

Economics Group

Special Commentary

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Midwestern States: 2019 Midyear Outlook

Weather, Trade Cast Uncertainty over the Heartland

In the face of weakening global demand, continuing uncertainty surrounding trade policy and severe flooding from the wettest year on record, the American Midwest continues to post modest economic gains. The region is facing a host of challenges, both near-term and long-term, but has so far proved remarkably resilient, with real GDP growth accelerating on a year-over-year basis for five consecutive quarters.

The most immediate concern facing the region is the lingering impact from severe and prolonged flooding brought about by incredibly rainy weather. The National Oceanic and Atmospheric Administration reported that the 12 months ending in April were the wettest since records for the United States began in 1895. With fields inundated, the spring planting season was significantly upended—farmers were forced to shift to less profitable crop mixes, or to leave millions of acres entirely bare. High water levels on key waterways throughout the Midwest also disrupted the transport of fertilizer and harvested product.

The Midwest is facing a host of challenges, but has so far proved remarkably resilient.

The flooding only adds insult to injury to a region that has been at the center of the ongoing trade war with China and, to a lesser extent, Europe. U.S. and Chinese officials recently ended negotiations but pledged to resume talks in September. The White House stated that China has confirmed its commitment to purchase more American agricultural products, but the details remain to be seen and President Trump just announced plans to extend a 10% tariff to the remaining \$300 billion of Chinese imports not already covered by tariffs. Lower demand from China has exacerbated the years-long decline in agricultural prices resulting from years of record or near-record harvests at a time when global growth has slowed. The Trump administration has pledged two farm aid packages in excess of \$10 billion, which have cushioned the blow from the trade war but do little to address the longer-term issues facing farmers.

Figure 1

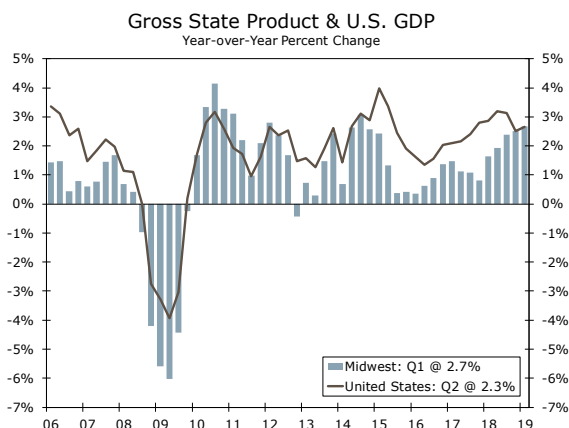
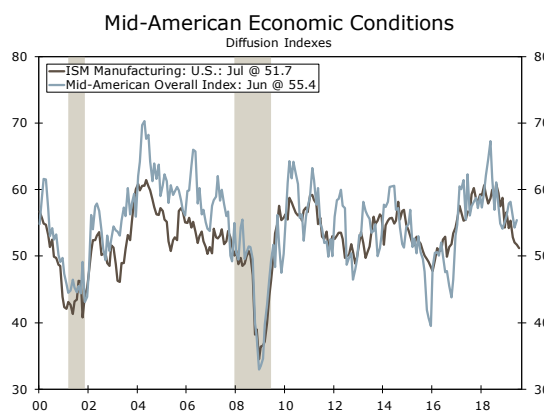


Figure 2



Source: U.S. Department of Commerce, ISM, NAPM and Wells Fargo Securities



Manufacturing Has So Far Proved Resilient

The Section 232 tariffs on steel and aluminum imports that went into effect in 2018 boosted some of the mills and foundries across Ohio, Indiana and Michigan, but the effect on industries utilizing steel and aluminum, including the region’s significant auto manufacturing sector, has been much less positive. These tariffs on Mexico and Canada were lifted in May in a push towards USMCA ratification, which reduced some uncertainty. Mexican retaliatory tariffs on American dairy products were also removed in response to this move.

The Midwest also faces long-term secular challenges related to the region’s ties to traditional manufacturing and its aging demographics. While manufacturing has been surprisingly strong since the middle of the decade, gains in output have significantly outpaced gains in employment. Part of this is out of necessity. Labor markets across the Midwest are very tight. The unemployment rate in the Midwest is roughly even with the nation but the region has the highest job openings rate according to the latest Job Openings and Labor Turnover Survey. The job openings rate compares the number of job openings—currently 1.724 million in the Midwest—with the sum of the region’s employment base and job openings.

Perennially tight labor markets create challenges for employers, particularly manufacturers with huge factories that they cannot easily pick up and move. Unemployment rates in Minnesota (3.3%), Nebraska (3.0%), South Dakota (2.9%), Wisconsin (2.9%), Iowa (2.4%), and North Dakota (2.3%) have consistently ranked among the lowest in the country. Most of these states have older populations that are growing slowly, and their employment-population ratios are among the highest in the country, leaving employers hard-pressed to find the workers they need. Many firms are adopting flexible work schedules to attract workers and are bringing back retirees to fill gaps in their workforce. Employers are also spending more on automation and worker training, so that they can upskill their existing workforce.

Minnesota is a case study on late-cycle economic growth arithmetic. While unemployment has remained low for years, Minnesota state GDP growth has been running ahead of job growth, suggesting the tightness of the labor market has led to a pickup in labor productivity. Many workers who were ‘less than fully employed’—but still counted in the employment statistics—have likely picked up more hours or shifted to higher value-added work, while employers are also likely investing more in labor-saving technology.

While the labor market is tight overall, there are still pockets of slack in parts of Michigan and Ohio. Moreover, several large tech employers have found considerable success hiring workers in new satellite and regional offices in Indianapolis, Columbus, St. Louis and Kansas City. The Midwest will likely slightly underperform the nation over the next couple of quarters as manufacturing pulls back in response to slower global economic growth and efforts to trim inventories.

The Midwest faces long-term secular challenges.

The Midwest will likely slightly underperform the nation over the next couple of quarters.

Figure 3

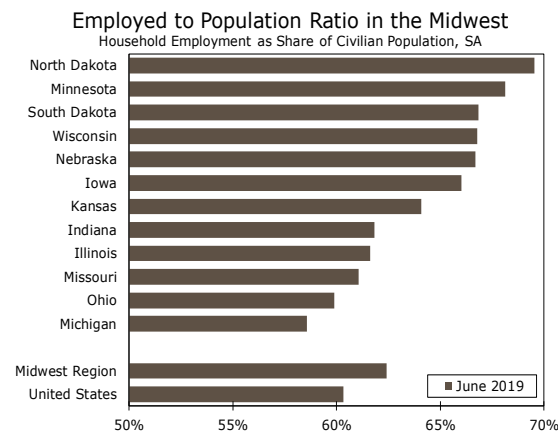
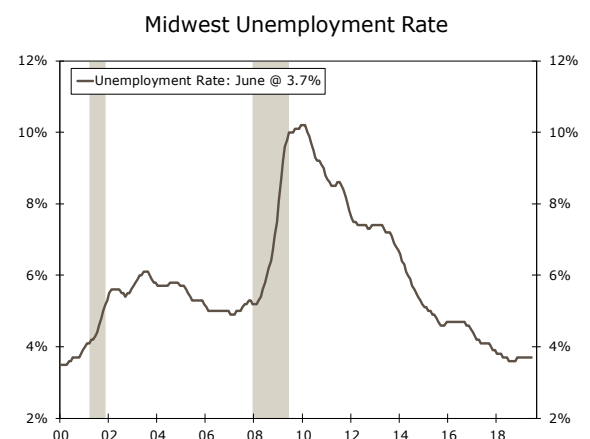


