

IOWA Department of REVENUE

Iowa Leading Indicators Index July 2008 Report

Tax Research and Program Analysis Section

The Iowa Leading Indicators Index (ILII) fell to 107.0 (100=1999) in July 2008 from a revised 107.6 value in June 2008. The ILII underwent an annual update between the June and July reports which shifted the series up roughly 0.6 points in each month, however the update had little impact on the recent movement of the index. The Iowa non-farm employment coincident index inched up 0.03 percent after a revised 0.02 percent increase in June.

The ILII's value in July decreased 0.6 percent, exceeding the 0.5 percent drop in June. The index has decreased four months in a row, dropping 0.1 in May and 0.2 percent in April. During the six-month span through July, the ILII dropped 0.9 percent (a -1.7 percent annual rate). The six-month diffusion index (value of 25.0) reflects two of eight components experiencing a 0.5 percent or greater increase over the last half year, the agricultural futures price index and the yield spread, and the remaining six components experiencing a 0.5 percent or greater decrease.

In July, two of the eight Iowa Leading Indicators components increased. The positive contributors were the agricultural futures price index and the yield spread. The negative contributors were average weekly manufacturing hours, new residential building permits, the new orders index, unemployment insurance claims (inverted), diesel fuel consumption, and the Iowa stock market index.

Figure 1. Iowa Leading Indicators Index and Iowa Non-Farm Employment Coincident Index: January 1999-July 2008

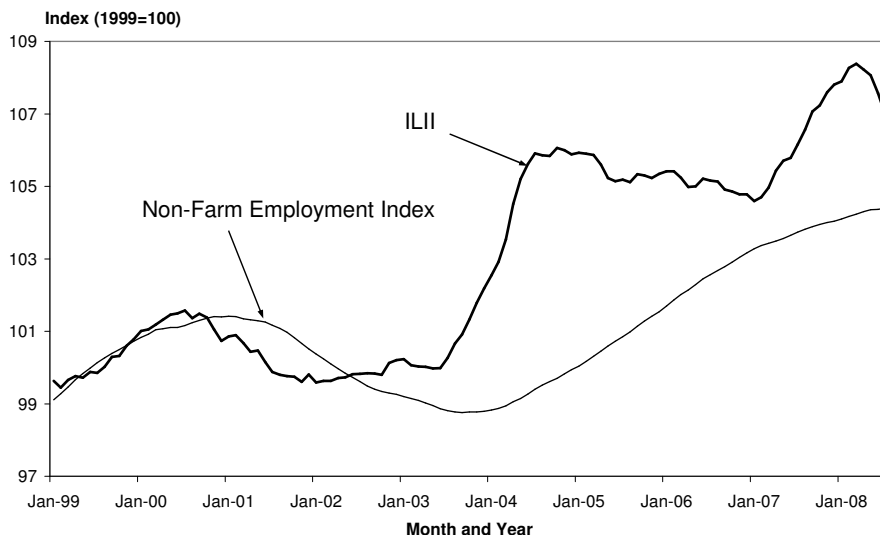


Table 1. Iowa Leading Indicators Index: Six Month Overview

Monthly Values	2008					
	February	March	April	May	June	July
ILII	108.3	108.4	108.2	108.1	107.6	107.0
Percentage Change ^a	0.3%	0.1%	-0.2%	-0.1%	-0.5%	-0.6%
Diffusion Index ^b	56.3	56.3	37.5	25.0	25.0	25.0
Six-Month Values	Aug to February	Sept to March	Oct to April	Nov to May	Dec to June	Jan to July
ILII						
Percentage Change	1.6%	1.2%	0.9%	0.4%	-0.2%	-0.9%
Annualized Percentage Change	3.2%	2.5%	1.8%	0.9%	-0.4%	-1.7%
Diffusion Index	87.5	75.0	75.0	62.5	43.8	25.0

Source: Tax Research and Program Analysis Section, Iowa Department of Revenue, produced August 28, 2008.

