Director, Bureau of Business and Economic Research

Flathead County Profile

Total Population, 2010	90,928
Percent Change in Population, 2000-2010	22.1%
Median Age, 2010	41.2
Percent 65 or Older, 2010	14.4%
Percent of Population with Bachelor's Degree or Higher, 2010	27.6%
Median Household Income, 2010	\$43,585
Percent of Population without Health Insurance Coverage, 2010	19.4%
Unemployment Rate, November 2011	10.96%

Sources: American Community Survey, U.S. Census Bureau; Research and Analysis Bureau, Montana Department of Labor and Industry.

Figure 1
Earnings in Basic Industries, Flathead County, 2009-2011 (Percent of Total)



Sources: Bureau of Business and Economic Research, The University of Montana; Bureau of Economic Analysis, U.S. Department of Commerce.

Probably most would now agree that the peak employment experienced in Flathead County during 2007 was the result of too much froth in the economic expansion. But regardless, over the past three years private employment declines, some significant, were experienced in every major sector except two: health care and the management of companies and enterprises. From 2007 to 2010, more than 5,270 private jobs were lost, with only 416 gained. Most employment losses were in manufacturing and construction, with wage losses totaling \$104 million. Five sectors – utilities, professional and technical services, management of companies, health care and social assistance, and other industries – added more than \$51 million in wage income back into the economy. For a slowdown so broadly spread in the economy, how have businesses responded?

Commercial Banking

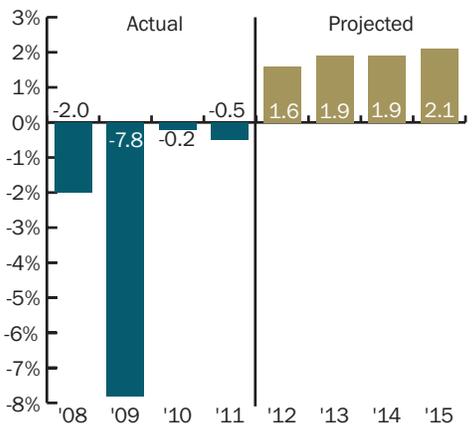
Commercial banking hasn't been hit as hard as other Flathead industries when it comes to employment (down 10 percent), but Glacier Bank in Kalispell first noticed storm clouds forming in September 2008. As all businesses do during economic downturns, Glacier Bank deployed resources to build loan reserves and cut costs through attrition, primarily by focusing on three strategic areas: core competencies, capital preservation and building, and intensified internal communication among its branch offices. Despite the

tough times in the Flathead Valley, Glacier Bank has more optimism this year than in the past two years. Cautious investors are returning to look for reduced-price assets with favorable yields, and among them is the Canadian investor.

Construction

Construction took a hard hit over the past three years, with employment declines of 44 percent from its 2007 peak. Located between Kalispell and Whitefish is Silverbrook Estates, a 325-acre subdivision in phase one of two phases of development. To cope with the slow economy, the development is holding on to inventory, including 236 building-ready sites out of the original 284. Some life is evident because of Canadian interest in vacation properties

Figure 2
Actual and Projected Change in Nonfarm Earnings, Flathead County, 2008-2015



Sources: Bureau of Business and Economic Research, The University of Montana; Bureau of Economic Analysis, U.S. Department of Commerce.

“From 2007 to 2010, more than 5,270 private jobs were lost, with only 416 gained. Most employment losses were in manufacturing and construction, with wage losses totaling \$104 million.”

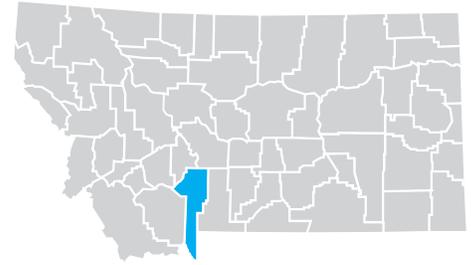
and out-of-state retirees looking for lifestyle changes. Potential buyers now have the opportunity to lease before purchasing a home. Entry-level home prices have been reduced to \$249,950 in hopes of attracting middle-income families. In addition, advertising has been scaled back, instead relying on location and drive-by traffic on Highway 93. The development also hosts various functions on site to increase exposure. Silverbrook is hopeful the real estate market is near its bottom and that home buyers will return this spring. One wild card, however, still looms. The uncertainty surrounding the political wrangling in Washington, D.C. could keep buyers away until people feel confident once again about their future.

Health Care

Personal health care spending in Flathead County this year is almost \$670 million and will increase to more than \$760 million by 2014. The health care sector is one of only two sectors to add jobs to the economy in the three years since the county’s peak employment in 2007. While other sectors in the economy have lost more than 5,000 jobs, health care has added more than 400 jobs, comprising a remarkable 99 percent

of the total jobs added economy-wide, and nearly 85 percent of the wages added to the economy since 2007. But even health care is seeing the effects of the recession. Charity care at Northwest Healthcare in Kalispell is averaging \$1 million per month, most likely a reflection of the jobless rate in the Flathead and health insurance extensions provided through the Consolidated Omnibus Budget Reconciliation Act (COBRA) running out. But the crane positioned over Northwest Healthcare is building for the future, adding \$40 million to the economy for new operating rooms, surgeons offices, and an unfinished third floor for future expansion. Another \$2 million is being spent for a new catheterization lab, electrophysiology suites, and special procedures room, and still another \$14 million for an emergency room expansion and remodel. The third floor of the facility will sit idle for now, but will be ready to accommodate future demands as the population of the valley not only grows, but also grows older.

Kalispell is evolving into a regional trade and service center. Residents are now less inclined to travel elsewhere for their health care, retail, and financial services needs. Because the recession hit the Flathead economy more so than other urban areas in the state, returning to pre-recession levels of labor earnings and employment may prove more challenging in the Flathead. But once the uncertainties surrounding budget policy are worked out in Washington, D.C., residents and visitors may feel more secure about their futures and return to pre-recession levels of spending and investment. 12



Gallatin County Recovery has Started

Paul E. Polzin, Director Emeritus, Bureau of Business and Economic Research

Gallatin County Profile

Total Population, 2010	89,513
Percent Change in Population, 2000-2010	32%
Median Age, 2010	32.5
Percent 65 or Older, 2010	9.5%
Percent of Population with Bachelor's Degree or Higher, 2010	44.4%
Median Household Income, 2010	\$50,239
Percent of Population without Health Insurance Coverage, 2010	13.7%
Unemployment Rate, November 2011	6.7%

Sources: American Community Survey, U.S. Census Bureau; Research and Analysis Bureau, Montana Department of Labor and Industry.

The Great Recession hit the Gallatin County economy hard, but none of the basic industries were permanently scarred. The recession impacts were concentrated in the home building, construction, and nonresident travel industries.

The Gallatin County construction industry bore much of the brunt of the recession. Overall construction activity declined by roughly 37 percent during the 2007 to 2009 period, and the median price of homes in Gallatin County decreased by 32 percent. Single family housing starts dropped from a peak of 1,269 in 2004 to 337 in 2010, a decrease of 73 percent.

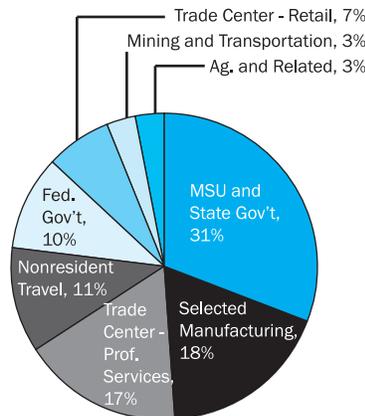
Nonresident travel accounts for about 11 percent of Gallatin County’s economic base and includes the firms

serving tourists and recreationists in Big Sky, West Yellowstone, and the Bozeman area. Spending by nonresidents declined significantly during both 2008 and 2009, in the midst of the Great Recession, and then recovered slightly during 2010 and 2011, but has not regained its pre-recession levels.

Montana State University-Bozeman and other state offices are the largest component of the local economic base, representing about 31 percent of the labor income earned in basic industries. On one hand, these state government jobs are noncyclical and provide an economic buffer during downturns in the business cycle. On the other hand, state employees are now in the third year of a scheduled four-year wage freeze, and this sector contributes little to local economic growth.

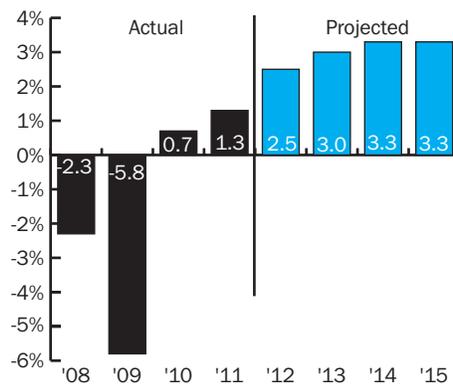
Gallatin County is the state’s center for high tech. These companies include manufactures such as Lattice Materials and Wavelength and software producers such as RightNow Technologies. Manufacturing, which also includes non-high-tech companies, accounts for about 18 percent of the economic base. Selected services, such as software production, represent about 17 percent. The sale of RightNow Technologies to Oracle (a multinational computer technology corporation) has recently been announced, and some concerns about the future of the company’s Montana operations have been expressed. But there are recent examples of sales that have benefited

Figure 1
Earnings in Basic Industries,
Gallatin County, 2009-2011
(Percent of Total)



Sources: Bureau of Business and Economic Research, The University of Montana; Bureau of Economic Analysis, U.S. Department of Commerce.

Figure 2
Actual and Projected Change in
Nonfarm Earnings, Gallatin County,
2008-2015



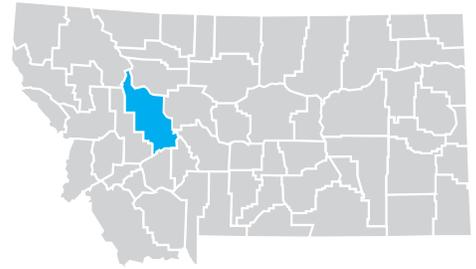
Sources: Bureau of Business and Economic Research, The University of Montana; Bureau of Economic Analysis, U.S. Department of Commerce.

