

IOWA Department of REVENUE

Iowa Leading Indicators Index August 2010 Report

Tax Research and Program Analysis Section
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The Iowa Leading Indicators Index (ILII) rose to 100.4 (100=1999) in August 2010 from 99.8 in July. The Iowa non-farm employment coincident index was flat during August after a 0.02 percent increase in July.

The ILII's value increased 0.6 percent in August, matching the 0.6 percent increase in July, and is the eleventh consecutive monthly increase in the index. During the six-month span through August, the ILII rose 4.0 percent (an annualized rate of 8.0 percent). The six-month diffusion index (value of 87.5) reflects an increase of 0.05 percent or greater over the last half year in seven of the eight components, with the yield spread experiencing a drop exceeding 0.05 percent over that time.

In August, six of eight Iowa Leading Indicators Index components contributed positively. The positive contributors were the agricultural futures profits index, unemployment insurance claims (inverted), the new orders index, diesel fuel consumption, average weekly manufacturing hours, and the Iowa stock market index. The negative contributors were the national yield spread and new residential building permits.

Figure 1. Iowa Leading Indicators Index and Iowa Non-Farm Employment Coincident Index: January 1999-August 2010

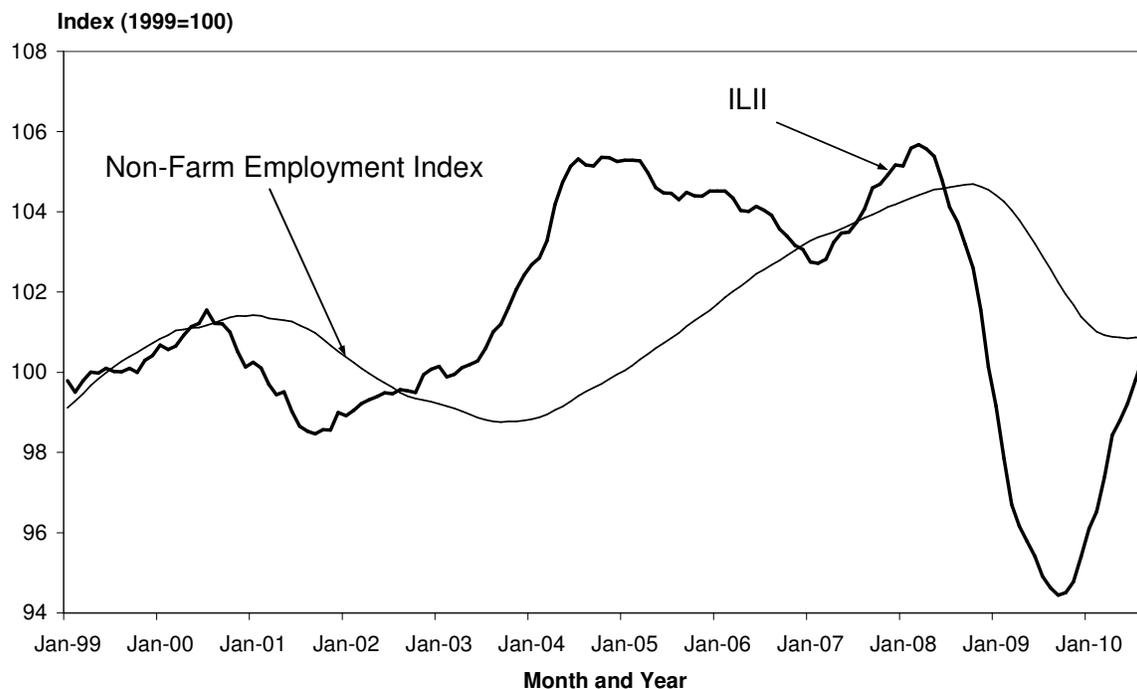


Table 1. Iowa Leading Indicators Index: Six Month Overview

Monthly Values	2010					
	March	April	May	June	July	August
ILII	97.4	98.4	98.8	99.2	99.8	100.4
Percentage Change ^a	0.9%	1.1%	0.4%	0.4%	0.6%	0.6%
Diffusion Index ^b	93.8	100.0	75.0	62.5	75.0	75.0
Six-Month Values	Sept to March	Oct to April	Nov to May	Dec to June	Jan to July	Feb to August
ILII						
Percentage Change	3.1%	4.2%	4.2%	4.0%	3.9%	4.0%
Annualized Percentage Change	6.3%	8.3%	8.5%	8.0%	7.7%	8.0%
Diffusion Index	87.5	100.0	87.5	87.5	75.0	87.5

Source: Tax Research and Program Analysis Section, Iowa Department of Revenue, produced September 28, 2010.