Figure 4

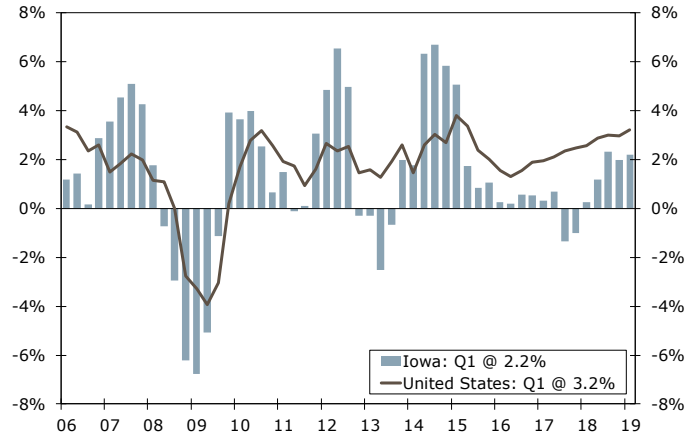


Source: U.S. Department of Labor and Wells Fargo Securities

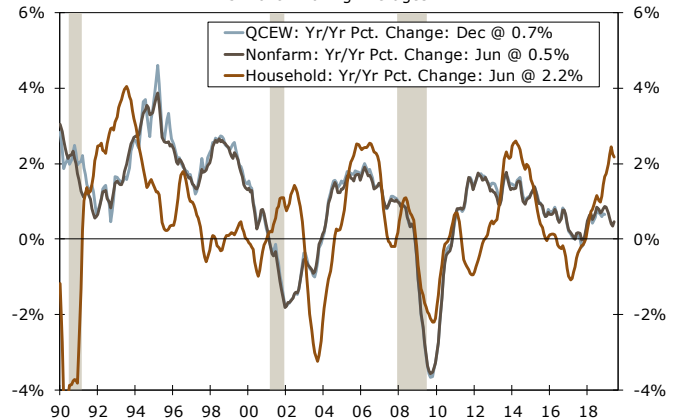
Iowa

- Iowa's economy has struggled to regain the solid momentum it had earlier in the expansion as nonfarm employment growth has slowed to just 0.7% on a year-over-year basis. The state's unemployment rate has remained low at around 2.4% since July 2018 and is currently the third lowest in the nation. Real GDP growth moderated late last year amid rising trade frictions, slowing exports and rising anxiety throughout the agriculture and manufacturing sectors. Growth appears to have remained sluggish through the first half of 2019, which also brought massive flooding to parts of the state.
- Approximately 85% of Iowa's land is used for farmland. Unusually severe spring floods destroyed millions of dollars of stored corn, soybeans and grain, and reduced plantings. Federal aid may help alleviate these losses, as well as losses from trade frictions.
- Renewable fuels are a key part of Iowa's agriculture sector, creating an end market that adds value to crops grown in the state and utilizes waste products. The state is also a key center of biofuel research and is the nation's second largest producer of wind energy.
- Iowa's demographics are challenging. The state has an older population that is growing slowly. Attracting and retaining skilled workers is a constant challenge for employers, particularly in the state's rural areas. A trade deal with China that boosts exports and bolsters global economic growth remains a powerful potential upside.

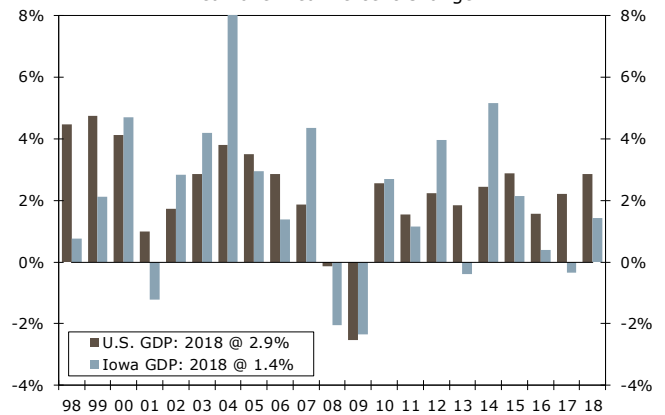
Real GDP Growth vs. U.S.
Year-over-Year Percent Change



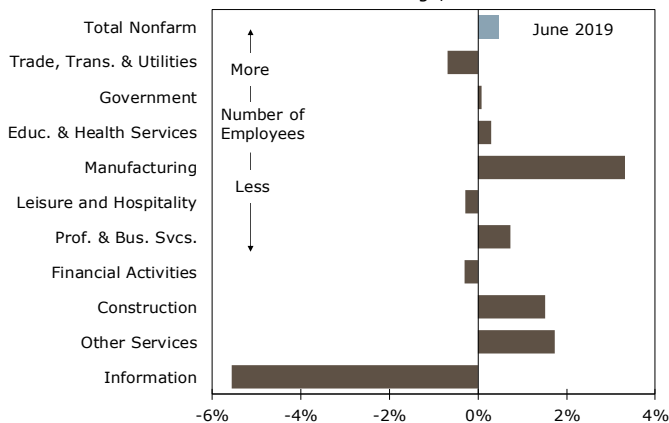
Iowa Nonfarm Employment
3-Month Moving Averages



Iowa Gross State Product & U.S. GDP
Year-over-Year Percent Change



Iowa Employment Growth By Industry
Year-over-Year Percent Change, 3-MMA

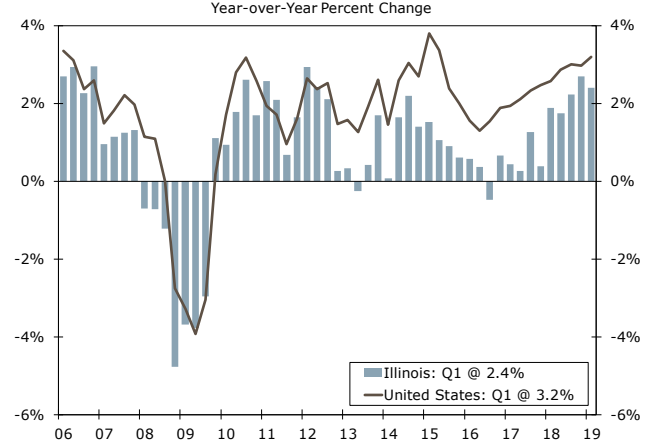


Source: U.S. Department of Labor, U.S. Department of Commerce and Wells Fargo Securities

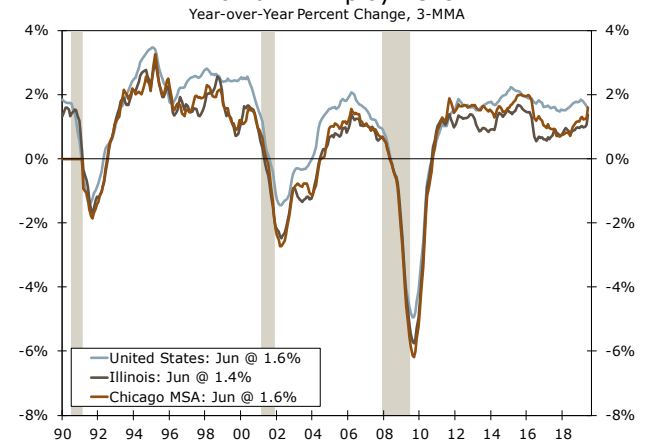
Illinois

- Economic growth gained momentum over the past year in Illinois, despite continuing challenges surrounding the state's finances. Real GDP ended 2018 up 2.2% year-over-year, slightly trailing the Midwest and the nation. Large gains in professional & business and education & health services offset declines in the agricultural sector, highlighting the state's urban-rural split.
- Payrolls have risen modestly, with nonfarm employment up 1.3% over the past year. Trade, transportation & utilities payrolls—20% of the state's total nonfarm jobs—rose just 0.9%, with sluggish growth in retail trade offsetting solid gains in wholesale trade, transportation & warehousing.
- Rising fertilizer costs and falling soybean prices continue to weigh on Illinois' farm sector. The situation only got worse in the first half of the year, when record rainfall flooded thousands of farms. Excess moisture in fields pressured farmers to plant cover crops and delay corn and soybean planting.
- Chicago lost 22,000 residents in 2018. The metro area is losing many of the young skilled workers needed to attract new and expanding businesses. Unemployment has been steady, however, primarily due to the strength of the health services sector, which saw employment rise nearly 3% year-over-year. Over the year, professional & business services was one of the fastest growing industries, with software and tech jobs accounting for much of the increase.

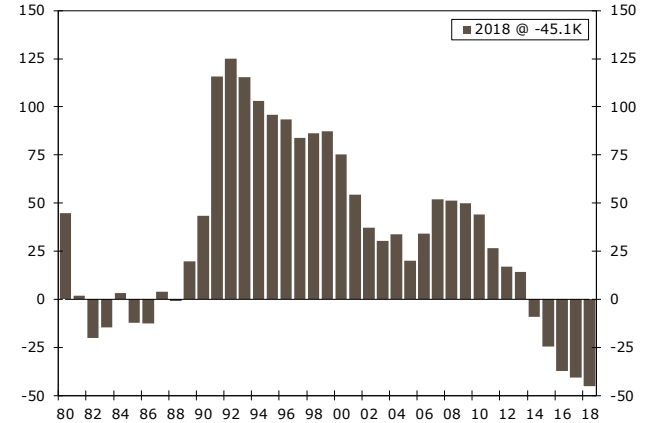
Real GDP Growth vs. U.S.