“Even though future growth will be more moderate than before the recession, Gallatin County is projected to be among the fastest-growing urban areas in Montana.”

Montana-based companies such as the purchase of Kalispell-based Semitool by Applied Materials, another multinational corporation in Silicon Valley.

The Bozeman area is evolving into a regional trade center. More and more retail trade customers from nearby rural areas are now shopping in Bozeman stores rather than traveling to Billings. Health care has also expanded significantly but has not yet reached “export” status where the inflows of patients exceed those going to Billings or elsewhere for treatment.

After two consecutive years of declines in 2008 and 2009, the Gallatin County economy posted a slight increase in 2010 and a modest acceleration in 2011. The forecasts are for approximately 3.2 percent growth from 2012 to 2015. These increases are down sharply from the roughly 6 percent annual increases from 2001 to 2007. Even though future growth will be more moderate than before the recession, Gallatin County is projected to be among the fastest-growing urban areas in Montana. ¹²



Lewis and Clark County

A Distinctly Different Recession Experience

Patrick M. Barkey, Director, Bureau of Business and Economic Research

As its moniker suggests, the recent “Great Recession” has been different than previous downturns. But in at least one respect it has been exactly the same – its effects on Lewis and Clark County have been much more muted than elsewhere in the state. With almost two-thirds of its economic base accounted for by state and federal government, Helena’s economy has always been much less responsive to swings in the private sector economy than the state as a whole. And while Helena’s relatively robust performance has helped businesses and workers survive in better shape than elsewhere, its outlook is clouded by the forces that are expected to reduce public sector growth in the coming years.

The recession’s impacts are visible in Lewis and Clark County, but as a slowdown instead of a reversal in growth. And the closer one moves to the present time, the more pronounced the slowdown appears. From the recession’s onset until the statewide low point at the end of 2009, Helena-area inflation-corrected wages and salaries managed to grow by 3.7 percent, the highest in the state. Despite this growth, the recession remained apparent from declines in construction, retail, and goods distribution industries.

Since that point in time, however, real earnings growth has been practically zero. Government wages and salaries

Lewis and Clark County Profile	
Total Population, 2010	63,395
Percent Change in Population, 2000-2010	13.8%
Median Age, 2010	40.9
Percent 65 or Older, 2010	13.8%
Percent of Population with Bachelor’s Degree or Higher, 2010	35.6%
Median Household Income, 2010	\$51,581
Percent of Population without Health Insurance Coverage, 2010	11.6%
Unemployment Rate, November 2011	4.9%

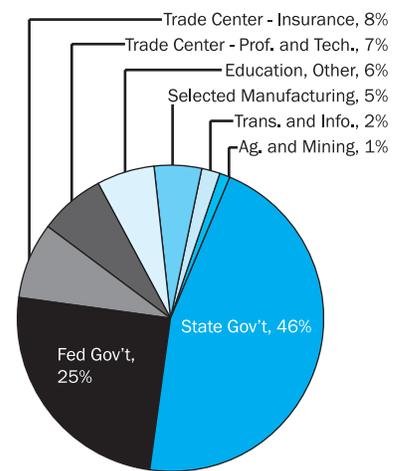
Sources: American Community Survey, U.S. Census Bureau; Research and Analysis Bureau, Montana Department of Labor and Industry.

“The recession’s impacts are visible in Lewis and Clark County, but as a slowdown instead of a reversal in growth.”

barely registered any growth, and were it not for a large increase in wages paid by temporary help supply firms, the declines since the end of 2009 in retail, local public schools, and health care would have produced an actual decline.

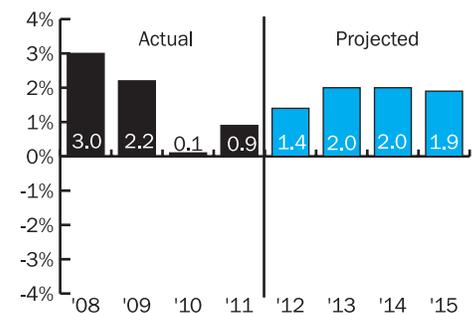
Two years into a state pay freeze and recession-induced pressures on state spending, the performance of the Helena-area economy has been better than expected. Our baseline forecast calls for renewed growth in 2012 and beyond at just below the state average. ¹²

Figure 1
Earnings in Basic Industries, Lewis and Clark County, 2009-2011 (Percent of Total)



Sources: Bureau of Business and Economic Research, The University of Montana; Bureau of Economic Analysis, U.S. Department of Commerce.

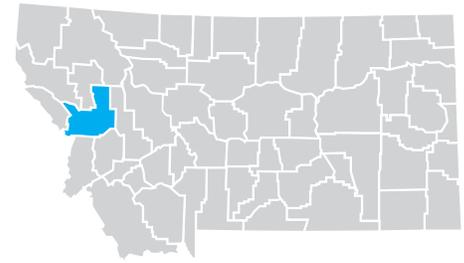
Figure 2
Actual and Projected Change in Nonfarm Earnings, Lewis and Clark County, 2008-2015



Sources: Bureau of Business and Economic Research, The University of Montana; Bureau of Economic Analysis, U.S. Department of Commerce.

Missoula County Still Waiting For Growth to Arrive

Patrick M. Barkey, Director, Bureau of Business and Economic Research



The postponement of the return of stronger growth to Montana's economy was felt acutely in Missoula. Continued declines in construction and manufacturing, as well as a recent retraction in government, caused the Missoula economy to experience a decline in inflation-corrected nonfarm earnings in 2011 – after declining in each of the three previous years as well. As a regional hub for a wide range of retail, professional, and services activities, the sluggishness reflects the continued weak demand among both consumers and businesses in the western part of the state.

We expect to see growth return in 2012, as construction declines are finally halted and a firmer recovery in tourist and trade center-related spending takes hold. Short-term growth prospects are a bit better for professional services and the transportation sectors and a bit worse for government and real estate. Even by 2014, construction activity will be quite restrained by pre-recession standards, but its modest growth will help area banks, equipment dealers, and building supply businesses show signs of life.

Missoula's Recession Experience

The Missoula economy experienced a longer recession than most other parts of the state. Its

Missoula County Profile

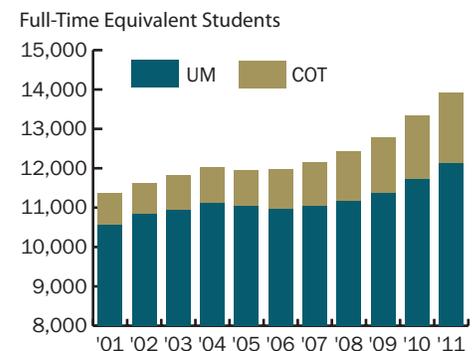
Total Population, 2010	109,299
Percent Change in Population, 2000-2010	14.1%
Median Age, 2010	34.3
Percent 65 or Older, 2010	11.4%
Percent of Population with Bachelor's Degree or Higher, 2010	39.0%
Median Household Income, 2010	\$42,399
Percent of Population without Health Insurance Coverage, 2010	16.3%
Unemployment Rate, November 2011	6.9%

Sources: American Community Survey, U.S. Census Bureau; Research and Analysis Bureau, Montana Department of Labor and Industry.

decline began in 2007, before the national recession was declared, with the closure of the Stimson mill in Bonner. Enrollment growth at The University of Montana, continued growth in health care payrolls, and a major reclamation project at the Milltown Dam offset at least part of the losses from deep declines in home construction, retail, and the closure of the Smurfit Stone pulp mill in the beginning of 2010. Yet the net result was a 3.9 percent contraction in inflation-corrected wages and salaries between 2007 and 2010.

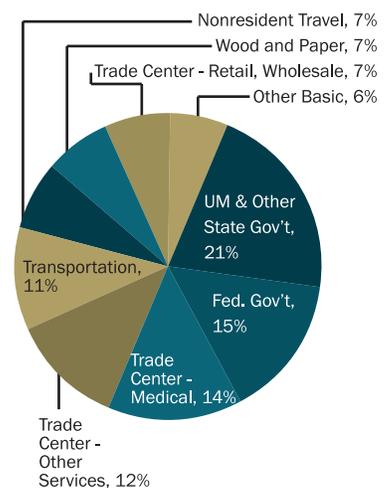
Recovery from the recession low point in the spring of 2009 has been mixed. Recovery in rail and truck transportation has been interrupted by the closure of Smurfit Stone but appears to have returned to levels predating that event. Industries serving out-of-state visitors suffered significant declines, but have swung to register

Figure 1
Enrollment,
The University of Montana – Missoula
and the College of Technology



Sources: Office of the Commissioner of Higher Education.

Figure 2
Earnings in Basic Industries,
Missoula County, 2009-2011
(Percent of Total)



Sources: Bureau of Business and Economic Research, The University of Montana; Bureau of Economic Analysis, U.S. Department of Commerce.

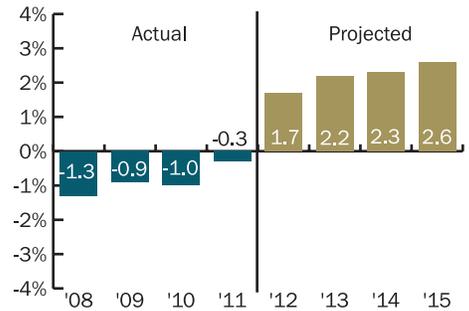
modest growth since late 2010. On the other hand, health care's trajectory has slowed significantly, and the expansion in government earnings due to both the Census and the stimulus has swung towards modest contraction.

Standing alone from these trends has been the growth at The University of Montana, the largest part of Missoula's economic base. Steady increases in research activities and a recession-related enrollment increase of nearly 15 percent have provided steady, if unspectacular, growth in its total payroll. It stands virtually alone among Missoula's major employers in displaying accelerating growth in 2011.

The Outlook

The short-term prospects for Missoula hinge on improvement in the climate for consumer spending and an end to the housing price and construction slump. Our baseline forecast calls for the resumption in growth in 2012, as currently declining sectors such as construction and retail swing to at least modest growth. Overall growth in the Missoula economy will continue to slightly undershoot the state average, as natural resource-led growth propels other parts of the state faster and Missoula continues to experience the gradual erosion of its trade center role to other communities. 12

Figure 3
Actual and Projected Change in Nonfarm Earnings, Missoula County, 2008-2015



Sources: Bureau of Business and Economic Research, The University of Montana; Bureau of Economic Analysis, U.S. Department of Commerce.

