

TEN

FEDERAL RESERVE BANK OF KANSAS CITY

Winter 2013



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**New person-to-person payments
advance in the U.S.**

**Community banks remain
relevant in today's market**

Where job and life converge

BRICK BY BRICK

Banking land for urban revitalization



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Can Community Banks Still Compete?

Community banks are an important part of the Federal Reserve Bank of Kansas City's regional economy, and we have significant supervisory responsibilities for those banks and their holding companies. Certainly, we recognize the challenges facing community banks today. In fact, some have questioned whether community banks will be able to effectively compete going forward. Others remain optimistic and continue to see opportunities for the community bank model.

Without question, the recent financial crisis and slow economic recovery are now focusing much attention on the banking industry and its regulatory framework. In particular, the Dodd-Frank Act and the proposed Basel III capital rules are bringing major changes to the regulatory structure. These include the new Financial Stability Oversight Council and Consumer Financial Protection Bureau, enhanced supervision and orderly liquidation authority for systemically important organizations, a new regulatory regime for the capital markets and financial infrastructure, and higher and more complex capital requirements.

Understandably, we often hear from community bankers that they do not expect this changing environment to work well for them. These bankers anticipate being hit with significant regulatory costs for a crisis that originated in other parts of the financial system. I have similar concerns about the current direction of regulatory policy and how it may negatively affect the ability of community banks to be competitive and serve the credit needs of their communities. Today I will discuss my concerns and the importance of ensuring a more equitable landscape for community banks.

Past challenges

I should begin by acknowledging that community bankers are no strangers to a challenging operating environment. Over the past few decades, community banks have encountered many challenges and developments that were often thought to favor larger institutions and threaten the future of community banks. Some of you here today experienced those challenges.

When I started at the Federal Reserve in 1982, bank expansion laws were viewed as a serious threat. In many parts of the Tenth District, we still had a unit banking structure in which banks could only operate out of a single office or perhaps with a few additional limited-service facilities. Several District states also did not allow multibank holding companies, and interstate banking was nonexistent outside of a few special exceptions.

When efforts were begun to relax these expansion restrictions, a common assertion was that larger, expansion-minded institutions would invade community bank markets and steal their business. We often heard that "multibank holding companies would be the death of the community bank." As it happened, the liberalization of bank expansion laws still left many community banks in operation, albeit with some reduction in their numbers and overall share of industry assets. Many well-managed community banks have been able to capitalize on this new expansion framework by making acquisitions of their own and spreading



their skills over a larger base of operations. In fact, about 60 percent of bank mergers since 1985 have involved one community banking organization acquiring another one.

Similarly, when deposit interest rate ceilings were removed in the 1980s, community bankers were concerned that larger banks would be able and willing to pay more for deposits than community banks—an outcome many claimed would pull deposits out of community banks and destroy their net interest margins. Technological change was also thought to favor large banks because they had the resources to be on the cutting edge of such developments as ATM networks, online banking, automation of banking operations, new financial instruments and risk-management models. Finally, community banks have seen certain lending and product markets shift to larger institutions, captive finance companies, credit unions and the capital markets. Among these shifts have been credit card lending, auto loans, equipment lending and the dominant role community banks once had as the principal repository for their customers' savings.

In all of these cases, community banks have established an innovative track record, whether it is an increased ability to manage funding needs by paying competitive deposit rates, develop their own expertise in technology and find vendors to provide other services, or discover new services to provide to customers. To be sure, the community bank business model has proven resilient and able to withstand significant challenges when boards of directors and their management teams demand strong

performance and are willing to be flexible and ready to capitalize on new opportunities.

How community banks survived

Understanding how community banks successfully overcame these challenges is important, especially as we consider the direction of today's financial reforms. I'd like to highlight a couple of studies we've done to analyze this.

First, community banks generally operate with the right incentives and an effective corporate governance structure. Many community banks are closely held institutions with the top management and board members having significant ownership positions. These ownership incentives help to ensure that key policymakers are committed to achieving good performance, have enough at stake to avoid excessive risk-taking, and also have a vested interest in the health of their communities. This is well-understood by community bankers, and it stands in sharp contrast to some of the governance problems apparent at larger banks, especially during the crisis. Few outside of the community banking sector, though, fully understand the significance and implications of this governance structure.

The staff of the Federal Reserve Bank of Kansas City has conducted several studies on the ownership and management structure of community banks. We found that the better performing and safer community banks are those where the major policymakers have much to lose if they do not make the right decisions. This conclusion is significant when we consider

how community banks should be supervised compared to larger banking organizations.

Another commonly noted strength of community banks is that they have close relationships with and detailed knowledge of their customers. As a general practice, community banks do not make “cookie-cutter” loans and do not offer the same standardized products as larger banks, but instead tailor their services to the needs of their customers.

While many now claim that the value of customer relationships is declining with credit scoring and credit risk models, a recent study at our Bank found that there is real value in relationship lending and in the soft personal information on customers that community bankers typically have.