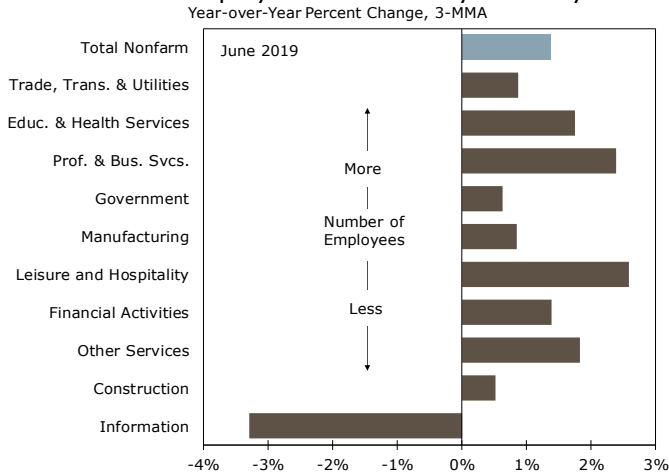
Nonfarm Employment



Illinois Population Growth
In Thousands



Illinois Employment Growth By Industry

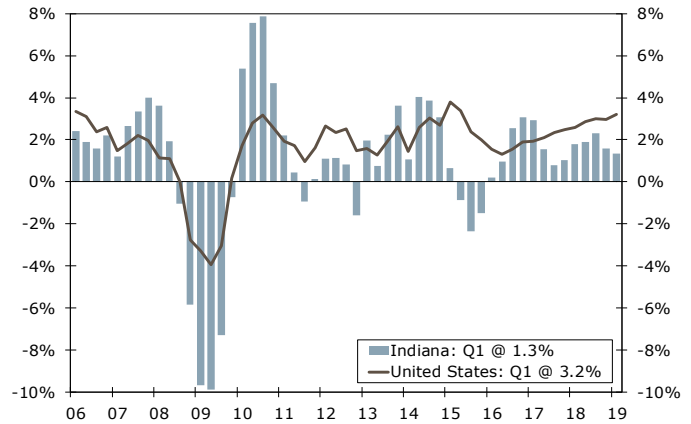


Source: U.S. Department of Labor, U.S. Department of Commerce and Wells Fargo Securities

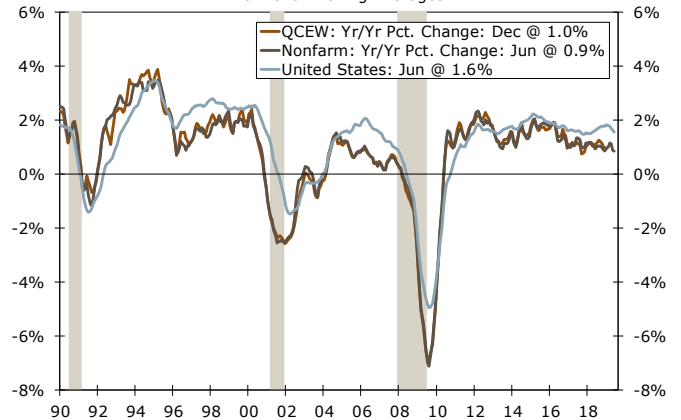
Indiana

- As one of the nation's most manufacturing-intensive states, Indiana remains susceptible to trade disputes, particularly threats of auto tariffs that would interfere with the extensive auto and RV supply chains across northern Indiana. Chemicals and pharmaceuticals are the second largest export category. Eli Lilly, the state's largest manufacturing employer, is headquartered in Indianapolis.
- Indiana's 1.3% Q1 real GDP growth trailed the national rate for the eighth consecutive quarter. The unemployment rate, however, is slightly lower than the U.S. rate. Payroll growth has steadily moderated since 2015, and now lags the nation's pace by almost a full percentage point.
- The state's economy is becoming more diverse. Indianapolis has benefited from the recent proliferation of tech jobs from firms seeking refuge away from the high costs of Silicon Valley into relatively more affordable secondary cities, as well as corporate migrations from Chicago. Salesforce operates a regional headquarters in downtown Indianapolis and Infosys plans to hire 3,000 workers by 2023 at its Technology and Innovation Hub there.
- FedEx is in the midst of a seven-year \$1.5 billion expansion at the Indianapolis International Airport, as it builds out its cargo capacity to accommodate surging e-commerce growth. Dubbed the "crossroads of America", Indiana has benefitted from its central location and seen strong growth in transportation & warehousing.

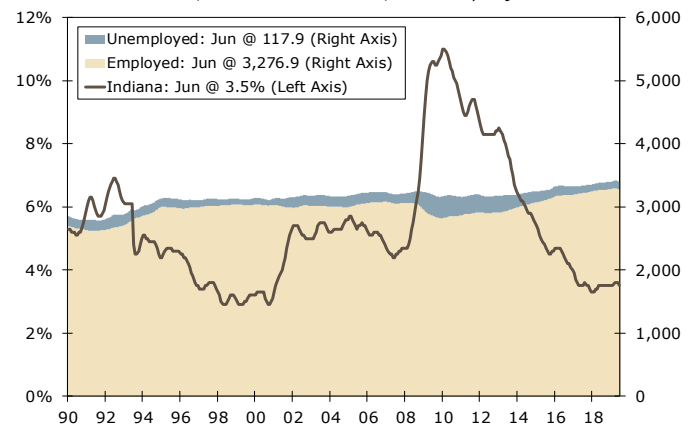
Real GDP Growth vs. U.S.
Year-over-Year Percent Change



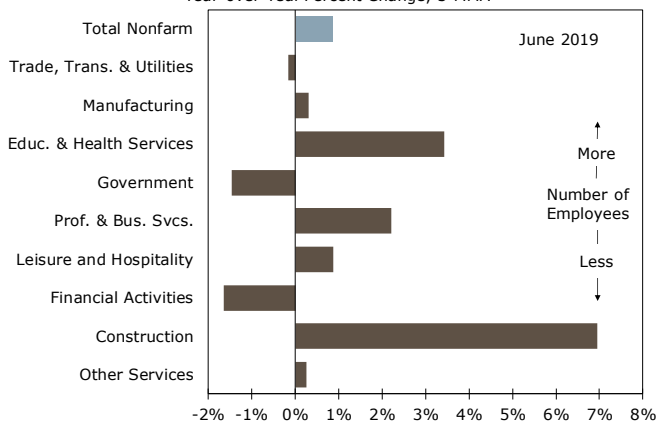
Indiana Nonfarm Employment
3-Month Moving Averages



Indiana Unemployment & Labor Force
Percent, Thousands of Workers, Seasonally Adjusted



Indiana Employment Growth By Industry
Year-over-Year Percent Change, 3-MMA

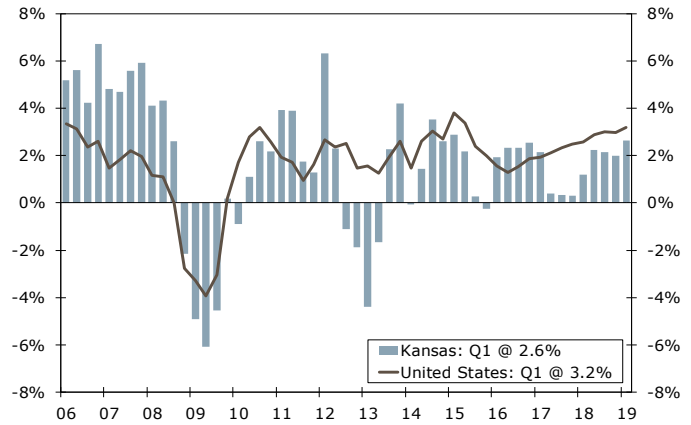


Source: U.S. Department of Labor, U.S. Department of Commerce and Wells Fargo Securities

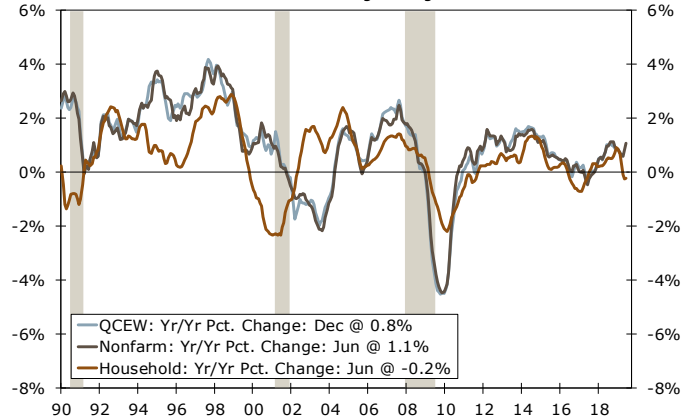
Kansas

- GDP and employment growth have both picked up nicely after dipping into near-contraction territory in 2017 due to a nationwide manufacturing slowdown and the tremendous uncertainty surrounding the state's finances. Earlier tax cuts were rolled back over the governor's veto in 2017, and economic growth and tax revenues have increased as uncertainty about tax policy has subsided.
- Kansas' heavy reliance on agriculture—the state is the nation's largest producer of sorghum and wheat—and aerospace underlies the need to further diversify its economy. Kansas remains susceptible to swings in the weather and global demand. Agriculture and related downstream industries support roughly 40% of the state's economy and over 125,000 jobs.
- Nicknamed “the Air Capital of the World”, Wichita has been challenged by the grounding of the Boeing 737 MAX. Spirit Aerosystems, which employs over 10,000 in the metro area, sells the vast majority of its output to Boeing and has been forced to reduce hours for most of its workforce. While manufacturing stalwart Boeing moved its operations to Oklahoma City and Seattle in 2014, Textron Aviation—the second largest employer in Wichita after Spirit—plans to add 1,000 workers this year.
- Fort Riley and McConnell Air Force Base provide stability, even amid some downsizing, while professional & business services help drive the transition to a more service-based economy.