Ravalli County
Waiting for Recovery

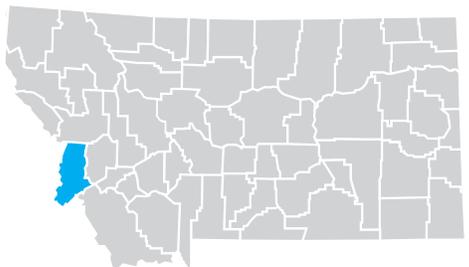
James T. Sylvester, Director of Survey Operations, Bureau of Business and Economic Research

Ravalli County continues to experience the hard times of the current recession, which is evident in the depressed real estate market. While residential real estate sales are about the same in 2011 as in 2009 and 2010, prices continue to decline. The median price for recent residential sales is about 12 percent lower than 2010.

The weak real estate market is affecting Ravalli County household mobility. The latest American Community Survey data show that 11 percent of Ravalli County households live in a different house compared to one year ago. In 2007 when

markets were stronger, 20 percent of households changed homes. Net migration between Missoula County and Ravalli County is essentially zero, reversing a trend from the last decade when people moved from Missoula to Ravalli because of lower housing costs. High gasoline prices and a sluggish housing market have significantly affected migration patterns.

Housing construction, a mainstay of the Ravalli economy, continues to lag, with employment levels about half what they were in 2007. A return to 2007 levels is not seen in the foreseeable future. Construction on Highway 93 is nearly complete,



Ravalli County Profile

Total Population, 2010	40,212
Percent Change in Population, 2000-2010	11.5%
Median Age, 2010	46
Percent 65 or Older, 2010	19.2%
Percent of Population with Bachelor's Degree or Higher, 2010	23.9%
Median Household Income, 2010	\$39,931
Percent of Population without Health Insurance Coverage, 2010	18.9%
Unemployment Rate, November 2011	8.8%

Sources: American Community Survey, U.S. Census Bureau; Research and Analysis Bureau, Montana Department of Labor and Industry.

so future highway construction will decline substantially in the next year.

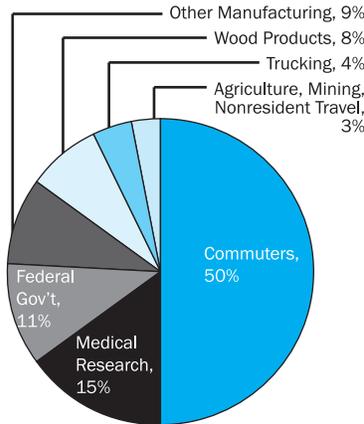
Recovery in the wood products industry, primarily log home

manufacturing, depends on a recovery in the national housing market. Wood supply remains a concern, but poor markets for building materials dominate the decline.

The bright spot in the Ravalli economy is the growth in professional services led by Glaxo-Smith-Kline, a major pharmaceutical company, and the U.S. Center for Disease Control's Rocky Mountain Lab. Both facilities employ medical researchers who earn average annual wages that are more than double the county average of \$23,000 per year.

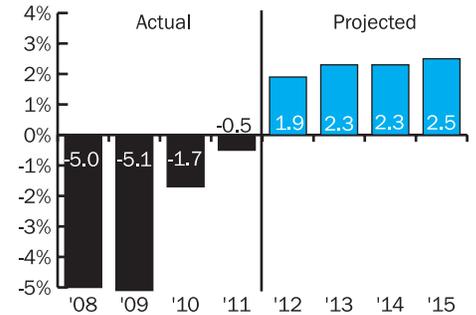
Ravalli County's nonfarm earnings should increase about 2 percent per year through 2015 if the national housing market rebounds, reversing four years of decline. 12

Figure 1
Earnings in Basic Industries,
Ravalli County, 2009-2011
(Percent of Total)



Sources: Bureau of Business and Economic Research, The University of Montana; Bureau of Economic Analysis, U.S. Department of Commerce.

Figure 2
Actual and Projected Change in
Nonfarm Earnings, Ravalli County,
2008-2015



Sources: Bureau of Business and Economic Research, The University of Montana; Bureau of Economic Analysis, U.S. Department of Commerce.

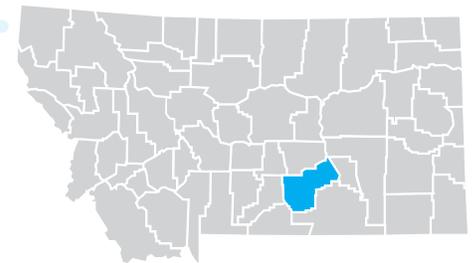
Yellowstone County Economy Improves Moving East

Patrick M. Barkey: Director, Bureau of Business and Economic Research

The Billings-area economy saw respectable growth in 2011 led by growth in its traditional base as a services and distribution hub, as well as by a one-time surge in activities associated with the cleanup of the Yellowstone River from the Exxon-Mobil pipeline rupture. Yellowstone County's growth prospects look bright relative to other parts of the state in light of the oil boom unfolding just across the North Dakota border.

Should that boom shift into Montana – to Glendive, say – then our forecast of growth for Yellowstone County in the coming years could prove to be too low. But despite energy's promise, the uncertain situation for commercial and residential real estate and signs of weakness in consumer spending make the forecast more restrained.

With few exceptions, the Great Recession impacted every part of Yellowstone County's economic base.



Yellowstone County Profile

Total Population, 2010	147,972
Percent Change in Population, 2000-2010	14.4%
Median Age, 2010	38.3
Percent 65 or Older, 2010	14.1%
Percent of Population with Bachelor's Degree or Higher, 2010	29.4%
Median Household Income, 2010	\$47,980
Percent of Population without Health Insurance Coverage, 2010	14.9
Unemployment Rate, November 2011	4.7%

Sources: American Community Survey, U.S. Census Bureau; Research and Analysis Bureau, Montana Department of Labor and Industry.

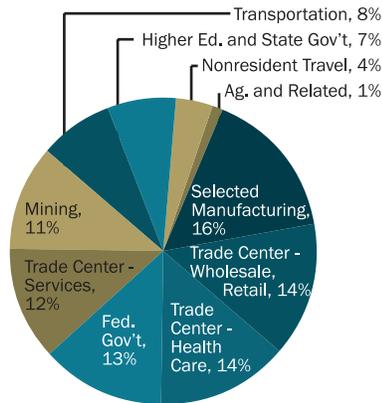
The collapse in commodity prices in 2009, the sharp contraction in the trade, transportation, and distribution of goods, and the housing price bust contributed to a loss of more than \$80 million in inflation-corrected wages and salaries paid, a 3.1 percent decline. The wage decline was most severe for construction, followed by wholesale trade and transportation and warehousing. The overall decline would have been much more severe had it not been for a \$35 million expansion in health care services earnings that occurred at the same time.

The evidence suggests that the trough of the recession for Yellowstone County occurred during the last three months of 2009.

It is heartening to note that most of the major industries in the Billings area that contributed most to the overall decline during the recession have halted their skid. Wholesale trade earnings growth has wiped out almost a third of the recession-induced decline, while transportation and warehousing has eradicated 70 percent of earnings losses since the end of 2009. Support activities for the oil and gas industry have grown enormously since the trough of the recession, posting a 47 percent gain since that time. The data do not yet fully capture the impact of the cleanup activities following the Yellowstone River oil spill, which gave a one-time boost to area contractors, equipment rental companies, and the accommodations industry.

Of Montana's larger cities, Billings is uniquely situated, both geographically and economically, to benefit from the more than four-fold increase in oil drilling activity that has occurred on

Figure 1
Earnings in Basic Industries,
Yellowstone County, 2009-2011
(Percent of Total)

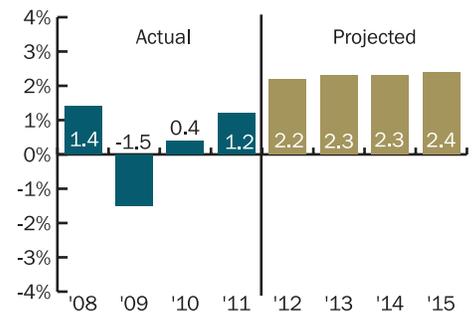


Sources: Bureau of Business and Economic Research, The University of Montana; Bureau of Economic Analysis, U.S. Department of Commerce.

the North Dakota side of the Bakken formation, which straddles the state border with Montana. Even with Montana drilling dormant (to date) by comparison (Figure 3), the repair, engineering, and other services in Yellowstone County have captured a considerable amount of Bakken-related business. Speculation that drilling activity will move west has heated up commercial real estate activity in Billings, particularly for warehousing and industrial space.

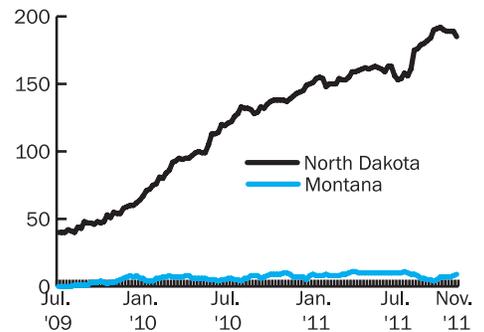
Yet some of the uncertainties that hang over almost every other Montana city cause our outlook for the Yellowstone economy in the coming years to be more restrained than the optimism over energy would suggest. As is the case elsewhere, consumer spending remains extraordinarily weak – the retail trade sector has continued to shrink even as the rest of the economy

Figure 2
Actual and Projected Change in
Nonfarm Earnings,
Yellowstone County, 2008-2015



Sources: Bureau of Business and Economic Research, The University of Montana; Bureau of Economic Analysis, U.S. Department of Commerce.

Figure 3
Oil Drilling Rigs, North Dakota
and Montana, 2009-2011



Sources: Baker Hughes.

grew in 2011. Office space remains abundant, housing prices weak, and construction activity is low.