a. Percentage changes in the ILII do not always equal changes in the level of the ILII due to rounding.

b. A diffusion index measures the proportion of components that are rising based on the actual changes (not the standardized contributions to the ILII). Components experiencing increases greater than 0.05 percent are assigned a value of 1.0, components that experience changes less than an absolute value of 0.05 percent are assigned a value of 0.5, and components experiencing decreases greater than 0.05 percent are assigned a value of 0.0.

Table 2. Iowa Leading Indicators Index Components: Six Month Overview

Component Series Monthly Values ^a		2010					
		March	April	May	June	July	August
AFPI ^b	↑ ^c						
Corn Profits (cents per bushel)		31.6	23.9	14.4	14.7	25.1	38.6
Soybean Profits (cents per bushel)		185.3	173.8	153.4	149.9	159.5	168.0
Hog Profits (cents per pound)		9.4	11.1	13.1	15.2	17.1	19.7
Cattle Profits (cents per pound)		-3.5	-1.7	-0.3	0.8	1.3	2.4
Iowa Stock Market Index (10=1984-86)	↑	67.01	71.55	67.20	62.00	62.22	62.52
Yield Spread (10-year less 3-month)	↓	3.58	3.69	3.26	3.08	2.85	2.54
Building Permits	↓	641	668	673	672	664	659
Average Weekly Unemployment Claims ^d	↑	6,980	6,675	6,435	6,124	5,813	5,530
Average Weekly Manufacturing Hours	↑	39.6	40.0	40.2	40.4	40.7	40.8
New Orders Index (percent)	↑	55.7	59.1	61.6	64.2	66.4	68.8
Diesel Fuel Consumption (mil gallons)	↑	51.32	51.63	51.97	52.18	52.31	52.58

Source: Tax Research and Program Analysis Section, Iowa Department of Revenue, produced September 28, 2010.

a. For all component series except for the yield spread and the Iowa stock market index, the values represent 12-month backward moving averages.

b. The agricultural futures profits index is computed as the sum of the standardized symmetric percent changes in the four series, each weighted by the commodity's annual share of Iowa cash farm income (updated August 31, 2010).

c. Arrows indicate the direction of the series' contribution to the ILII for the latest month.

d. Changes in unemployment claims are inverted when added to the ILII, thus a negative change in the series contributes positively to the index.