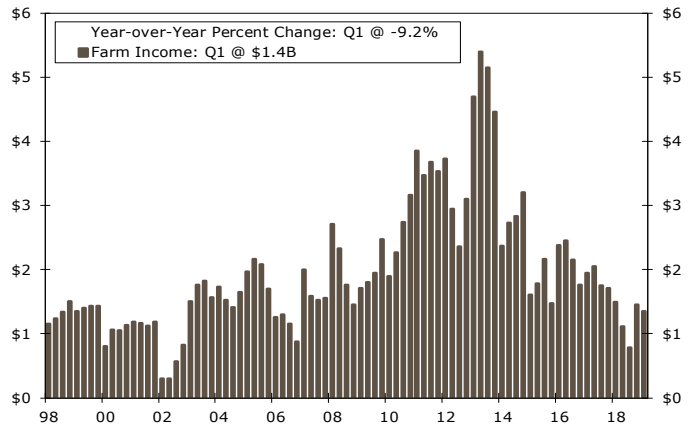
Real GDP Growth vs. U.S.
Year-over-Year Percent Change



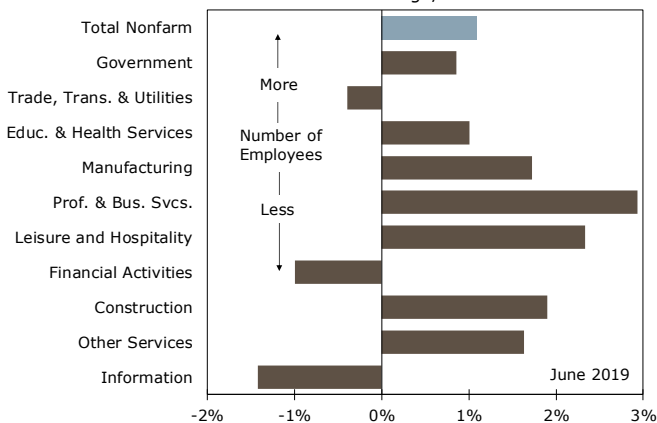
Kansas Nonfarm Employment
3-Month Moving Averages



Kansas Farm Income
Billions of Dollars



Kansas Employment Growth By Industry
Year-over-Year Percent Change, 3-MMA

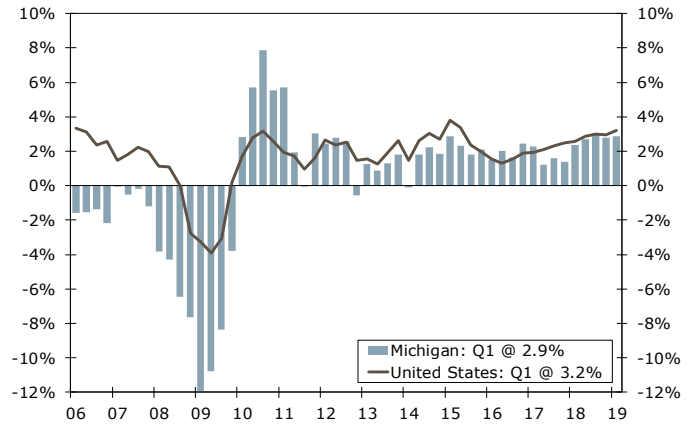


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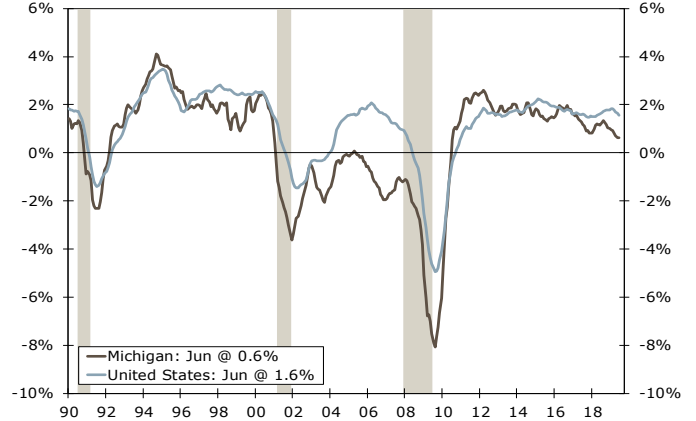
Michigan

- Michigan's resurgence has been largely tied to the revitalization of the auto sector, and growth has moderated as domestic vehicle sales have leveled off. Thousands of white collar job cuts by Ford and GM have taken some wind out of the modest rebound in the professional & business services sector, as well as the revival of downtown Detroit.
- Real GDP growth has kept pace with the nation the past four quarters, while the unemployment rate remains half a point above the U.S. rate at 4.2%.
- Michigan's strength lies in its deep talent pool in automotive engineering and production, and it remains the center of the industry's large supply chain. In recognition of this, and emblematic of the growing trend toward 'reshoring', Fiat Chrysler is set to expand production in Detroit for the first time in decades, investing \$4.5 billion and creating around 6,500 jobs. Ford is likewise positioning itself for the future by investing \$900 million and hiring 900 new workers in Flat Rock to work on electric cars and self-driving vehicles.
- The state's strong university system is another competitive advantage, with vibrant start-up scenes in Ann Arbor and Lansing attracting tech and biotech investment. In addition, Kalamazoo, home to Western Michigan University, recently secured a new Pfizer manufacturing plant that will employ 450 pharmaceutical workers.
- Solid international migration has kept overall population growth positive despite a median age above the nation and decades of persistent domestic out-migration.

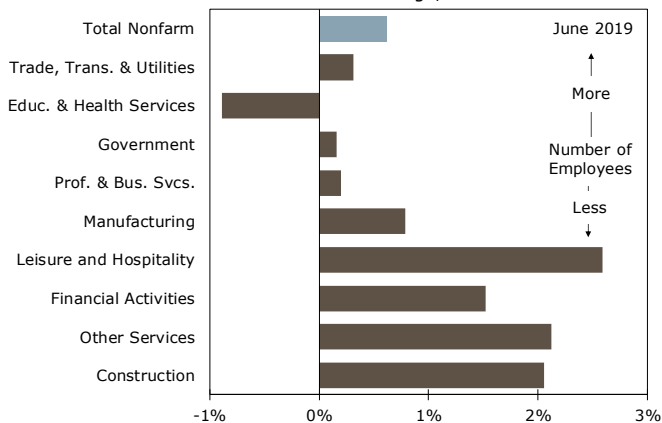
Real GDP Growth vs. U.S.
Year-over-Year Percent Change



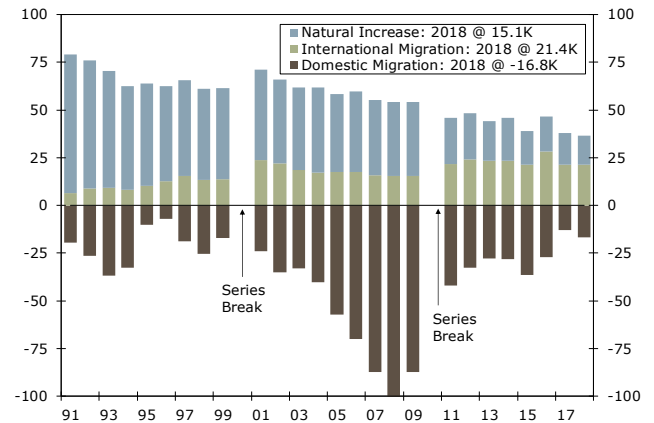
Nonfarm Employment Growth
Yr/Yr Pct. Change 3-Month Moving Averages



Michigan Employment Growth By Industry
Year-over-Year Percent Change, 3-MMA



Components of Population Change: Michigan
In Thousands

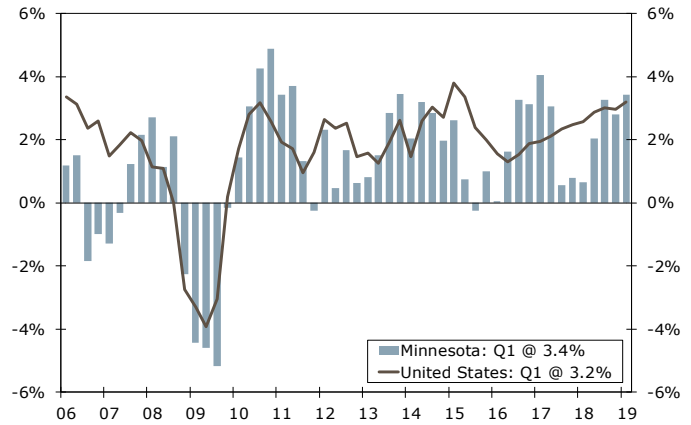


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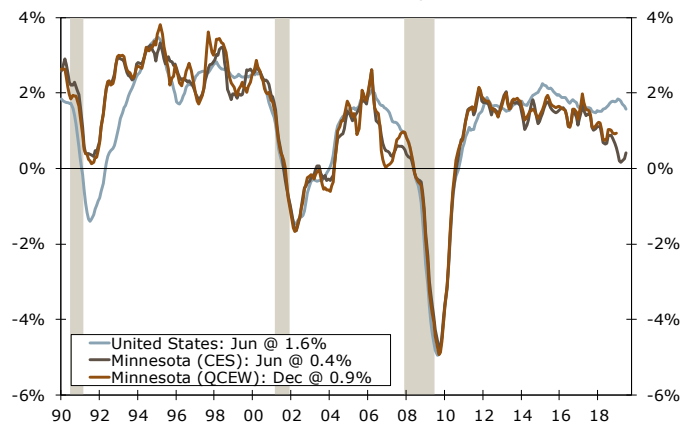
Minnesota