We expect Yellowstone County growth to accelerate in 2012, with inflation-corrected nonfarm earnings growth roughly at the state average throughout the forecast period of our baseline forecast. 12

Home Sales in 2011

The Adjustment Continues

Scott Rickard, Director, Center for Applied Economic Research, Montana State University-Billings

The residential real estate market for Montana showed little signs of improvement in 2011, with only a small increase in transactions. Meanwhile, home values are continuing to decline and new construction is a fraction of the unsustainable, albeit historic high just five years earlier.

While housing unit sales across the country show little movement, our region shows much more variability (Table 1). According to the National Association of Realtors, the pace of U.S. housing unit sales in 2011 is running 1 percent above that of 2010 totals, with sales at 5 million units.

Within our region, Wyoming shows the largest increase in sales rates at 15 percent. South Dakota and Idaho are experiencing modest sales rate increases of 9 percent and 4 percent, respectively, over their 2010 year-end values, while sales in Montana are slightly above 2010 totals. Only North Dakota appears to be experiencing a sales decline in 2011, with the average annual sales rate for the first three quarters 3 percent below the total sales seen in 2010.

By using data on the repeated sales of individual homes, the Federal Housing Finance Agency creates an index of home prices that estimates how the underlying value of homes change over time for states and larger urban areas. In Montana, this index shows a 2.7 percent decrease in home values over the past year, with Missoula home values losing 3.8 percent and Cascade and

Table 1
2011 Housing Unit Sales Estimates

State	Estimated Number of Sales in 2011	Percent Change from 2010
Wyoming	9,700	15%
South Dakota	15,600	9%
Idaho	40,300	4%
Montana	20,700	1%
United States	4,967,000	1%
North Dakota	12,100	-3%

Source: National Association of Realtors.

Yellowstone counties experiencing losses of 1.3 and 1.0 percent, respectively (Figure 1).

For surrounding states, Idaho fared the worst, with an 8.6 percent statewide decline and home values in Boise down 13.4 percent. In South Dakota, values were little changed while in Wyoming state-average home values show 2.9 percent improvement, but at the same time Laramie County (Cheyenne) has experienced values falling by the same percentage. North Dakota performed best in our region, with values statewide up 5.4 percent and its urban areas seeing value improvements of 1.9 percent to 5.5 percent. It is likely that for Wyoming and North Dakota, continued home value growth is connected to energy development.

Within Montana

Publicly available sales statistics reported by local realty associations allow us to compare the sales and prices in a number of Montana urban areas.

Figure 2 describes the year-over-year change in the number of sales

and median home price for six of Montana's most populated counties. Unlike the FHFA index, median price data reflect the mix of high and low priced homes that are selling in addition to underlying price changes. Using January 1 through September 30 data for each year, only Gallatin County showed both an increase in the number of sales and the median sales price. Median prices increased in Missoula and Cascade counties by 3.3 percent and 0.3 percent, respectively, but the number of sales declined by 4.6 percent in Missoula and 9.7 percent in Cascade County across the same time span. Yellowstone County experienced the same change in the number of homes sold as did Missoula, however Yellowstone County median prices declined by 3.2 percent compared to Missoula's increase. In Lewis and Clark and Flathead counties, the number of homes sold declined by relatively small amounts (0.2 percent in Lewis and Clark and 1.4 percent in Flathead). However, in these counties the median price of these sales were 4.5 percent (Lewis and Clark) and 9.3 percent (Flathead) below the values seen in the same time period in 2010.

Looking at the average length of time needed to sell a residence, only Gallatin County did not see an appreciable increase in this measurement over the past year. Cascade and Missoula counties experienced nearly 4 percent and 8 percent increases, while the average

HOUSING OUTLOOK

days on market for Yellowstone and Lewis and Clark grew by 16.1 percent and 18.5 percent, respectively. Even with this growth, the days-on-market for Yellowstone – at 10 weeks – is one-third less than that for Cascade and Gallatin counties (16 weeks) and only one-half that of Missoula (19+ weeks) or Lewis and Clark (20 weeks).

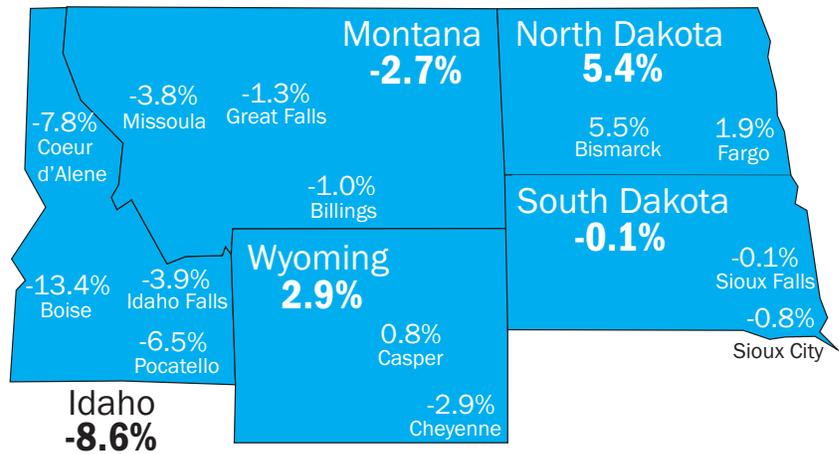
Outlook

There is little reason to expect residential home sales in Montana, or home prices, to increase in 2012. Even if Montana’s economy outperforms the nation as a whole, it will not be enough to improve households’ net worth and too soon to repair their confidence. But there are a few bright spots that point to better performance in the longer term.

A recent Federal Housing Administration forecast predicts price growth in the range of 4 percent to 5 percent in the 2013-2016 timeframe, as does a Macromarket’s survey of economists and industry analysts. Currently fewer than 2 percent of the first liens in Montana are in foreclosure, meaning we don’t have a large excess supply of homes for sale keeping a lid on prices. Also, with the low levels of Montana home construction (down one-third from 2010 and three-quarters from the peak) we may be below the replacement rates needed to supply new family formation, which also points toward growth in demand and prices.

The housing industry may no longer be the economic force it was in the past decade, but home ownership remains a goal and reward which most Americans will seek when their personal economic fortunes make it possible. [12](#)

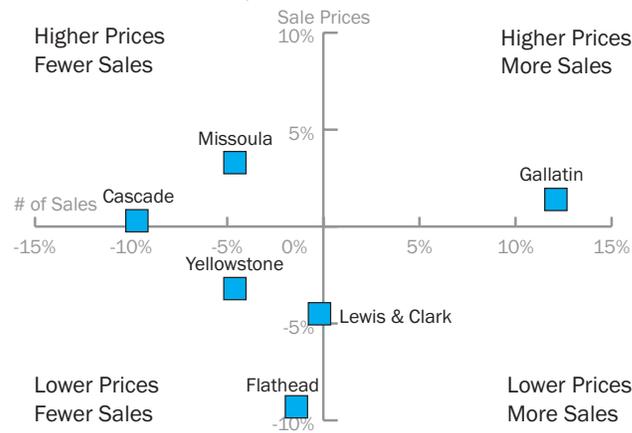
Figure 1
Statewide vs. Urban Area 12-Month Price Index Growth, 2011



Bismarck ND	5.5%	Great Falls MT	-1.3%	Pocatello ID	-6.5%
Fargo ND	1.9%	Denver CO	-2.8%	Spokane WA	-7.5%
Casper WY	0.8%	Cheyenne WY	-2.9%	Coeur d'Alene ID	-7.8%
Sioux Falls SD	-0.1%	Logan UT	-3.6%	Boise ID	-13.4%
Sioux City SD	-0.8%	Missoula MT	-3.8%		
Billings MT	-1.0%	Idaho Falls ID	-3.9%		

Source: Federal Housing Finance Agency.

Figure 2
Home Sales Statistics, 2010-11



County	Number of Sales	Percent Change	Median Price	Percent Change	Days on Market	Percent Change
Cascade	685	-9.7%	\$146,969	0.3%	113	3.7%
Flathead	868	-1.4%	\$180,750	-9.3%	-	-
Gallatin	678	12.1%	\$238,372	1.4%	114	0.0%
Lewis and Clark	507	-0.2%	\$191,000	-4.5%	141	18.5%
Missoula	827	-4.6%	\$206,641	3.3%	136	7.9%
Yellowstone	1,268	-4.6%	\$182,900	-3.2%	72	16.1%

Source: Center for Applied Economic Research, Montana State University-Billings.

Travel and Recreation

Stories Behind the Trends

Norma P. Nickerson, Director, Institute for Tourism and Recreation Research, The University of Montana

What best describes Montana’s travel and recreation industry – growth, stability, or decline? The answer: It all depends on the lens being used, the activity being discussed, and what the weather brings. In fact, it’s best to look at some history to understand where the industry may be headed.

Nonresident travel is dependent on visitors from other states. Seven of the past 11 years have shown growth in both U.S. domestic travel and Montana nonresident travel, but in varying years (Figure 1). What explains these declines and growth? First of all, as long as worldwide population continues to grow, tourism has the potential to always be on a growth trajectory. That doesn’t mean there won’t be dips along the way, but the overall picture shows continual growth for travel in the United States as well as in Montana.

Explaining visitation declines, then, helps us understand what affects tourism. First of all, the 2001 decline in U.S. travel occurred because of the Sept. 11 terrorist attacks. Montana was not affected as much since the busy summer season had already taken place.

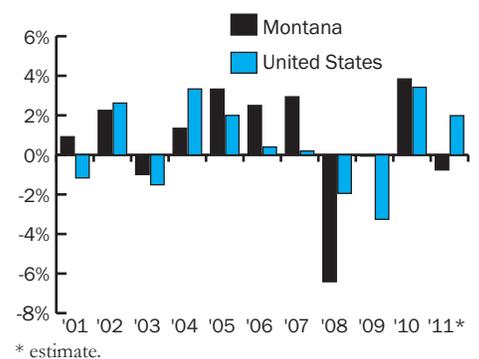
During 2002, travel rebounded, in part due to U.S. residents feeling uneasy about foreign travel and, therefore, exploring their own backyards. Both the U.S. and Montana experienced slight declines in 2003 visitation. In the U.S., leisure travel grew but business travel decreased in 2003, affecting

overall travel numbers. Declining business travel was a lingering effect of the economic downturn from Sept. 11. However, Montana’s nonresident visitation is built upon leisure travel, not business. The persistent drought reduced skier visits because of low snow levels and created serious wildfires in 2003, resulting in a 43 percent drop in visitation for the month of August in Glacier National Park. This scenario helps explain the slight impact on 2003 overall nonresident visitation in Montana.