This study looked at a large sample of Small Business Administration loans made by community banks to new businesses and to other businesses with blemished credit records. Given the inherent risk in such loans, one might expect that having a good personal knowledge of these customers would be useful. Not surprisingly, the study found that default rates on these loans were indeed lower when the lending was to businesses located in the same market as the bank. Defaults were higher when the borrowers were in a different market where the bank would not be expected to have the same type of close personal relationships with these borrowers.

Furthermore, the lowest default rates were in smaller communities where local bankers typically have lifelong knowledge of their customers and the closest personal

relationships. This research suggests that community banks fulfill a very important function in establishing close relationships and directing credit to customers whose needs might otherwise go unserved. This evidence suggests that policymakers must understand the business model dynamics and incentives for banks of all sizes and must carefully consider the implications of new regulation, its cost and benefit, and its unintended consequences.

A rational path for community banks

Going forward, community bankers will be challenged once again to find ways to be successful in a difficult environment, ranging from an economy that is growing slowly amid an interest rate environment that is not especially conducive to good banking, to a complex and burdensome regulatory regime. I will focus my remarks on the latter.

The challenges of regulatory compliance have long ranked among community bankers’ top concerns. And you and I both know that the industry and regulators view risk differently. For example, in 2006, the banking regulators issued interagency guidance regarding commercial real estate concentrations. We received thousands of letters from the industry and members of Congress questioning the guidance and causing regulators to back away. As it turned out, some bankers would have been well-served to heed this warning. So, we believe supervision and regulation can and should play an important role. That said, having been

involved in community bank supervision for 30 years, I see today's regulatory issues having different implications.

As you are well-aware, much of the new regulation is a reaction to the shortcomings and problems at large banks and within capital markets that contributed to this crisis. Their business model and related activities and practices, combined with lax supervision, have been well-documented. The result is a new regulatory environment that is substantially at odds with how community banks actually operate.

For example, residential mortgage lending is likely to become much more complicated despite the focus on simplifying disclosures. This complexity includes new provisions defining qualified mortgage loans, requirements regarding a borrower's ability to repay the loan, risk-retention standards, and an array of risk weights under Basel III based on standard mortgage lending terms. In addition, the Consumer Financial Protection Bureau will be rewriting many of the key regulations related to mortgage lending.

This approach of specifying how residential mortgage loans should be structured and underwritten will undoubtedly leave community bankers with far less flexibility and authority to tailor such lending to the characteristics of their communities and customers. Because of this, it is not uncommon to hear community bankers say that they may be forced to cut back substantially on their home lending activities or even eliminate them entirely. Such unintended consequences are costly and impede mortgage lending at a time

when housing markets are weak.

New capital rules, known as Basel III, contain a variety of features that could have a significant effect on community banks if they are adopted as originally proposed. I know this because I read all 1,000 pages of the draft rule. Some of these include higher and more complex risk weights for selected types of loans and securities, inclusion of unrealized gains and losses on certain debt securities in regulatory capital calculations, the treatment of trust preferred securities, and additional capital deductions of mortgage servicing assets.

To be clear, I absolutely support efforts to increase the level of capital in our largest banks and improve the quality of this capital, but I find many of these rules to be costly for community banks and of little public benefit for this part of the industry. Risk weights based on standardized lending terms, for instance, completely ignore the data I referenced earlier—that lending relationships and personal information are of substantial value to community banks in controlling credit risks. Nor do the higher, more complex risk weights, as well as the restrictive provisions of Dodd-Frank, accurately reflect the low loss rates that community banks typically experienced on their residential mortgage lending and small business lending during the crisis. In addition, Basel III will almost certainly lead to greater fluctuations in regulatory capital levels at community banks even though the underlying assets and risks may not have changed much.

Furthermore, we should not forget that the proposed Basel III rules are designed to be a three-pillar approach, linking

capital requirements with supervision and market discipline. Unfortunately, I think the complexity embedded in the proposed capital requirements fails to acknowledge that supervisory and market assessments of a bank's capital are critical factors in judging capital adequacy. In my experience, the supervision of community banks clearly provides a more refined measure of risk than can be achieved with one-dimensional, static risk weights. And, based on the performance of risk weights in the recent crisis, I support efforts to strengthen our supervisory regime for large banking institutions to balance the assessment of risk beyond quantitative measures of capital.

We should also acknowledge that market discipline plays an important role in community banks. As our studies have shown, the ownership and management structure of community banks provides important incentives, as does a strong corporate governance framework. In the end, community bankers know they are not “too big to fail” and must manage their operations and risk exposures accordingly.

Overall, the strength of the community banking model should tell us that a regulatory format aimed at the largest banking organizations and the recent crisis is not likely to be a good fit for community banks. Some have advocated for a different regulatory framework for community banks to recognize the difference in business models of large and small banks. At best, though, this strikes me as only a partial fix. Until we address the incentive problems and “too big to fail” status of our largest financial institutions, the entire financial sector—indeed the entire economy—

will be vulnerable to future crises. For that reason, I would argue that we must also take steps to ensure that the largest institutions operate under a framework that encourages safe and sound banking and allows for failure of mismanaged risk.