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		2008					
		February	March	April	May	June	July
AFPI ^b	↑ ^c						
Corn (cents per bushel)		402.4	414.7	434.1	453.2	481.4	508.3
Hog Profits (cents per pound)		11.6	10.7	10.3	10.4	10.3	10.6
Soybeans (cents per bushel)		979.1	1028.9	1077.0	1123.6	1176.2	1227.1
Cattle Profits (cents per pound)		-1.0	-2.0	-3.0	-3.4	-3.6	-3.6
Iowa Stock Market Index (10=1984-86)	↓	63.84	63.81	63.94	63.85	63.49	62.80
Yield Spread (10-year less 3-month)	↑	1.57	2.23	2.37	2.12	2.21	2.35
Building Permits	↓	890	844	813	785	747	702
Average Weekly Unemployment Claims ^d	↓	3,320	3,346	3,439	3,531	3,791	3,921
Average Weekly Manufacturing Hours	↓	41.4	41.5	41.4	41.4	41.3	41.1
New Orders Index (percent)	↓	60.7	60.3	59.5	58.7	56.0	53.4
Diesel Fuel Consumption (mil gallons)	↓	57.24	57.38	57.25	57.35	57.17	56.88

Source: Tax Research and Program Analysis Section, Iowa Department of Revenue, produced August 28, 2008.

a. For all component series except for the yield spread (the only national series) the values represent 12-month backward moving averages.

b. The agricultural futures price 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 15, 2008).

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 price index:** Composite measure of cattle, hogs, corn and soybeans futures prices weighted by the respective share of annual Iowa cash farm income. Changes are calculated based on a 12-month moving average of the futures price series, where cattle and hogs series also incorporate estimates of break-even costs. During July 2008 this component contributed 0.17 to the ILII value as corn and soybean futures prices continued their rise and expected hog profits increased while cattle profits held steady.
- **Yield spread:** Difference between the yield on 10-year Treasury bonds and 3-month Treasury notes. During July, the yield spread increased as the long-term rate fell 9 basis points while the short-term rate fell 23 basis points. This component contributed 0.03 to the ILII value.
- **Iowa stock market index:** Capitalization-weighted index of 36 Iowa-based or Iowa-concentrated publicly-traded companies. Changes are calculated based on a 12-month moving average. During July 2008 this component fell, contributing -0.07 to the ILII value. Only seven of the 36 companies and two of the 14 financial-sector companies gained value during the month. As part of the annual update, two stocks were dropped from the index, including one financial company, and the stock of one manufacturing company was added.
- **Diesel fuel consumption:** Number of taxable gallons of diesel fuel sold in Iowa. Changes are calculated based on a 12-month moving average. During July 2008 this component's contribution to the ILII value was -0.09 as diesel fuel consumption decreased 6.1 percent relative to the prior year. Because of the two-month lag in this component, part of the reduction reflects impacts of the flood including the closure of part of I-80 and other travel disruptions throughout Iowa.
- **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. During July 2008 this component contributed -0.11 to the ILII value with unemployment claims 66.1 percent above July 2007 claims because of manufacturing lay-offs.
- **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. The monthly new orders index value rose slightly in July to 38.2 from June's 35.7, but remained far below the July 2007 value of 69.6. With the low number attributed to continued negative impacts on manufacturers from the June floods, this component contributed -0.15 to the July 2008 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. During July 2008 this component contributed -0.17 to the ILII value. July permits dropped 13.7 percent below June's value and 46.0 percent below the number reported in July 2007, pushing the 12-month moving average down by 6.0 percent. July 2008 permits were 50.3 percent below the historical average for July, based on reports from 1998 through 2007.
- **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. During July 2008 this component contributed -0.18 to the ILII value even as July hours rose 0.3 percent relative to the previous month. However, July 2008 hours were 6.9 percent below the strong July 2007 report, pushing the 12-month moving average down by 0.6 percent.

Table 3. ILII Components and Standardization Factors for FY 2009

Iowa Leading Indicator Components	Standardization Factor
Agricultural Futures Price Index	0.117
Iowa Stock Market Index	0.060
Yield Spread	0.239
Building Permits	0.028
Unemployment Claims	0.032
Average Weekly Hours	0.300
New Orders Index	0.055
Diesel Fuel Consumption	0.168

Source: Tax Research and Program Analysis Section, Iowa Department of Revenue, produced August 15, 2008. 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 2008 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 moving averages for all components except the yield spread, which is the only national series. 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 the summer.

Comments

The Iowa Leading Indicators Index 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 indicators index. A movement in the ILII for only one month 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 national leading indicators index reliable when two conditions are met: 1. the index declines by at least two percent over a six month period (using an annual rate); and, 2. a majority of the individual components also decline over those six months (six-month diffusion index less than 50.0).

The Iowa Non-Farm Employment Coincident Index measures the change in non-farm employment of all workers 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 designed to represent the current state of economic activity in Iowa.

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