The next four years (2004-2007) saw growth in visitation for both the U.S. and Montana, but in 2008, gas prices hit record highs during the peak travel season, resulting in a serious pull-back by travelers throughout the U.S. and Montana. Because of gas prices, consumers changed their travel behavior, especially in the number of weekend or long weekend trips taken that summer. With 40 percent of nonresident visitation to Montana relying on visitors who could take weekend or spontaneous trips to Montana (residents of Washington, Idaho, Wyoming, Alberta, and North Dakota), a drop in these trips affected overall visitation numbers.

In the following year, 2009, the United States was deep into the recessionary period. Unemployment nationwide was the highest it has been since the Great Depression. The continual negative economic news had consumers holding on tightly to

Figure 1
Percent Change in Montana and United States Visitation, 2001-2011



* estimate.
Source: Institute for Tourism and Recreation Research, The University of Montana.

their pocketbooks. For the first time in decades, U.S. residents were saving rather than spending their money, resulting in less discretionary money to spend on such things as travel.

The 2010 rebound in traveler numbers has been described as “pent-up demand.” For two years, consumers laid low on spending and traveling. The economy was coming back ever so slightly (the nightly news wasn’t always negative), and people who had delayed past travel opportunities decided they needed a vacation. That wasn’t the entire picture, though. The Canadian dollar, suddenly at par or even slightly higher than the U.S. dollar, encouraged Albertans to travel south into Montana. The Hi-Line and communities just south of U.S. Highway 2 experienced a surge in Canadian visitation. In fact, of the nonresident visitors who said shopping was one of their reasons for

TRAVEL AND RECREATION OUTLOOK

visiting Montana, 27 percent were from Alberta. Growth in 2010 continued in 2011 for the U.S., but Montana is projected to have a slight decline. Preliminary data is showing that the number of travel groups went up but each group had fewer people, thereby reducing the overall total individuals visiting Montana.

In 11 years (2001-2011), U.S. domestic travel has increased 7.2 percent while Montana nonresident visitor numbers have increased 7.8 percent.

A Closer Look at 2011

Weather patterns play a significant role in Montana travel and recreation. With help from La Niña, the 2010-11 ski season was the best on record for the state, recording a 9 percent increase over 2009-10, representing nearly 1.5 million skier visits. Thirty-five percent of all skiers are nonresidents, meaning that 511,575 nonresidents came skiing in Montana and dropped new dollars into the state.

With all that snow, however, it eventually had to melt. The 2011 melting season lasted into July, causing numerous ripple effects. First, the Going-to-the-Sun Road in Glacier National Park had its second ever latest opening of July 13. Second, the Beartooth Highway had a two-week delay in opening due to the heavy snowpack. Third, the late spring run-off in most of Montana caused fishing enthusiasts to delay their fishing expeditions. Finally, Amtrak was stopped by flooding in Minot, North Dakota, for much of June due to snow melt. June Amtrak numbers in Montana dropped 66 percent from June 2010.

“As one advertisement from the Office of Tourism says, “There’s nothing here. ...” People require, need, and desire some of that “nothing.”

With those setbacks, preliminary Montana visitation numbers show a slight decrease in 2011 over 2010 but still exceed 10.2 million nonresident visitors. All these nonresidents visitors support local and small businesses around the state. A recent Institute for Tourism and Recreation Research survey – with a sample of 345 tourism businesses in Montana – highlighted the small business theme. The survey found that 44 percent of the respondent tourism businesses are sole proprietors who don’t hire workers. These types of businesses are mostly represented by outfitters/guides, rental homes/cabins, and bed and breakfasts. For some, it is their sole income. For most, it is supplementary income that allows them to live in Montana. Other tourism businesses vary in their employment listings. Sixty percent of those who have full-time, year-round employees have one to three full-time workers. Twenty-four percent hire 10 or more full-time employees, and these businesses are found in the accommodation sector (motel/hotel, ranches, and resorts).

Trends to Watch

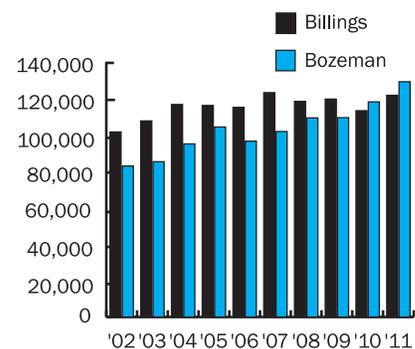
On the national scene, visitation from overseas has seen tremendous growth in recent years due in part to

the soft dollar. The largest increase was in 2010, with 8.8 percent growth from Canada and Mexico and 11 percent growth from overseas. However, as in all international discussions, China tops the list in percent growth of international arrivals to the United States, followed by Brazil. Montana is already experiencing Chinese visitation and has potential for further growth, particularly to the Yellowstone area.

Another trend to watch is the substantial growth in airport deboardings at Gallatin Field in Bozeman. During the third quarter of 2010, Gallatin Field surpassed Billings in airport deboardings for the first time ever (Figure 2). The trend continued in 2011.

Finally, the trend in tourism is growth with occasional small declines. This will always be the case as people desire a change of pace from their daily routines. Montana may not be on everyone’s “bucket list,” but it is close. As one advertisement from the Office of Tourism says, “There’s nothing here. ...” People require, need, and desire some of that “nothing,” and as populations grow, that need for what Montana can offer becomes higher on their list. ¹²

Figure 2
Billings and Bozeman Airport Deboardings, 2002-2011, Q3



Source: Montana Aeronautics Division.

The Affordable Care Act

Health Care Spending in Montana

Gregg Davis, Health Care Director, Bureau of Business and Economic Research

Health Care Spending Under the Spotlight Again

In the past several years, national spending on health care has been at its lowest rate of growth in the 50-year history of the national health expenditures accounts. In 2009, spending grew by 4 percent compared to the average annual growth rate of 9.6 percent since 1960. The slowdown in spending growth is due to a deceleration of private health insurance and health care capital spending, as well as a decline in out-of-pocket spending by consumers during the recession.

While health care spending declined during the economic downturn, so did Gross Domestic Product (GDP). A measure of our nation's economic health, nominal GDP experienced its largest drop (-2.5 percent in 2009) in 72 years. As a result, health care's share of GDP increased a full percentage point in 2009 to 17.6 percent, the largest increase in the history of the national health expenditures accounts. In previous recessions, health care's share of GDP also grew, but by much smaller shares. Health care spending as a share of GDP is expected to reach 19.8 percent by 2020 since spending is expected to grow at 6 percent annually for the foreseeable future, well above most expectations for growth in the nation's economy.

“Health care spending as a share of GDP is expected to reach 19.8 percent by 2020 since spending is expected to grow at 6 percent annually for the foreseeable future, well above most expectations for growth in the nation's economy.”

Deficit Reduction and the “Doc Fix”

One immediate challenge facing Congress is the “doc fix,” a fee schedule with prices for more than 7,000 services used by Medicare beneficiaries. Current law requires the Centers for Medicare and Medicaid Services to update the 7,000 plus prices each year. In 1997, the Sustainable Growth Rate formula was introduced in an effort to keep spending for each Medicare enrollee from growing faster than the growth in per capita GDP.

At the time this article was written, physicians are still facing a 27.4 percent reduction in fee for service Medicare reimbursement in February. Since 2003, Congress has prevented cuts in physician payment schedules 12 times, instead granting increases or freezing the rates to prior year schedules.

The Joint Select Committee on Deficit Reduction, the “Super Committee,” failed to find at least \$1.2 trillion in deficit reductions by November 23, 2011. The Congressional Budget Office estimates the “doc fix” alone will cost \$298 billion over 10 years if physician payments are frozen at present levels and \$358 billion if rates are allowed to increase with inflation.

The Future of Physician Medicare Reimbursement

Should Congress pass a short-term fix to the Sustainable Growth Rate formula before the close of 2011, no offsetting revenues have to be found. Otherwise, Congress will have to find between \$200 billion and \$358 billion in new revenue over the next 10 years just for the “doc fix.” The Medicare Payment Advisory Commission proposed a \$200 billion fix by freezing primary care physician office visit rates for 10 years, and reducing all other services, including those provided by non-primary care physicians by 5.9 percent per year until 2014. Thereafter, all services for all physicians are frozen until 2021. Although one of the lowest cost fixes, it faces stiff opposition by provider groups. Pharmaceutical companies would be required to give rebates to low-income Part D beneficiaries, skilled nursing facilities and clinical labs would

face significant payment reductions, and excise taxes on Medigap plans – the supplemental plans Medicare beneficiaries purchase for physician services – would be imposed.

In a state with a disproportionate share of its citizens eligible for Medicare and a shortage of primary care physicians, failure to find a long-term fix for physician reimbursement could threaten access to medical care.

The Affordable Care Act and its Impact on Montana: Preliminary Evidence

Several provisions of the Affordable Care Act (ACA) may benefit 171,000 Medicare beneficiaries living in Montana. Medicare Part B, the Supplementary Medical Insurance Program, helps pay for physician, outpatient, home health, and preventive services. Of the 134,000 Montanans enrolled in Medicare Part B for 12 months or longer, 4 percent received an annual wellness exam at no cost, compared to 4.1 percent nationally. Several preventive services are also now provided at no cost to Medicare enrollees, including cardiovascular, bone mass, and diabetes screenings, mammograms, and many others. Nationally, 55.6 percent of Medicare Part B beneficiaries received at least one preventive service in the first 35 weeks of 2011, compared to only 42.1 percent of Montana's Part B beneficiaries.

