

# **Minnesota Business Services Firms Expect Contraction Next Year**

Due to the COVID-19 pandemic, Minnesota business service firms (such as engineers, accountants and architects) expect contraction during the next four quarters, particularly for consumer spending and corporate profits.

These results come from a random sample of Minnesota business service firms conducted in August and September by the Minnesota Department of Employment and Economic Development and the Federal Reserve Bank in Minneapolis.

**Business Services Firms: Previous Four Quarters**
Minnesota business services firms described unchanged or declining conditions. Seventy-nine percent of respondents indicated no changes in selling prices and 70% experienced stable labor availability. Additionally, 62% reported unchanged employment levels. However, 53% indicated decline in sales revenue and 52% reported a drop in profits. Declining conditions were confirmed by diffusion indices, most of which were below 50, indicating contraction.

Business Services Firms: The Coming Year
Minnesota business services firms expect unchanged or declining conditions for the coming year. Seventy-eight percent anticipate unchanged space occupied and 74% expect constant selling prices. Sixty-seven percent foresee unchanged labor availability. Nonetheless, nearly half of respondents expect a decline in profits while 43% anticipate a drop in sales revenue.

All diffusion indexes were below 50, indicating contraction with profits showing the greatest decline at 34, compared to 62 the year before.

**Outlook on the State Economy**Minnesota business services firms expect mostly contracting conditions. Fifty-two percent expect a decline in consumer spending and corporate profits. Additionally, 44% anticipate a drop in employment.

Nearly half of respondents indicated they expect unchanged inflation while a similar percentage (46%) expect an increase.

Most diffusion indexes were lower than 50 indicating contraction with consumer spending at the lowest with 31, compared to 56 the previous year. Only mergers and acquisitions had a diffusion index of 55, indicating expansion.

**Table 1. Minnesota 2020 Business Services Firms Condition Survey Results1**

| **Business indicators in the last 4 quarters:** | **Up** | **Same** | **Down** | **Diffusion Index 2020(2)** | **Diffusion Index 2019(2)** |
| --- | --- | --- | --- | --- | --- |
| Sales revenue | 21% | 26% | 53% | 34 | 62 |
| Profits | 18% | 29% | 52% | 33 | 57 |
| Productivity | 14% | 38% | 48% | 33 | 62 |
| Employment level | 11% | 62% | 27% | 42 | 55 |
| Labor availability | 8% | 70% | 23% | 43 | 41 |
| Selling prices | 6% | 79% | 15% | 46 | 63 |
| Input costs | 17% | 74% | 8% | 55 | 74 |
| Space occupied (square footage)Exports (sales for foreign clients) | 3%3% | 84%84% | 13%13% | 4545 | 5150 |

| Labor indicators in the last 4 quarters | Decrease | 0% | 1-2% | 3-5% | 6-9% | >10% |
| --- | --- | --- | --- | --- | --- | --- |
| Wages per worker | 11% | 47% | 13% | 19% | 3% | 6% |
| Benefits per worker | 11% | 59% | 9% | 13% | 3% | 4% |

| Expected business indicators during the next four quarters | Up | Same | Down | Diffusion Index 2020(2) | Diffusion Index 2019(2) |
| --- | --- | --- | --- | --- | --- |
| Sales revenue | 19% | 38% | 43% | 38 | 66 |
| Profits | 17% | 34% | 49% | 34 | 62 |
| Productivity | 16% | 48% | 36% | 40 | 67 |
| Employment level | 10% | 65% | 25% | 43 | 62 |
| Labor availability | 14% | 67% | 19% | 48 | 47 |
| Selling pricesInput costs | 9%22% | 74%68% | 17%10% | 4656 | 6067 |
| Space occupied (square footage) | 3% | 78% | 19% | 42 | 53 |
| Exports (sales for foreign clients) | 4% | 84% | 12% | 46 | 50 |

| Expected labor indicators during next four quarters: | Decrease | 0 | 1-2% | 3-5% | 6-9% | >10% |
| --- | --- | --- | --- | --- | --- | --- |
| Wages per worker | 13% | 42% | 19% | 22% | 1% | 3% |
| Benefits per worker | 11% | 63% | 9% | 12% | 5% | 0% |

| Expected outlook on the following state economic indicators during the next year:  | Up | Same | Down | Diffusion Index 2020(2) | Diffusion Index 2019(2) |
| --- | --- | --- | --- | --- | --- |
| Employment | 22% | 34% | 44% | 39 | 63 |
| Consumer spending | 14% | 34% | 52% | 31 | 56 |
| Inflation | 46% | 49% | 6% | 70 | 71 |
| Corporate profits | 20% | 28% | 52% | 34 | 60 |
| Mergers and acquisitions | 34% | 42% | 24% | 55 | 67 |

| Have changes in credit conditions in the last4 quarters affected your firm?: |  No Changes |  Increased Hiring | IncreasedCapital Expenditures | DecreasedHiring | Decreased Capital Expenditure |
| --- | --- | --- | --- | --- | --- |
|  | 76% | 2% | 4% | 15% | 15% |

