

# **Small Improvements And Challenges Are Expected In The Coming Year**

Business services firms expect minor improvement in revenue, profits, productivity and employment in the coming year. Labor availability is expected to increase slightly, but supply of workers will continue to exert upward pressure on wages. Inflation is predicted to increase as well.

These results come from a random sample of Minnesota businesses service firms conducted in May and June 2024, by the Minnesota Department of Employment and Economic Development and the Federal Reserve Bank in Minneapolis.

**Business Services Firms: Previous Year**
Minnesota business services firms faced varied economic conditions. The diffusion indexes for revenue (57) and productivity (54) remained nearly unchanged from the previous year, indicating expansion and stable conditions. The employment level index rose slightly to 52, suggesting modest growth compared to the contraction indicated by the previous year's index of 48. Labor availability showed an index of 41, still in contraction territory but improved from 32 the year before.

The input cost index increased to 86 from 80, pointing to higher inflation (Chart 1 or Table 1-A).

\* Above 50 indicates expansion, below 50, contraction.

**Business Services Firms: The Coming Year**
Minnesota business services firms are cautiously optimistic about the upcoming four quarters, expecting modest growth in revenue, profits, productivity, and employment shown by diffusion indexes. Although the diffusion index for labor availability remains in contraction at 46, this marks an improvement from the previous year's index of 41. However, this improvement comes at a cost: 58% of respondents anticipate raising wages at least 3% to attract workers. Input costs remain a concern, reflected by a diffusion index of 80 (Chart 2 or Table 1-B).

\* Above 50 indicates expansion, below 50, contraction.

**Outlook On The State Economy: Next Year** Minnesota business services firms hold a pessimistic outlook for the overall economy in the coming year. The diffusion index for consumer spending has declined to 37 from 40, indicating further contraction. Similarly, the diffusion index for corporate profits has dropped to 40 from 45, reflecting diminishing profitability. While respondents expect inflation to rise, the diffusion index of 73, down from 79 the previous year, indicates cautious optimism about slowing price increases (Table 1-C).

A question about credit conditions revealed that businesses experienced a slight deterioration compared to the previous year. Approximately 40% reported higher interest rates, up from 35% the year before. Twelve percent indicated difficulties accessing capital, compared to 9% previously, and 18% experienced a decrease in hiring, compared to 11% the prior year (Table 1-D).

**Table 1: Minnesota 2024 Business Services Firms Condition Survey Results1**

| 1. **Business indicators in the last year**
 | **Up** | **Same** | **Down** | **Diffusion index 2024(2)** | **Diffusion index 2023(2)** |
| --- | --- | --- | --- | --- | --- |
| Sales revenue | 46% | 21% | 34% | 57 | 57 |
| Profits | 36% | 24% | 41% | 48 | 49 |
| Productivity | 29% | 49% | 21% | 54 | 55 |
| Employment level | 26% | 51% | 23% | 52 | 48 |
| Labor availability | 12% | 58% | 30% | 41 | 32 |
| Selling prices | 53% | 38% | 9% | 72 | 70 |
| Input costs | 73% | 25% | 2% | 86 | 80 |
| Space occupied (square footage)Exports (sales for foreign clients) | 9%2% | 81%85% | 10%13% | 5045 | 5050 |

| Labor indicators last 4 year | Decrease | 0% | 1-2% | 3-5% | 6-9% | >10% |
| --- | --- | --- | --- | --- | --- | --- |
| Wages per worker | 9% | 9% | 7% | 45% | 20% | 10% |
| Benefits per worker | 5% | 23% | 8% | 30% | 19% | 15% |

| 1. Expected business indicators during next year
 | Up | Same | Down | Diffusion index 2024(2) | Diffusion index 2023(2) |
| --- | --- | --- | --- | --- | --- |
| Sales revenue | 45% | 33% | 22% | 62 | 58 |
| Profits | 36% | 33% | 31% | 53 | 50 |
| Productivity | 29% | 61% | 10% | 60 | 56 |
| Employment level | 30% | 54% | 16% | 57 | 52 |
| Labor availability | 12% | 67% | 21% | 46 | 41 |
| Selling pricesInput costs | 40%60% | 54%39% | 6%2% | 6780 | 6676 |
| Space occupied (square footage) | 10% | 83% | 7% | 52 | 49 |
| Exports (sales for foreign clients) | 8% | 85% | 7% | 51 | 50 |