The Affordable Care Act makes Medicare prescription drug coverage (Part D) more affordable. Before the ACA, when the total retail cost of prescription drugs reached \$2,930, the “donut hole,” Medicare beneficiaries

“In a state with a disproportionate share of its citizens eligible for Medicare and a shortage of primary care physicians, failure to find a long-term fix for physician reimbursement could threaten access to medical care.”

were responsible for the full cost of prescription drugs until they reached a level of spending qualifying them for catastrophic coverage (\$4,700). During 2010, those who reached the coverage gap received one-time rebate checks of \$250. Beginning last year, those caught in the donut hole were eligible for a 7 percent discount for generics and a 50 percent discount for brand name drugs. For the first three-quarters of 2011, more than 6,000 Montanans qualified for \$3.5 million in gap discounts, or \$578 per beneficiary. Beginning in 2012, generic discounts increase to 14 percent and increase every year until 2020 when both generic and brand name drugs are discounted 75 percent.

Section 1102 of the ACA established the Early Retiree Reinsurance Program (ERRP) designed to help retirees ages 55-64 keep their employer-sponsored health insurance. ERRP was scheduled to end in 2014, but in May 2011, the program stopped accepting applications. Accumulated payments had already accounted for nearly 75 percent of the \$5 billion appropriated by Congress. In Montana,

ERRP payments totaled \$3.8 million through October 2011, with all but 4 percent going to public employee health insurance programs. Montana state government received \$1.4 million (38 percent), followed by public school systems (32 percent), the Montana University System (10 percent), city governments (9 percent), and county governments (7 percent). Yellowstone County alone accounts for 34 percent of the ERRP funds in Montana.

On the other side of the age spectrum, insurance plans offering dependent coverage now must offer the same coverage to enrollees' adult children up to age 26. While the number of people benefiting from this provision is unknown for Montana, during the first quarter of 2011, nearly 1 million young adults throughout the U.S. between the ages of 19 and 25 gained health insurance coverage.

Perhaps one of the least successful aspects of the ACA is the small business tax credit. The credit has several qualifying conditions, including the proportion of the premium paid by the employer, the number of employees, the average wage, and a premium cap set for each state by the Department of Health and Human Services. Only 5 percent of qualifying small businesses throughout the nation applied for the credit by mid-May 2011. The disappointing response to the federal tax credit is blamed on several factors. First and foremost, businesses found it was simply not worth the time and effort to apply. To make matters worse, the tax form used for the credit, Form 8941, did not contain all the data and calculations necessary to verify each step on the form. In Montana, more than 26,000

postcards were sent to businesses that may qualify for the tax credit. Whether the 2011 tax year and beyond will increase business interest in the tax credit is unclear. Shopping for health insurance however may be easier for small businesses. The Department of Health and Human Services announced in November 2011 an expanded website for small businesses to shop for insurance, by zip code (see www.HealthCare.gov).

Health Care Spending in Montana

A benchmark for tracking health care trends, personal health care spending was \$2.1 trillion throughout the nation in 2009, the most recent data available. Hospital care accounted for 36 percent of this spending, followed by physician and clinical services (24 percent), and prescription drugs (12 percent). This year, personal health care spending is projected to be \$2.4 trillion, and by 2014, when the Affordable Care Act kicks into full gear, \$2.7 trillion.

Personal health care spending in Montana is \$7.2 billion this year, increasing to \$8.2 billion by 2014. How this spending translates to health care jobs in Montana is a relevant policy question since Montana is disproportionately dependent on the health care industry. Only seven other states devote more of their respective GDP to health care than Montana. Health care was by far the major contributor to the 1.1 percent growth in Montana's GDP from 2009 to 2010.

Using health care spending levels for the past 20 years and projecting

them forward to 2014, health care earnings in Montana are estimated according to two scenarios, with and without the policies of the Affordable Care Act. How the health care sector responds to more health care spending is dependent upon whether health care providers can increase productivity or whether there is an expansion in the health care labor force.

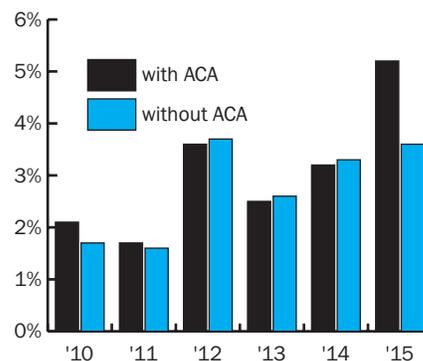
Figure 1 shows the expected growth in health care labor earnings for Montana over the next three years, with and without implementation of the ACA. Earnings in Montana directly attributable to personal health care spending were \$3.3 billion in 2010.

This year, personal health care spending in Montana is expected to increase by \$163 million, supporting more than 5,900 jobs and generating nearly \$256 million in earnings economy-wide. Not only are the average earnings (\$43,000) well above average earnings for all private industries in Montana (\$35,000), the average annual growth in earnings for health care over the past five years has considerably exceeded the growth in private earnings, 4.8 percent compared to only 1.7 percent.

Conclusion

Spending on health care will continue to have a bulls-eye on its back for many years to come. Public health insurance programs alone consume one-fifth of all federal spending, making it a likely target in deficit reduction talks. Given its prominence in budget deliberations nationally, and state concerns about

Figure 1
Projected Annual Growth
in Health Care Earnings, Montana
(in constant dollars)



Sources: Bureau of Business and Economic Research, The University of Montana; Bureau of Economic Analysis, Centers for Medicare and Medicaid Services.

the future of Medicaid, health care will continually be under the budget-cutting scalpel. Certain for the short term, however, is that health care spending will continue to increase. An aging population, health insurance for the uninsured, and technological advances which extend life but do little to contain costs will be the main drivers behind health care spending for years to come and indirectly behind new job creation in health care. But the focus on the growth in health care spending will also limit job creation in the future. The health care industry will have incentives to outsource many of its administrative and technical jobs, adopt measures to increase productivity, and adapt to new payment models that will limit the number of procedures and instead reward providers on value-based delivery. 12

Agricultural Outlook

Floods, Drought, and Price Volatility

George Haynes, Professor and Extensions Specialist, Department of Agricultural Economics and Economics, Montana State University

Montana farmers and ranchers will likely remember the floods of 2011 for many years. A heavy winter snowfall followed by record-setting rainfall in May and June provided a great start to the winter wheat crop, but delayed planting spring crops and left thousands of acres unplanted. At the same time, the southwestern United States was mired in a severe drought. Preliminary harvest figures show U.S. and Montana wheat production down by 9.5 and 19 percent, respectively, and wheat prices up by more than 25 percent from one year ago. The U.S. cow herd continued to decline, driving cattle and calf prices higher. U.S. net farm income is expected to increase by more than 30 percent in 2011, the highest inflation-adjusted value recorded since 1974. Based on gross revenue estimates, Montana net farm income is likely to rise between 15 and 20 percent from 2010 to 2011.

Perhaps, the most important issue in agriculture is food price inflation in 2011. Increases in agricultural commodity prices have driven up food prices by more than 4.5 percent. These increases have been somewhat lower than expected because of the slow economic recovery. The price index for food consumed at home has increased by 6.2 percent, while the price index

“Perhaps, the most important issue in agriculture is food price inflation in 2011. Increases in agricultural commodity prices have driven up food prices by more than 4.5 percent.”

for food consumed away from home has risen at a much slower rate of 2.9 percent over the past year. The USDA expects food price inflation of 2.5 to 3.5 percent in 2012.

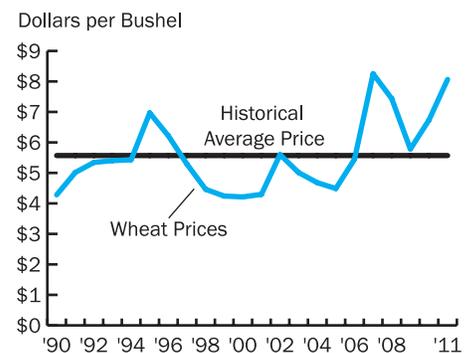
A high-priced agricultural production sector is the organic market, where producers sell directly to consumers or small health food stores. In the past year, organic producers have received substantial price premiums on some products, such as organic milk and eggs. Organic milk has maintained a price premium of around 100 percent over conventional milk, and organic eggs have maintained a price premium of three-fold over conventional eggs. Montana’s most significant organic crop is wheat, which actually sold somewhat below conventional wheat over the past year. Organic agriculture continues to gain a stronger foothold in Montana as

producers respond to the increasing demand for these food products. As the general economy emerges from the recent recession and median household income improves, the demand for high quality organic and locally grown foods will continue to grow.

Outlook for Grain and Wheat

World and U.S. average wheat prices increased by more than 25 percent between 2010 and 2011, from \$6.29 per bushel in 2010 to \$8.00 per bushel in 2011 (Figure 1). These price increases followed a price increase of 10 percent last year. World wheat production rebounded by 1.3 billion bushels, or 5 percent, from 2010. U.S. wheat production declined by 207 million bushels, or nearly 10 percent, while

Figure 1
All Wheat Prices (Inflation Adjusted) and Historical Average Price, 1990 to 2011



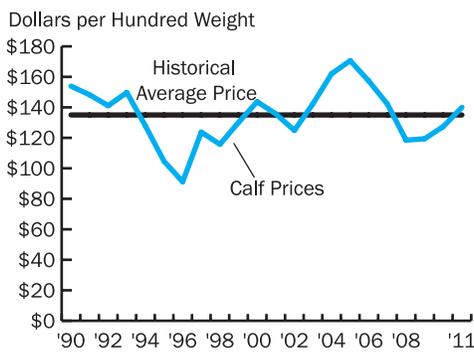
Source: National Agricultural Statistics Service, Montana.

Montana wheat production declined by 40 million bushels, or 19 percent. The most severe production declines in the U.S. occurred in Texas (61 percent), North Dakota (43 percent), Oklahoma (42 percent), and Kansas (23 percent). In the international arena, the Former Soviet Union countries' (FSU-12) wheat production returned to a more normal level of production in 2011 following a very severe drought in 2010. Montana and U.S. shares of world wheat production and sales decreased slightly to around 0.7 percent (world) and 8.8 percent (U.S.), respectively. Current commodity futures prices for September 2012 suggest that grain prices will remain well above historical averages through the 2012 harvest.