**Impact of COVID-19**New questions inquired about the impact of the COVID-19 pandemic on Minnesota business services firms. The pandemic had a particularly negative effect on revenue and employee productivity. Fifty-seven percent of respondents experienced a decline in revenue while half indicated a drop in employee productivity.

Forty-three percent indicated they did not furlough employees while 44% did not lay off workers.

A significant share of respondents indicated an increase of employees working from home, 64%.

The large majority of respondents indicated they have not missed loan payments (56%) nor rent payments (60%).

Forty-four percent of respondents indicated no change in cash availability while 39% responded they had a decrease.

Nearly half of respondents indicated they expect to go back to normal operations in more than six months while almost one-fifth expressed their businesses will not go back to normal.

Table 2. Impact of COVID-19 on Minnesota Services Firms1

| Impact of COVID-19 on your business:  | Increase | No Change | Decrease | Not Applicable | Total |
| --- | --- | --- | --- | --- | --- |
| Cash availability | 15% | 44% | 39% | 2% | 100% |
| Revenue | 12% | 30% | 57% | 1% | 100% |
| Employee productivity | 11% | 35% | 50% | 5% | 100% |
| Employee furloughs  | 16% | 43% | 6% | 36% | 100% |
| Employee layoffsEmployees working from homeMissed loan paymentsMissed rent paymentsRequested financial assistance | 18%64%4%7%41% | 44%20%56%60%33% | 3%1%3%1%0% | 35%15%37%32%27% | 100%100% 100%100% 100%  |

| Expectations toreturn to normaloperations: | 1 Month orLess | 2-3Months | 4-6Months | More than 6Months | Will Not GoBack to Normal | Little or NoEffect | Going OutOf Business |
| --- | --- | --- | --- | --- | --- | --- | --- |
|  | 0% | 2% | 11% | 48% | 19% | 17% | 3% |

Respondents were asked to provide comments related to the impact of the pandemic on their business. Selected responses are provided *verbatim*, broken down by type of comment:

Hiring:
*“Health concerns for staff have limited new hiring. We are concerned about bringing new people on board. We work close together and know each other’s family and lifestyle. We aren’t concerned about COVID-19 among our existing staff, just any new people we hire.”*

Positive impact:
*“As a broadband provider, demand for our services has been higher than normal. Even so, we’ve been able to function quite effectively with the majority of our staff transitioned to work from home. Operational costs have increased in some areas of our operation due to offering free distance learning services for unserved students as well as free community wifi hot spots.”*

Negative impact:
*“COVID-19 has had a disastrous impact on the airline industry… [Company name] is an important client of ours, and the downturn in the airline industry has negatively impacted our revenue and profit.”*

*“My business is 65% down. It is brutal. I am hanging on by threads, and I don't know how much longer I will [be able] to do this. After 26 years in business it is very sad.”*

No impact:
*“We are doing well. Not worse, just different.”*

Supply Chain:
*“We are a sales firm in the outdoor recreation industry (hunt, fish, camp) and we have seen an increase in demand for our product, but with a number of domestic suppliers, supply chain interruption has created the biggest challenge to keep up with the demand. Recreating outdoors we anticipate will continue to see increased participation until a permanent solution to COVID-19 exists.”*

## Uncertainty:

*“Uncertainty in the marketplace has limited companies’ ability to predict future revenue, and therefore limits their ability to contract for services.”*

## Working from home:

*“Having staff working from home is a challenge to co-ordinate but shows a slight increase in productivity.”*

*“Hard on our business and difficult working from home. People need to communicate in same building.”*

(1) Based on responses from 148 Minnesota business service firms, for a response rate of 12.3%. The sampling error is plus or minus 8.0 percent at a 95% confidence level. Percentages might not add to 100$ due to rounding.
(2) A diffusion index greater than 50 indicates expansion, lower than 50 indicates contraction.
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