- Minnesota's payroll growth has slowed as it continues to struggle with a very tight labor market and skilled labor shortages. Yet the Gopher State has seen much stronger GDP growth relative to job growth, suggesting exceptionally high labor force participation has allowed Minnesotans to become 'more fully employed' and more productive. The shortage of skilled workers has also incentivized employers to invest more in training and upskilling their workforces.
- Manufacturing employment has struggled recently, while recent regulatory victories and higher commodity prices should boost the state's iron ore mining sector. Health services employment has surged, with much of the growth centered around the Mayo Clinic in Rochester.
- Like much of the Midwest, Minnesota has turned to international migration as a way to overcome sluggish labor force growth. Net domestic migration has also been positive the past two years, following 14 consecutive years of attrition. Stronger job growth is likely pulling jobseekers in.
- Employment growth in the Twin Cities—home to roughly 70% of the state's workforce—has slowed towards zero and dipped into negative territory the past two months, while the unemployment rate has ticked up to 3% from 2.5% one year ago.
- In December 2018, Minneapolis became the first city in the U.S. to ban single-family zoning in an attempt to spur more multifamily development in growing areas and drive down housing costs, as part of its strategic 'Minneapolis 2040' plan. Portland, Oregon has since followed suit.

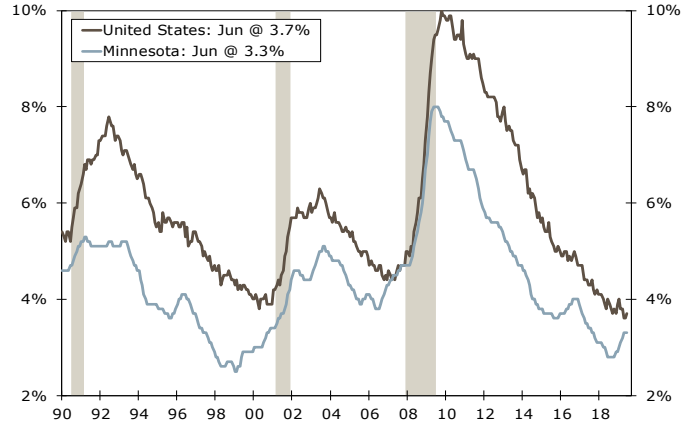
Real GDP Growth vs. U.S.
Year-over-Year Percent Change



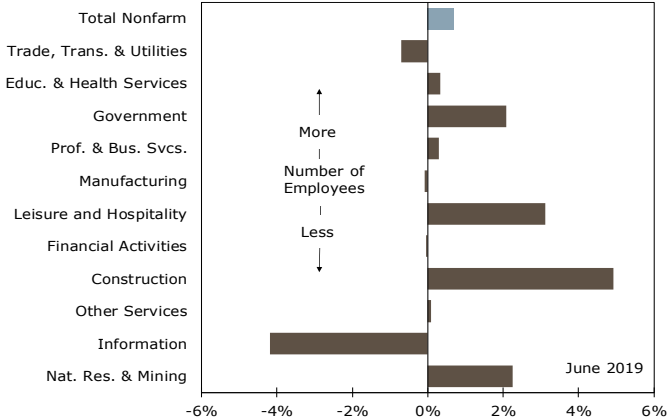
Nonfarm Job Growth: U.S. vs. Minnesota
Year-over-Year Percent Change, 3-MMA



Minnesota vs. U.S. Unemployment Rate
Seasonally Adjusted



Minnesota Employment Growth By Industry
Year-over-Year Percent Change, 3-MMA

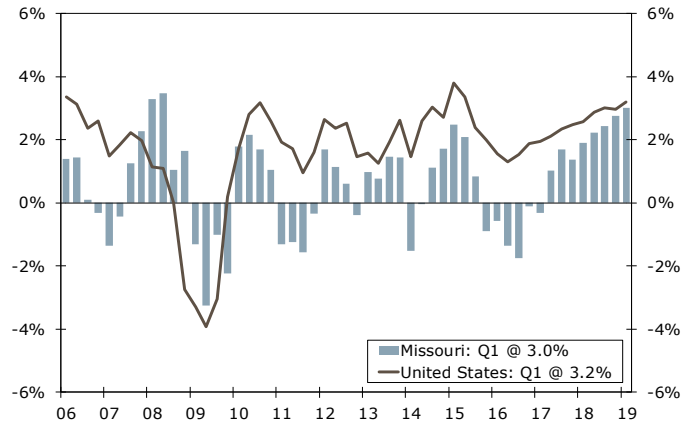


Source: U.S. Department of Labor, U.S. Department of Commerce and Wells Fargo Securities

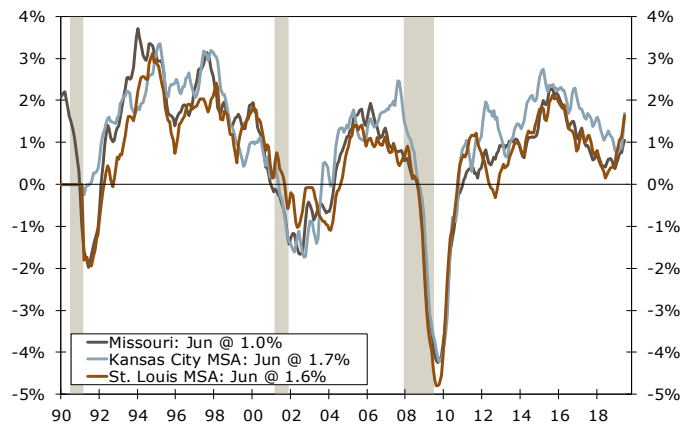
Missouri

- Missouri's real GDP growth has accelerated for five consecutive quarters on a year-over-year basis, driven primarily by growth in the Kansas City and St. Louis metro areas, which bookend the state, connected by I-70.
- Long home to significant agricultural and food manufacturing operations, the state has worked to foster a dynamic AgTech sector through accommodative corporate income tax rates, subsidies and the placement of graduates from the state's large leading universities.
- St. Louis has emerged as somewhat of a late-cycle tech hotspot, attracting firms with its low costs and talent pool. Square recently announced plans to double its workforce there and establish its largest presence outside of the Bay Area. Nestle also moved its IT operations from California to the Gateway City.
- The presence of 10 Fortune 500 headquarters as well as its central geographic location provide Missouri a solid base of relatively high-paying jobs and a strong link to the rapidly growing transportation, distribution and logistics sectors.
- Harley-Davidson closed its Kansas City manufacturing plant this year, but the factory sector across the state has otherwise been strong, with payrolls rising around 2% over the past year.
- Research & development investment is also on the rise in the state, as Pfizer announced plans to invest more than \$200 million for a new plant in Chesterfield, on the western edge of St. Louis.

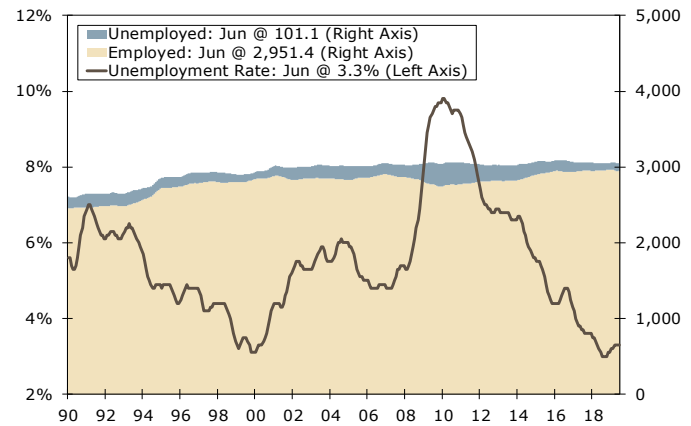
Real GDP Growth vs. U.S.
Year-over-Year Percent Change



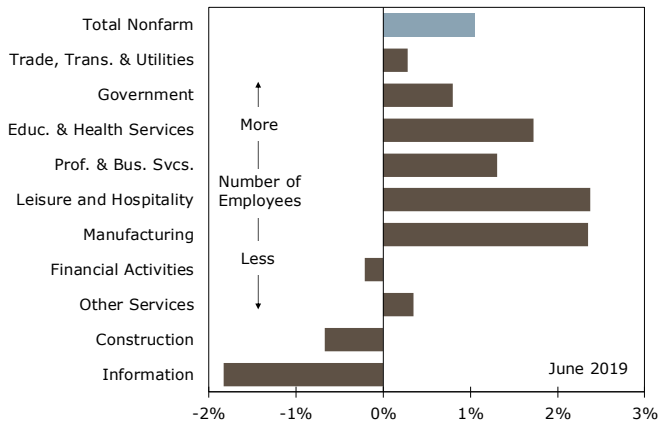
Missouri Nonfarm Employment
3-Month Moving Averages



Missouri Unemployment & Labor Force
Percent, Thousands of Workers, Seasonally Adjusted