In Montana, wheat production decreased by 19 percent from a record-breaking 215 million bushels in 2010 to 175 million bushels in 2011. At harvest time, winter wheat production was down slightly from 2011 because lower average yields and fewer acres planted. Spring wheat and barley production decreased by 29 percent and 19 percent, respectively, from 2010 because of prevented or delayed planting for many producers and lower average yields at harvest time.

U.S. wheat exports are expected to decline by 24 percent this year with increased competition from the Black Sea countries, Australia, Europe, and Argentina. Last year, Russia imposed an embargo on wheat because of severe drought conditions. This year, the strongest export competitor has been from Russia with its abundant

Figure 2
Calf Prices (Inflation Adjusted)
and Historical Average Price,
1990 to 2011



Source: National Agricultural Statistics Service, Montana.

and competitively priced wheat. While U.S. wheat exports are expected to decline, U.S. wheat imports are expected to increase by about 24 percent to 120 million bushels. U.S. wheat stocks at the end of the year are expected to be down 4 percent from 2010 to 827 million bushels. However, world wheat stocks at the end of year are expected to increase by 3 percent from a year ago to 7.4 billion bushels, reflecting the increase in global production.

Several factors are driving the agricultural economy for 2012: consumer demand in developing countries, the weak U.S. dollar, a weak domestic economy, and ethanol. Incomes are rising in many developing countries, which will likely increase wheat, corn, and soybean demand in Asia, especially China. The U.S. dollar continues to be relatively weak against most foreign currencies, except the Euro. In the longer term, a continued weak dollar will make our

grain exports more attractive to our customers abroad. The weak domestic economy has placed 14 million people on unemployment and reduced median household incomes, dampening demand for agricultural products. And finally, ethanol producers are likely to require about 5 billion bushels of corn, or 40 percent of U.S. total corn production, to meet demand in the U.S., and 1.6 billion bushels of corn are needed to meet feed export demand. The demand for corn in the ethanol and domestic and export markets is very strong. Substantially higher corn prices will likely continue to increase feed costs for cattle feeders, resulting in downward pressure on stocker and feeder cattle prices.

Cattle Outlook

The Montana cow herd declined by 2 percent in 2010, but total herd value reached a record high. Drought conditions across the Southwest have resulted in a sell-off of breeding cattle. These drought conditions have driven calf prices up by 17 percent from last year, when calf prices increased by nearly 20 percent over the previous year (Figure 2). Improving economies worldwide are increasing the demand for beef. By the end of the year, U.S. beef exports are expected to set a record, exceeding 10 percent of total production. Drought conditions continue to dominate non-fed slaughter as breeding cattle slaughter rates remain high and supplies of choice-grade cattle have declined. Supplies of beef will be limited as commercial production is expected

to remain low into 2012 and retail prices for pork, a competing product, have remained at unusually high levels. These factors offset some of the impact of higher corn prices and translate into excellent prices for Montana's cow-calf producers.

U.S. commercial beef production has been relatively stable since 2009, although the demand for beef has changed substantially over the past two decades. Montana's beef production increased by 15 percent between 2009 and 2010, but remained virtually stable in 2011. Montana's share of the U.S. beef market remains around 2.5 to 3.0 percent. Commodity futures prices for the cattle market suggest that calf prices will remain strong in 2012.

U.S. beef exports for 2011 are expected to be more than 19 percent higher than in 2010 and are expected to increase slightly into 2012. Most recently, beef exports have been positively affected by a weak dollar. Mexico, Canada, Japan, and South Korea purchase nearly 90 percent of U.S. beef exports. U.S. beef exports have realized substantial increases in sales to Japan (38 percent), South Korea (50 percent), and Canada (39) through the third quarter 2011. Exports to our largest customer, Mexico, are virtually unchanged from last year. Additional export potential is developing with Russia, where our beef exports have increased 72 percent over the past year.

Cattle imports into the United States from all sources are expected to decline by 10 percent in 2011. Canada, one of the largest exporters of cattle to the U.S., has decreased exports to

“Several factors are driving the agricultural economy for 2012: consumer demand in developing countries, the weak U.S. dollar, a weak domestic economy, and ethanol.”

the U.S. by 40 percent over the past year. Canadian pasture and forage conditions have been very good, and slaughter cattle have been priced high enough in Canada that no strong incentive exists to export cattle to the U.S. The decline in Canadian imports has been offset by a 25 percent increase in feeder cattle from Mexico, due to drought conditions.

The economic downturn has changed the price relationship between cheaper (hamburger) and more expensive (steak) cuts of beef. While prices have increased for both, hamburger prices have increased at a faster rate than steak prices because of the increased demand for lower cost beef products. The more rapid increase in hamburger prices in relation to steak prices is less encouraging news for Montana cattle producers, who depend on the steak market for their high quality beef.

Grocery Bill

The largest increases in food prices over the past year have been in fats and oils, eggs, dairy products, and beef and veal, which increased by 10 percent or more. Products made from our wheat

and other grains (cereals and bakery products) increased by 5.6 percent. When assessing food price inflation, there are many other factors than prices at the farm gate. The food dollar is divided between the farm gate value (19 cents) and the marketing value (81 cents); hence, when considering rising food prices many factors must be considered (Canning, 2011). On the marketing side, changes in the price of labor (39 cents), packaging (8 cents), transportation (4 cents), advertising (4 cents), and other off-farm costs (26 cents) are critically important. Recent estimates by the USDA's Economic Reporting Service suggest that food prices are likely to rise in 2012. Although, continued food price inflation in 2012 depends on the pace of the U.S. and global economic recovery and unforeseen production events, such as weather-related disasters.

Conclusion

Montana's farmers and ranchers have weathered the Great Recession with above-average production and strong prices. Grain production was lower in 2011 than 2010 – a record setting production year – while average grain prices approached historical highs. Cattle production remained relatively stable with calf prices gaining strength throughout the year. Farmers and ranchers are cautiously optimistic for 2012, with strong futures prices in the grain and cattle markets. However, all agricultural producers are closely watching the public policy arena, where the continuation of agricultural subsidies is being debated. ¹²

Montana's Manufacturing Industry

Modest Improvement Expected

Todd A. Morgan, Charles E. Keegan III, and Colin B. Sorenson

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The recession of 2007-2009 and subsequent weak economic conditions have led to four years of declining manufacturing employment in Montana. However, these industry sectors continue to be important elements of Montana's economy. Montana manufacturers had sales topping \$10 billion, employed nearly 20,000 workers, and accounted for approximately \$1.1 billion in earnings during 2011.

The manufacturing sectors account for roughly 20 percent of Montana's economic base, and throughout the recession, four Montana counties retained more than 2,500 manufacturing employees with total earnings exceeding \$125 million (Table 1). Although wood, paper, and furniture remains the largest manufacturing sector in Montana by number of employees (Figure 1), earnings are highest in the chemicals, petroleum, and coal section, which has seen growth in employment while wood products has been declining.

Montana manufacturing employment has declined from nearly 24,000 workers at the start of the recession in 2007 to approximately 19,900 workers in 2011, with the majority of the decline (2,600 workers) occurring between 2007 and 2009 when wood, paper, and furniture shed nearly 2,000 jobs. Employment dropped by nearly 800 workers in 2010, followed by another 600 job losses during 2011. Manufacturing

Table 1
Montana Manufacturing Employment and Earnings by County, 2009

	2009 Manufacturing Employment	Percent of Total	2009 Manufacturing Earnings (Millions of 2009 \$)	Percent of Total
Yellowstone	3,567	17%	291	27%
Flathead	3,040	15%	150	14%
Gallatin	2,718	13%	133	13%
Missoula	2,531	12%	128	12%
Ravalli	1,081	5%	38	4%
Cascade	996	5%	58	5%
Lewis and Clark	871	4%	39	4%
Lake	740	4%	27	3%
Silver Bow	608	3%	39	4%
Lincoln	338	2%	9	1%
Park	322	2%	14	1%
Other counties	3,824	19%	135	13%
Montana Total	20,636	--	1,060	--

Source: Bureau of Economic Analysis, U.S. Department of Commerce.

employment turned upward in mid-2010, but fell late in the year and dropped further as the U.S economy weakened and national unemployment hovered around 9 percent throughout 2011. Estimated workers' earnings in 2011 were approximately equal to the \$1.1 billion reported for 2010.

Looking at the past decade and comparing 2001 to 2011, total manufacturing employment and earnings for 2011 are estimated to be 18.3 percent and 7.4 percent, respectively, lower than 2001 levels in Montana (Table 2). However, a number of sectors have shown growth over the decade including chemicals, petroleum and coal, food and beverages, and a mix of manufacturers in the miscellaneous

category including high-tech and light manufacturing. Declines since 2001 were largest in Montana's wood and paper products industry (see pages 30-31), with segments of Montana's metals, machinery, and nonmetallic minerals manufacturers also suffering declines.

Value of production increased slightly in 2011 to more than \$10 billion. The increase was due to higher gasoline and diesel prices received by Montana's petroleum refineries and increased product prices and output across most manufacturing sectors, offsetting the 2010 closure of the Frenchtown linerboard facility.

Nearly 40 percent of the 211 Montana manufacturing firms that BBER queried as part of its annual

MANUFACTURING OUTLOOK

survey reported increased profits during 2011, versus 30 percent indicating increased profits for 2010. Approximately 34 percent of firms reported decreased profits in 2011.

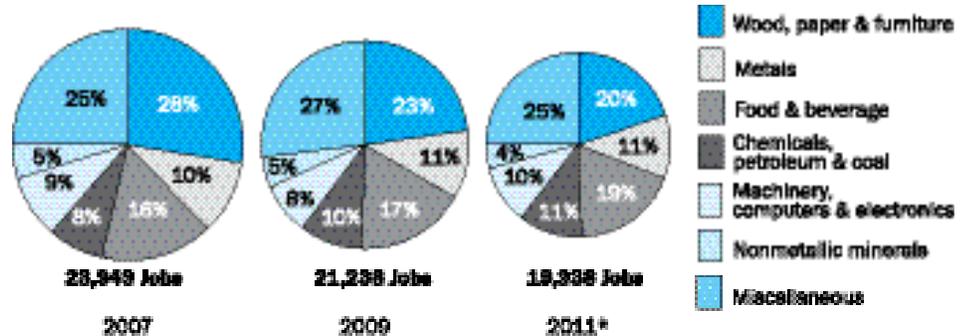
Outlook 2012: Exports, Energy, and Federal Government Spending

The manufacturing outlook for Montana in 2012 is for modest improvement with expectations of employment growth among several manufacturing sectors. Montana manufacturers should continue to benefit from improving export conditions. Exports are projected to continue to increase during 2012. In part due to strong global markets, the high-tech related sectors have shown recent growth, which will continue. Also benefiting U.S. and Montana manufacturers is the continued reduction in the rate of imports of manufactured goods from overseas.