ILII Components

- **Agricultural futures profits index:** Composite measure of corn, soybean, hog, and cattle expected profits, measured as the futures price less estimated breakeven costs, weighted by the respective share of annual Iowa cash farm income. Changes are calculated based on a 12-month moving average. During August, this component contributed 0.21 to the ILII value as the 12-month moving average of expected profits for all four commodities improved, with strong increases in the futures prices of corn, soybeans, and cattle.
- **Average weekly unemployment claims:** Weekly average of initial claims for unemployment insurance in Iowa. Changes are calculated based on a 12-month moving average and are inverted when added to the ILII. The 12-month moving average of claims fell to 5,530 with unemployment claims in August 2010 52.5 percent below August 2009 claims. This component contributed 0.17 to the ILII value. However, initial claims for August 2010 were still 34.6 percent above average August claims (1987-2008).
- **New orders index:** Diffusion index measuring the share of purchasing managers in Iowa reporting increases in orders received for manufacturing output. Changes are calculated based on a 12-month moving average. In August, the index fell to 73.8 from 81.0 in July, but remained above August 2009 when the index was at 44.5. The 12-month moving average of the new orders index rose to 68.8, contributing 0.15 to the ILII.
- **Diesel fuel consumption:** Number of taxable gallons of diesel fuel sold in Iowa. Changes are calculated based on a 12-month moving average. Diesel fuel consumption rose 6.1 percent between August 2009 and 2010, causing the 12-month moving average to rise 0.5 percent to 52.28 million gallons, and contributing 0.09 to the ILII value.
- **Average weekly manufacturing hours:** Weekly average of hours worked in the manufacturing sector in Iowa. Changes are calculated based on a 12-month moving average. For August 2010, this component contributed 0.08 to the ILII value with the 12-month moving average rising to 40.8 from a revised 40.7 in July. August 2010 hours were 41.0, below the historical average for August of 41.4 hours (1996-2008), but above 39.7 hours reported in August 2009.
- **Iowa stock market index:** Capitalization-weighted index of 34 Iowa-based or Iowa-concentrated publicly-traded companies. During August 2010, 16 of the 34 companies gained value, including 3 of the 12 financial-sector companies. The stock market index, rising to 62.52, contributed 0.01 to the ILII value.
- **Building permits:** Number of total permits issued in Iowa for the construction of residential housing units. Changes are calculated based on a 12-month moving average. For August, this component contributed -0.03 to the ILII with the 12-month moving average falling to 659. August 2010 permits were 11.5 percent lower than the number of permits issued in August 2009 and 54.8 percent below the historical average for August (1998-2008).
- **Yield spread:** Difference between the yield on 10-year Treasury bonds and 3-month Treasury notes. During August, the yield spread fell to 2.54 as the long-term rate dropped 31 basis points while the short-term rate was unchanged. For the month, the yield spread contributed -0.10 to the ILII.

Table 3. ILII Components and Standardization Factors for FY 2011

Iowa Leading Indicator Index Components	Standardization Factor
Agricultural Futures Profits Index	0.054
Iowa Stock Market Index	0.017
Yield Spread	0.326
Building Permits	0.037
Average Weekly Unemployment Claims	0.034
Average Weekly Manufacturing Hours	0.284
New Orders Index	0.062
Diesel Fuel Consumption	0.186

Source: Tax Research and Program Analysis Section, Iowa Department of Revenue, produced August 31, 2010. The standardization factors are the inverse of the standard deviation of the month-to-month changes in each component over the January 1999 to June 2010 period. These factors equalize the volatility of the contribution from each component and are normalized to one. The month-to-month changes are based on 12-month backward moving averages for all components except the yield spread and the Iowa stock market index. The yield spread and new orders index changes are simple arithmetic changes; month-to-month changes for the rest of the components are computed as symmetric percentage changes. The factors are updated annually during August.

Comments

The Iowa Leading Indicators Index (ILII) is designed to forecast the likely future direction of economic activity in the state of Iowa. The techniques used to build the ILII follow those used by The Conference Board to construct the national Leading Economics Index (LEI) prior to the 2001 revisions. A one-month movement in such an index does not produce a clear signal, rather it is necessary to consider the direction of the index over several consecutive months. The Conference Board considers a contraction signal in the LEI reliable when two conditions are met: 1. the index declines by at least two percent over a six month period (using an annualized rate); and, 2. a majority of the individual components decline over those six months (the six-month diffusion index less than 50.0).

The Iowa non-farm employment coincident index measures the change in non-seasonally adjusted, total non-farm employment in the state of Iowa. Changes are based on a 12-month moving average of employment and are computed as symmetric percentage changes. The index is a representation of overall economic activity in Iowa.

The employment index and the ILII are constructed to have a value of 100 in the year 1999.

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