Missouri Employment Growth By Industry
Year-over-Year Percent Change, 3-MMA

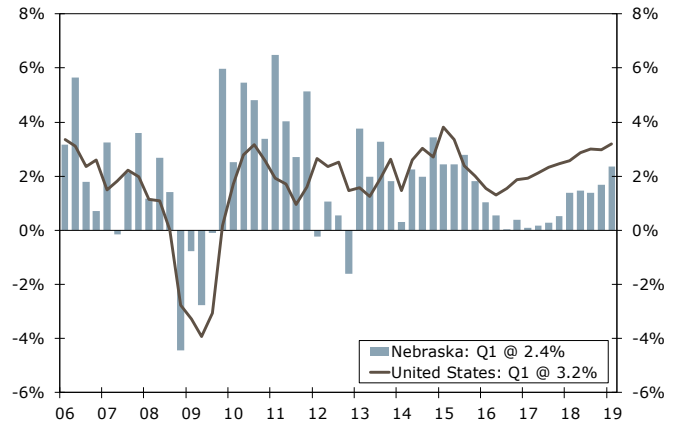


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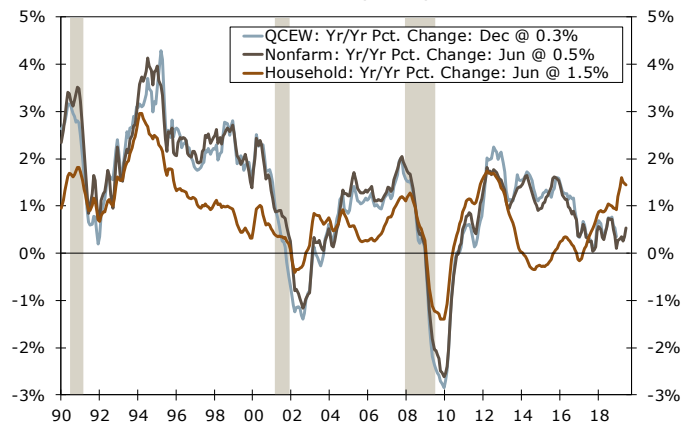
Nebraska

- Real GDP growth picked up again in the first quarter to a 2.4% year-over-year pace, marking an acceleration over the full-year 2018 growth of 1.5%, but still lagging the nation's growth.
- Severe and widespread flooding in March caused more than \$1 billion of damages, including \$449 million in damages to infrastructure, \$440 million in crop losses and \$400 million in cattle losses. Storms struck again in May and prompted the state's second disaster declaration of the year. The recovery has been slow, as is often the case with floods.
- Livestock is the dominant agricultural product, along with sizable corn, soybean and sorghum harvests. Agriculture-related manufacturing has also been a force in the state, with Conagra Foods and Caterpillar maintaining facilities in the Omaha region. But trade frictions are a major hurdle to stronger growth.
- Omaha—home to almost 40% of the state's workforce and five Fortune 500 headquarters—continues to benefit from rural-urban migration and a proliferation of finance and insurance companies attracted to the low cost of doing business. Professional & business services and financial activities are the fastest growing sectors across the state, and added 2,000 and 1,000 jobs, respectively, over the past year.
- The presence of Mutual of Omaha, Conagra and Berkshire Hathaway in Omaha provides a nice diversifying counterbalance for the otherwise agriculturally dominated state.

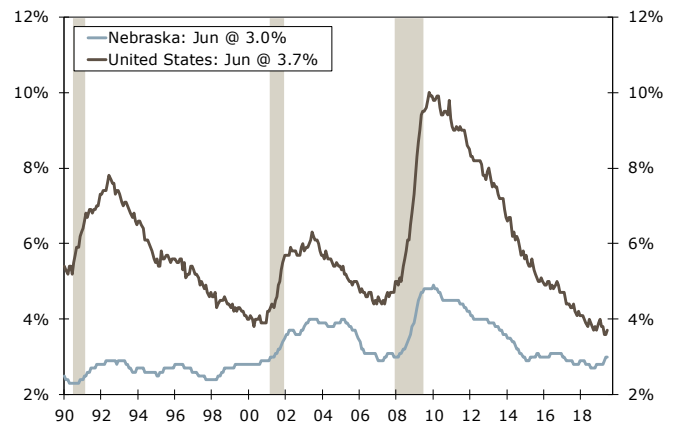
Real GDP Growth vs. U.S.
Year-over-Year Percent Change



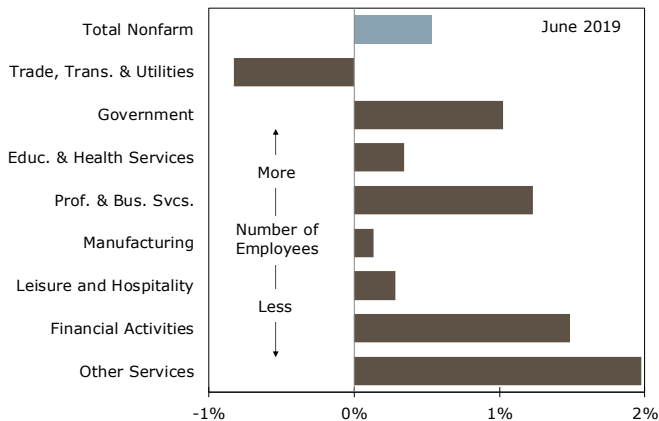
Nebraska Nonfarm Employment
3-Month Moving Averages



Nebraska vs. U.S. Unemployment Rate
Seasonally Adjusted



Nebraska Employment Growth By Industry
Year-over-Year Percent Change, 3-MMA

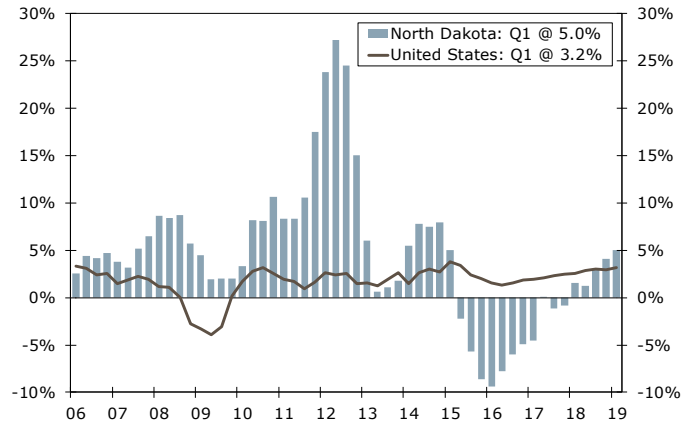


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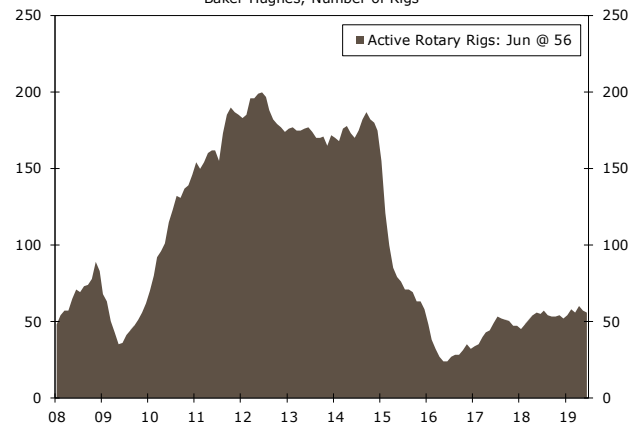
North Dakota

- North Dakota has finally emerged from its energy-related recession, but growth remains modest. One of the most energy-dependent states in the nation, the days of incredible growth following the initial development of the Bakken Shale play are now a thing of the past.
- The rig count has rebounded as oil prices have shored up but remains well below its prior peak. Moreover, the energy industry has learned to become significantly more efficient, which means production has rebounded much more than employment. Bottlenecks in the Permian—which has been the major shale hotspot the past few years—may have boosted the recovery in the Bakken. The surge in construction payrolls is likely due to a buildout of drilling facilities and increased pipeline capacity.
- Renewables are also on the rise. North Dakota ranks in the top-10 for installed wind capacity.
- North Dakota’s 2.3% unemployment rate is the second lowest in the nation. Labor shortages are particularly acute in energy-related occupations like construction and truck driving.
- In contrast to the Midwest as a whole, North Dakota’s median age *fell* this past year to 35.2 from 37, likely due to an influx of young males attracted to job openings across the energy sector and related support operations.
- Fargo is home to one third of the state’s population and most of the state’s service and knowledge-based jobs. The very low costs have attracted financial firms’ back office operations.