Montana manufacturers that responded to the BBER's annual survey continue to express optimism in the outlook for the coming year. Nearly 50 percent expected improved conditions for 2011, and about 36 percent expect better conditions for 2012. Only 11 percent expect worsening conditions in 2012. More than 90 percent of manufacturing respondents expect to keep their workforce at the same level or increase employment in 2012, while only 7 percent foresee a decline in employment.

Several factors are expected to impact Montana manufacturing in the coming year and beyond. Workers' compensation rates and health insurance costs continue to be identified as the most important issues, followed by cost of energy and availability of

Figure 1
Montana Manufacturing Employment,
2007, 2009, 2011



* estimate

Source: Bureau of Business and Economic Research; Bureau of Economic Analysis, U.S. Department of Commerce.

Table 2
Employment and Earnings in
Montana Manufacturing Sectors, 2001 and 2011

Manufacturing Sector	Earnings			Employment		
	2001 (Millions of 2009 Dollars)	2011*	Percent Change	2001	2011*	Percent Change
Wood, paper & furniture	359	187	-47.9%	7,907	3,969	-49.8%
Metals	103	77	-25.6%	2,526	2,191	-13.3%
Food & beverage	134	144	7.4%	3,365	3,722	10.6%
Chemicals, petroleum & coal	184	303	65.3%	1,607	2,222	38.2%
Machinery, computers & electronics	123	117	-5.1%	2,612	2,058	-21.2%
Nonmetallic minerals	50	40	-20.7%	1,090	885	-18.8%
Miscellaneous	170	171	0.9%	5,283	4,892	-7.4%
Total	1,122	1,039	-7.4%	24,390	19,938	-18.3%

* Estimate.

Source: Bureau of Economic Analysis, U.S. Department of Commerce.

qualified workers. Changes in federal government spending, particularly in the Department of Defense, could impact numerous Montana manufacturers that produce items used by the military. Changes in federal civilian spending, while considered necessary by many of the manufacturers responding to BBER's survey, could impact a variety of firms that provide goods related to the medical, educational, alternative energy, and natural resources fields.

More than half of manufacturers surveyed expect energy development

in Montana – including coal, natural gas, oil, wind, solar, biomass, and geothermal – to impact their business very little or not at all. Approximately 30 percent responded that energy development would positively impact their business, primarily through lower energy costs and through improvements in general economic conditions that could potentially boost sales. Less than 25 percent of manufacturers indicated that energy development would negatively impact their business, with many expressing concern over competition for skilled labor. ¹²

Montana's Forest Products Industry Slow to Recover

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2011: Marginal Changes From 2010 but Big Differences From Pre-Recession Years

Conditions for Montana's forest products industry improved very little during 2011. U.S. housing starts, coming off record lows of 2009 and 2010, increased 10 to 15 percent, up to about 630,000 starts for 2011. Commodity lumber prices, however, were 5 percent lower in 2011 than during 2010. Montana's sawmills, plywood, and reconstituted board facilities reported production levels for 2011 that were down slightly from 2010. Job losses from curtailments and permanent mill closures during 2009 and 2010 continued to be reflected in the state's forest industry employment figures. The logging sector has also suffered from years of extremely low demand for timber as well as competition for skilled labor from the natural gas fields of eastern Montana and western North Dakota.

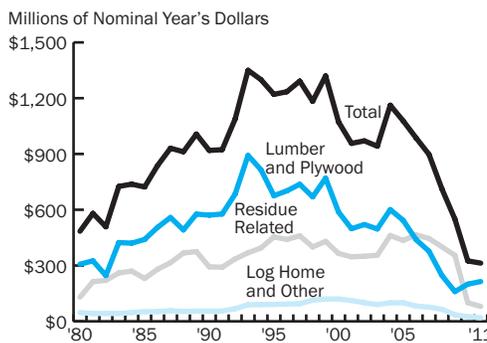
Sales value of Montana's primary wood and paper products was approximately \$314 million (fob the producing mill) during 2011, down about \$11 million or 3 percent from 2010. Primary sales were about \$670 million lower than pre-recession 2006 when sales were just under \$1.0 billion (Figure 1). Sales value of Montana's secondary wood products industry

was approximately \$275 million in 2011. The secondary industry includes window, door, and other wood products manufacturers that use outputs from the primary industry.

Total forest industry employment during 2011 was about 6,530 workers (including private sector foresters and loggers, primary and secondary wood product manufacturers, and forestry support activities), down by about 3 percent from 6,743 workers in 2010. Earnings in Montana's forest industry were about \$256 million during 2011, about 5 percent lower than the 2010 number of \$269 million. Among Montana's remaining sawmills, lumber production for 2011 decreased slightly, to about 495 million board feet lumber tally.

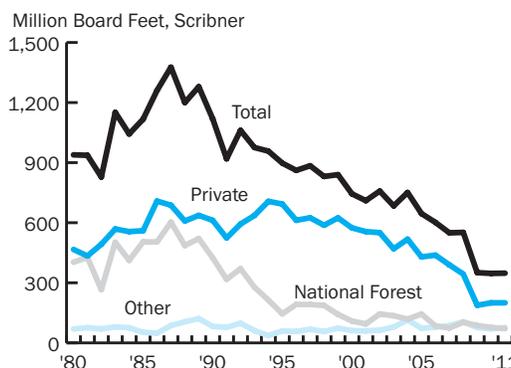
Montana's timber harvest volume during 2011 was an estimated 348 million board feet (Scribner), about the same as the estimate of 347 million board feet for 2010. The last three years' harvests are the lowest since 1945, and the industry is still dealing with harvest levels that have been declining since the early 1990s (Figure 2). The 2011 harvest from private lands is estimated to be 200 million board feet, roughly the same as 2010, which is less than half of the pre-recession 2006 harvest.

Figure 1
Sales Value from Montana
Primary Wood Products Industry,
1980-2011



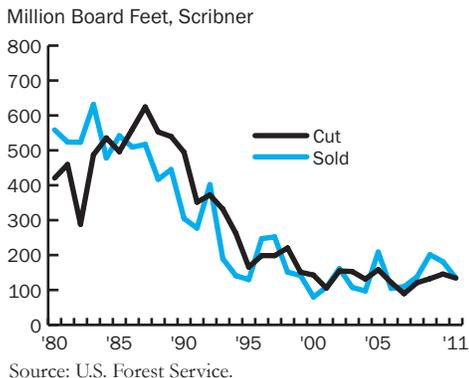
Source: Bureau of Business and Economic Research, The University of Montana; Western Wood Products Association.

Figure 2
Montana Timber Harvest by
Ownership Class, 1980-2011



Source: Bureau of Business and Economic Research, The University of Montana; U.S. Forest Service Region One.

**Figure 3
National Forest Cut and Sold Volumes
in Montana, 1980-2011**



National forest timber harvest during fiscal year 2011 (Figure 3) was 134.2 million board feet Scribner, about 8 percent lower than FY 2010. This harvest volume is approximately 25 percent of the average annual harvest from 1989 through 1991. National forest cut and sold volumes include considerable amounts (nearly 65 percent by volume in 2011) of fuelwood and non-sawlog material that result from salvaging dead timber and fuel reduction treatments. However, with the loss of Smurfit-Stone Container, in-state markets for fuelwood and non-sawlog material are more limited than just a few years ago, while Montana sawmills rely on Forest Service timber for approximately one-quarter of their timber inputs.

**Challenges and Optimism
for the Year Ahead**

National forecasts once again call for slow, modest growth in the U.S. economy and consumption of wood products, with substantial recovery in

“Federal lands, which account for more than 75 percent of the non-reserved timber in the state, face proposed budget cuts and a slew of internal and external issues that continue to keep timber harvest levels at historic lows.”

U.S. housing starts not predicted until 2013 and beyond. Lumber sales to China have benefited a few Montana mills that were selling products to the Chinese; however, increased Chinese demand is focused on logs more than lumber. International log exports from Montana to date are very low, but if transportation rates to coastal ports become low enough to allow Montana more access to overseas markets, Montana landowners and loggers could benefit, while Montana mills could face higher log prices from competition with exporters.

Montana’s forest industry will continue to deal with a combination of local factors that make major recovery in the near-term seem unlikely. Although the pulp mill site in Frenchtown has been purchased, its future use is still unknown and may or may not involve wood products. The mountain pine beetle continues to impact large portions of the state’s lodgepole and Ponderosa pine forests. Attempts to develop Montana’s woody

biomass energy industry have been hampered by very low prices for natural gas and air-quality concerns. Federal lands, which account for more than 75 percent of the non-reserved timber in the state, face proposed budget cuts and a slew of internal and external issues that continue to keep timber harvest levels at historic lows.

Optimism among Montana’s forest products industry has slipped from previous years. Only 11 percent of wood products manufacturers responding to the Bureau’s annual survey believe that 2012 will generally be better than 2011. More than 20 percent of respondents expect profits to decrease in 2012, and 89 percent do not expect to make major capital expenditures during 2012.

Despite these challenges, several manufacturers, agency personnel, and policymakers involved with Montana’s forest industry remain optimistic and eager to capitalize on new opportunities. Development of new wood-using industries continues, with the recent opening of a wood chipping facility at the mill site in Bonner that will process lower value timber suitable for pulp mills and biomass energy, and the start-up of firms converting wood into bio-based products that can replace petroleum-derived chemicals. Other efforts related to sustaining and revitalizing Montana’s forest industry include a Montana-based nonprofit planning to use beetle-killed timber to provide building materials for disaster victims, a grassroots campaign to promote locally harvested and manufactured wood products, and exploration of a Montana Forest Products Retention Office. ¹²

Outlook 2012 Speakers



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