| Expected labor indicators during next year | Decrease | 0% | 1-2% | 3-5% | 6-9% | >10% |
| --- | --- | --- | --- | --- | --- | --- |
| Wages per worker | 7% | 13% | 16% | 45% | 13% | 7% |
| Benefits per worker | 3% | 25% | 19% | 29% | 17% | 8% |

| 1. Outlook on the following state economic indicators during the next year
 | Up | Same | Down | Diffusion index 2024(2) | Diffusion index 2023(2) |
| --- | --- | --- | --- | --- | --- |
| Employment | 24% | 56% | 20% | 52 | 52 |
| Consumer spending | 14% | 46% | 40% | 37 | 40 |
| Inflation | 56% | 34% | 10% | 73 | 79 |
| Corporate profits | 21% | 38% | 41% | 40 | 45 |
| Mergers and acquisitions | 30% | 54% | 16% | 57 | 60 |

| 1. Have changes in

in credit conditionsin the last 4 quartersaffected your firm? | Higher Interest rates | No Changes | Increased Hiring | IncreasedCapital Expenditures | DecreasedHiring | Decreased Capital Expend. | NoDiff.accessing credit | Difficultiesaccessing credit |
| --- | --- | --- | --- | --- | --- | --- | --- | --- |
| Percent | 39% | 44% | 7% | 8% | 18% | 19% | 19% | 12% |

(1) Based on responses from 193 Minnesota business service firms. From those, 141 were usable surveys for an adjusted response rate of 12%.
Percentages might not add to 100% due to rounding.
(2) A diffusion index greater than 50 indicates expansion, lower than 50 indicates contraction.
Prepared by the Economic Analysis Unit, Minnesota Department of Employment and Economic Development, July 2024.

The survey also explored the impact of AI. Over 30% of respondents anticipated a slightly positive effect, while 23% foresaw no impact. Merely 4% believed it would have a very positive impact. Respondents that indicated “Other” commented that “it needs to be heavily policed” and that they “believe it to be significant, some negative and some positive.” Table 2.

**Table 2. Expected Impact of AI On Businesses**

|  |  |
| --- | --- |
| **Expected impact** | **Percent** |
| Very positive impact | 4%  |
| Slightly positive impact | 33%  |
| No impact | 23%  |
| Neutral impact | 21%  |
| Slightly negative impact | 9%  |
| Very negative impact | 7%  |
| Other | 4%  |

Note: Based on 141 usable surveys.

Participants were also asked about changes in office space. Sixty-five percent of respondents indicated they did not reduce space in the past 12 months while 60% specified they won’t in the next 12 months. Respondents that indicated “Other” commented they “have always been hybrid” and that they are ”remodeling existing space.” (Table 3).

**Table 3. Changes in Office Space**

|  |  |  |
| --- | --- | --- |
| **Office Space** | **Past 12\* months** | **Coming 12\* months** |
| Not reducing space | 65% | 60%  |
| Rent is too expensive | 19%  | 20%  |
| Permanent reduction in staff | 14%  | 15%  |
| Permanent shift to hybrid/remote work | 23%  | 20%  |
| Moving to a smaller space | 4% | 8%  |
| Moving to a lower rent space | 1%  | 9%  |
| Moving to a more desirable space/location | 4%  | 9% |
| Other | 4%  | 5% |

Note: Based on 141 usable surveys.
\*Percentages do not add to 100% due to multiple choice selections.

**Business Ownership**Only 3% of respondents identified themselves as veterans while 10% as minorities and 21% as women.

|  |  |
| --- | --- |
| **Ownership** | **Percent\*** |
| None of the above | 61% |
| Woman-owned | 21% |
| Minority-owned | 10% |
| Prefer not to answer | 10% |
| Veteran-owned | 3% |

Note: Based on 141 usable surveys.
\*Percentages do not add to 100% due to multiple choice selections.

Respondents were asked to provide additional comments. They indicated concerns with the economic impact of inflation, labor availability and cost. Examples of comments are provided below:

Inflation

* *“Inflation [is] causing reductions in project approvals.”*
* *“This economy is a vicious circle. Costs of everything continues to rise causing us to need to raise wages so employees are not going backwards. In turn our prices must go up and then our customers and so on. Interest rates have certainly had a big impact on our business as well.”*
* *“All costs of operation are increasing due to inflation, but our revenue/profit is decreasing, which is related to pressure (downward) in the marketing/advertising industry. We will experience layoffs in the next 12 months unless conditions improve.”*

 *Labor Availability*

* *“Demand remains very relevant. Our largest hinderance to growth will be finding qualified employees.”*