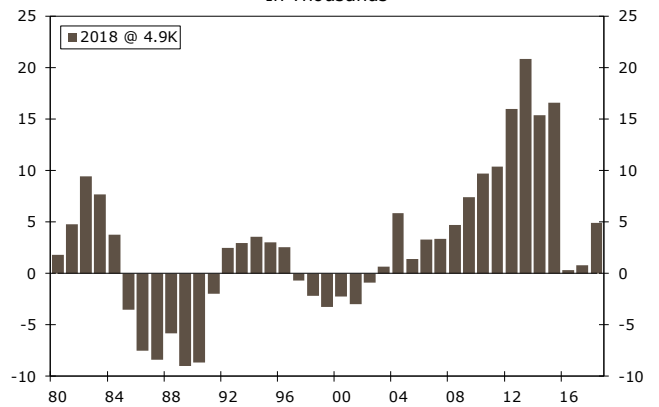
Real GDP Growth vs. U.S.
Year-over-Year Percent Change



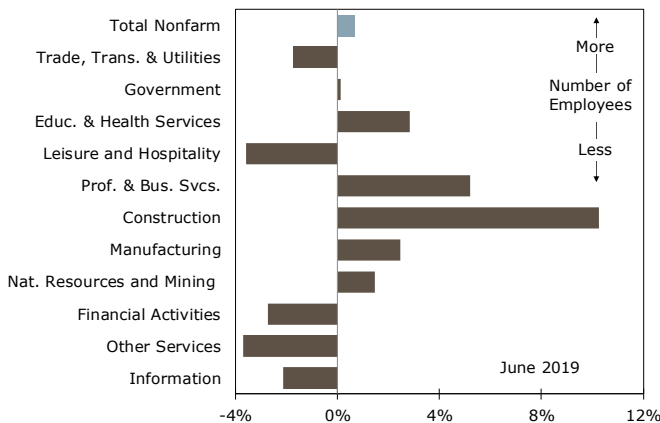
Active Rotary Rigs in North Dakota
Baker Hughes, Number of Rigs



North Dakota Population Growth
In Thousands



North Dakota Employment Growth By Industry
Year-over-Year Percent Change, 3-MMA

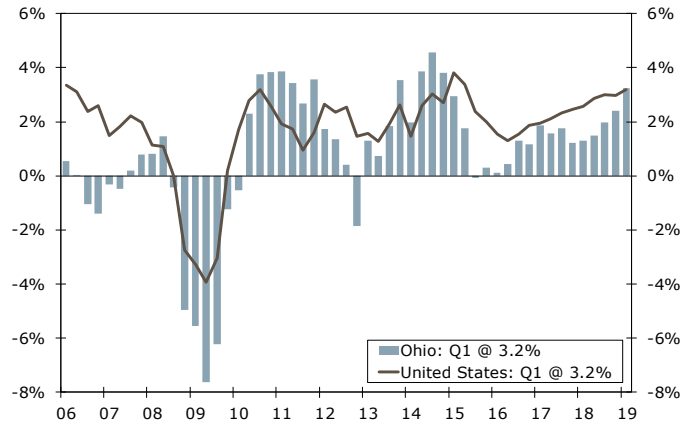


Source: U.S. Department of Labor, U.S. Department of Commerce and Wells Fargo Securities

Ohio

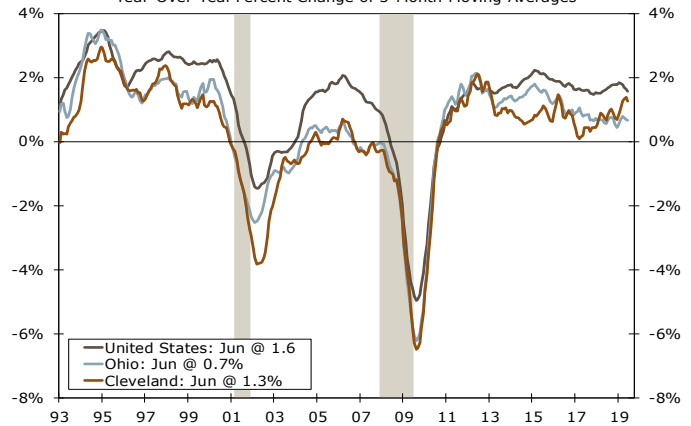
- A rain-delayed planting season for corn and soybeans in the western portion of the state along with the ripple effects from steel and aluminum tariffs (and the lingering threat of auto tariffs) are casting a shadow over the goods-producing areas of this diverse state.
- Ohio's largest metros are growing rapidly, led by a resurgence in downtown Cleveland and strong tech-related job growth in Columbus. A majority of the population lives in the 'three Cs'—the third of which is Cincinnati—that lie along I-71. These metros are generally younger, more diversified and growing faster than the state.
- The state's midsize metros and much of the eastern part of the state recovered more slowly from the last recession and continue to grapple with the secular decline in manufacturing jobs. GM is closing multiple plants across Ohio, and will lay off more than 1,500 workers at its Lordstown Chevy Cruze plant. Diversification and reskilling are crucial for the growth outlook of Youngstown, Toledo and Dayton.
- A resurgent energy sector and booming natural gas extraction from the Marcellus Shale in eastern Ohio have improved prospects for many otherwise struggling areas. Perhaps even more promising is the Utica Shale play, which lies beneath the Marcellus and is more geographically extensive. This massive untapped energy source presents a major industrial investment opportunity for a region that could use a boost.

Real GDP Growth vs. U.S.
Year-over-Year Percent Change



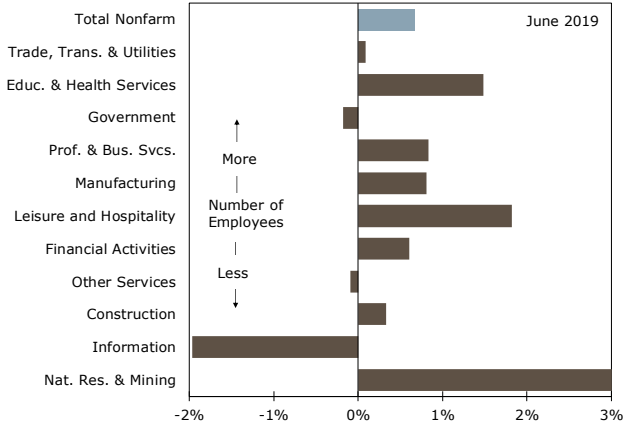
Nonfarm Employment

Year-Over-Year Percent Change of 3-Month Moving Averages

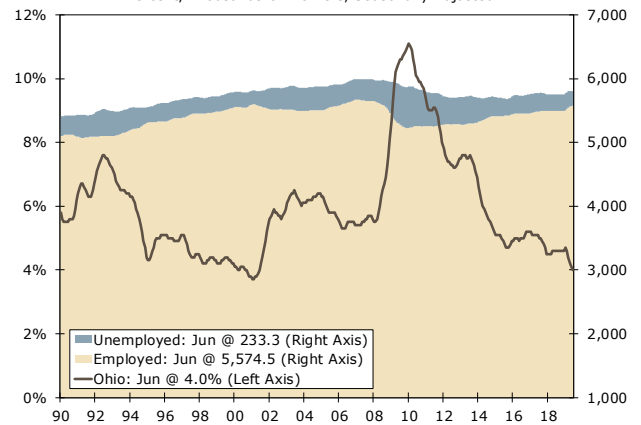


Ohio Employment Growth By Industry

Year-over-Year Percent Change, 3-MMA



Ohio Unemployment & Labor Force
Percent, Thousands of Workers, Seasonally Adjusted

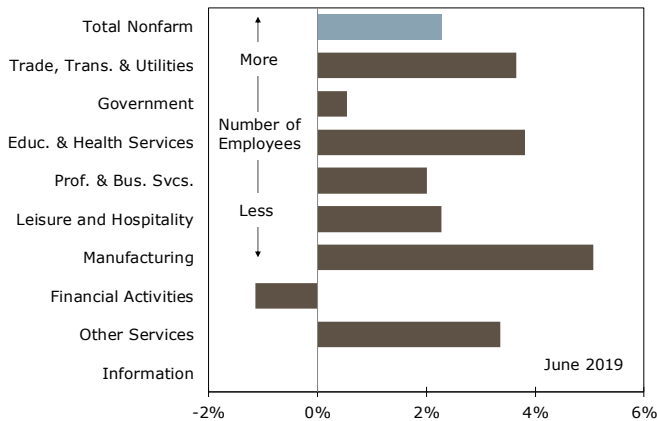


Source: U.S. Department of Labor, U.S. Department of Commerce and Wells Fargo Securities

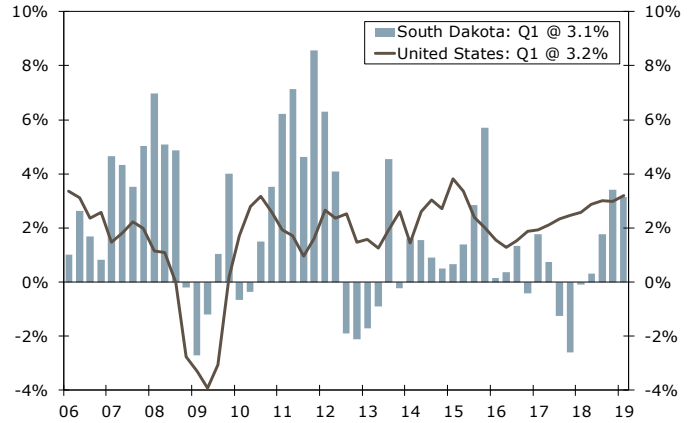
South Dakota

- South Dakota was hit hard by the flooding this past spring, which did not help its already struggling agricultural sector. Damage to the state's infrastructure—critical for its farmers—will likely prolong the recovery.
- Despite these challenges, nonfarm payrolls have accelerated nearly every month for the past two years, and are now rising at the fastest pace in more than a decade. Manufacturing payrolls—roughly 70% of which are in durable goods—are up more than 4% year-over-year. The state's low cost environment, along with the lack of any corporate or individual income tax, should continue to attract businesses, although the lack of a critical mass of young, skilled workers may limit the pace of the state's economic diversification into more dynamic industries.
- The 46th largest state by population, South Dakota grew faster than the nation in 2018—despite an older population—due to a strong influx from abroad and rapid growth in Sioux Falls, home to 30% of the state's population.
- The state's vast open spaces have facilitated the extensive development of renewable wind energy, a nice complement to the 15 ethanol producing plants that are responsible for 7% of nation's output. The scenic Black Hills in the western portion of the state, home to Mount Rushmore and the gargantuan, yet-to-be-completed Crazy Horse monument, attract a growing number of visitors, and support an array of leisure & hospitality jobs in Rapid City.

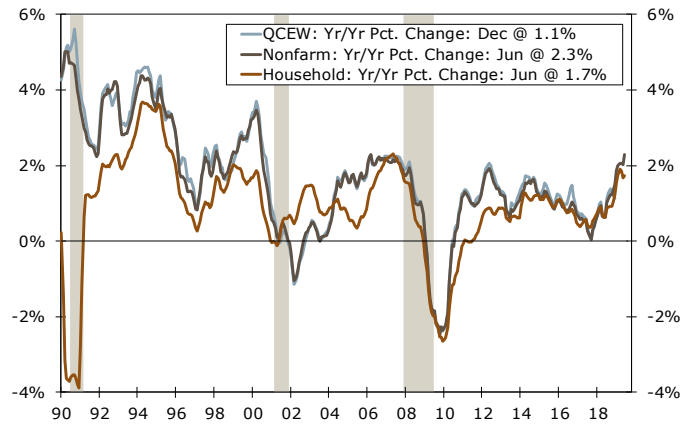
South Dakota Employment Growth By Industry
Year-over-Year Percent Change, 3-MMA



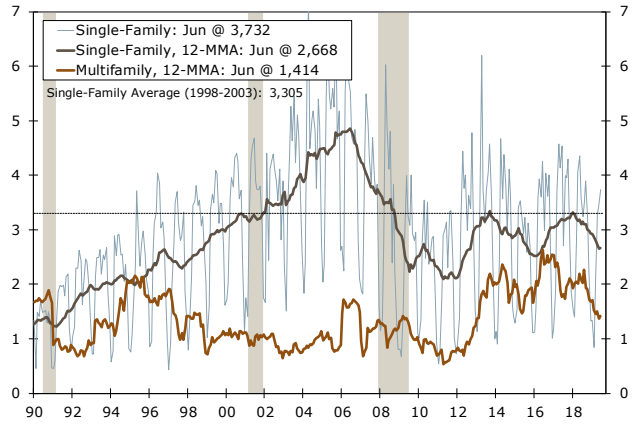
Real GDP Growth vs. U.S.
Year-over-Year Percent Change



South Dakota Nonfarm Employment
3-Month Moving Averages



South Dakota Housing Permits
Thousands of Permits, Seasonally Adjusted Annual Rate

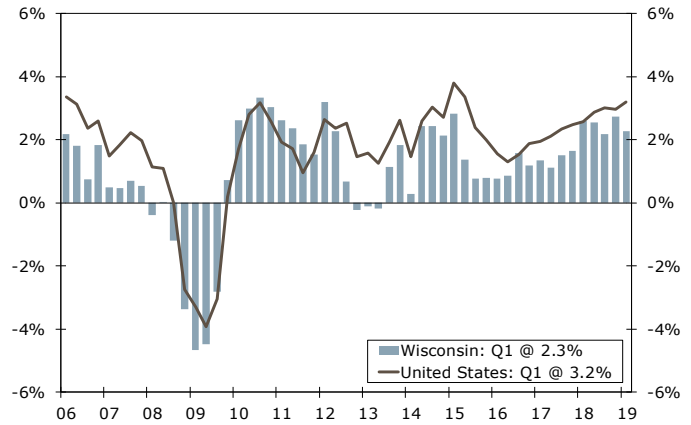


Source: U.S. Department of Labor, U.S. Department of Commerce and Wells Fargo Securities

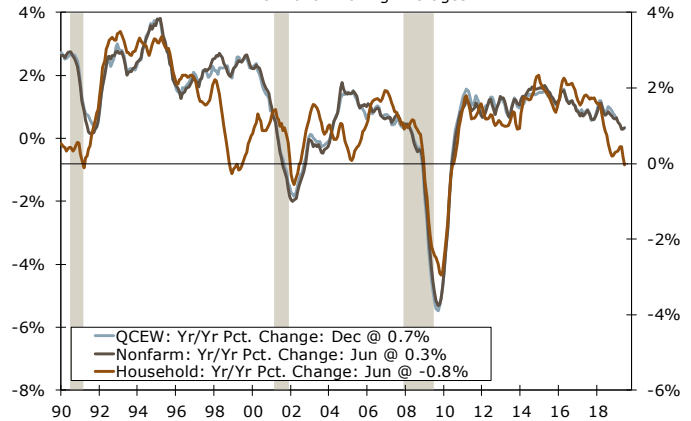
Wisconsin

- Wisconsin's GDP grew 2.5% in 2018, outpacing the Midwest but trailing the national average. Nonfarm employment growth has slowed amidst limited labor force growth and increasingly challenging demographics. The unemployment has held below 3% since January 2018.
- Home to the most dairy farms in the nation, Wisconsin was hit hard by retaliatory dairy tariffs imposed by Mexico that were effective July 2018 through May 2019. The tax, in addition to the nearly 40% decline in milk prices over the past five years, has pushed more than 1,000 dairy farms into bankruptcy in the past couple of years.
- Manufacturing, which comprises 16% of employment across the Badger State (well above the national average) has recovered only 63% of the jobs lost in the last recession.
- Foxconn's much-heralded manufacturing plant in Mount Pleasant, outside of Milwaukee, has come under much closer scrutiny after it became clear the Taiwanese company will fall short of the 13,000 jobs it initially planned to create. Negotiations with the statehouse in Madison are ongoing, but the realized investment will almost certainly be less than initially expected given slower global growth.
- Madison has become a hotbed for venture capital investment, attracted to innovations in biotechnology, chemistry and computer science emanating from the University of Wisconsin. Attracting young persons remains key.

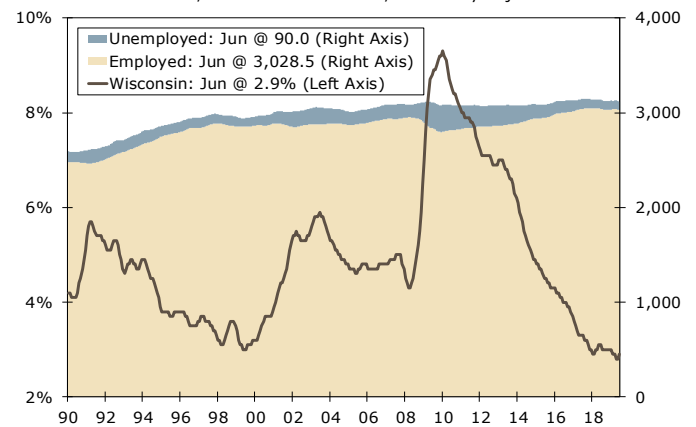
Real GDP Growth vs. U.S.
Year-over-Year Percent Change



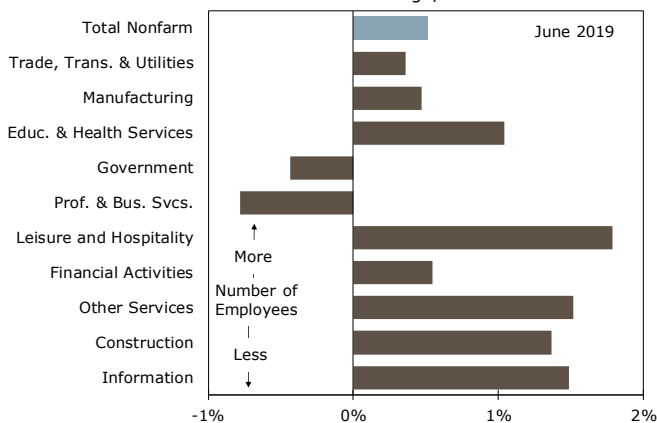
Wisconsin Nonfarm Employment
3-Month Moving Averages



Wisconsin Unemployment & Labor Force
Percent, Thousands of Workers, Seasonally Adjusted



Wisconsin Employment Growth By Industry
Year-over-Year Percent Change, 3-MMA



Source: U.S. Department of Labor, U.S. Department of Commerce and Wells Fargo Securities

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