Facing the future

In closing, history has shown that well-managed and innovative community banks are well-positioned to handle the challenges of the future and to take advantage of new opportunities. The new regulatory challenges, though, may be a different type of battle. I have been involved in discussions to encourage regulators to take steps to ensure that community banks are not put at a disadvantage by laws and rules meant to fix problems that do not exist in community banks. This Reserve Bank is fully committed to this objective, and I encourage all of you to share your thoughts with us and with other regulatory agencies at every opportunity.

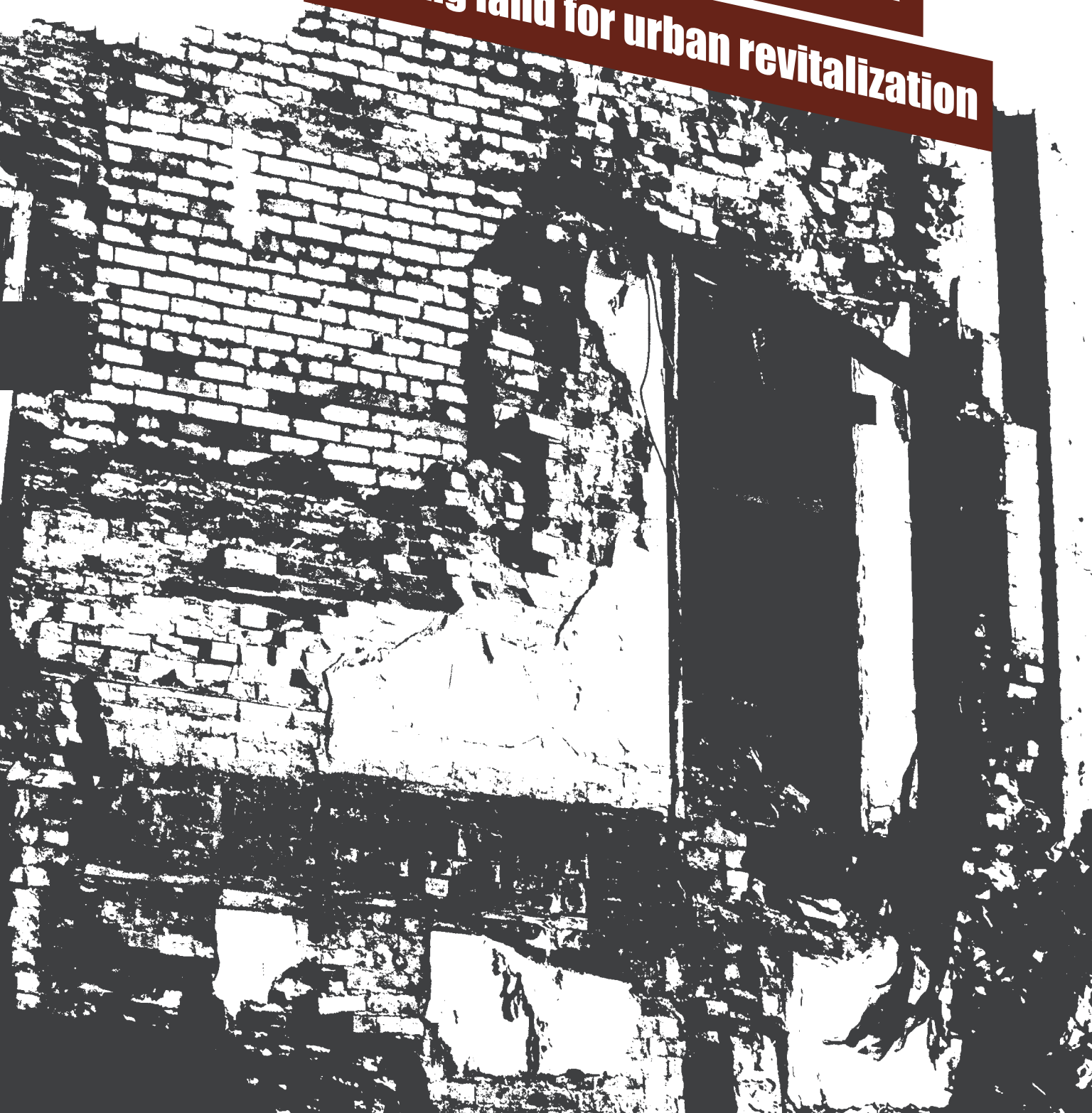


**ESTHER L. GEORGE, PRESIDENT
FEDERAL RESERVE BANK OF KANSAS CITY**

President George addressed the 2012 Community Banking Conference in November at the Kansas City Fed. See related story, Page 24.

Brick by Brick

Banking land for urban revitalization





The urban Kansas City house has sat vacant for years. Broken furniture, moldy rugs and discarded clothes lie strewn about. The roof caved in long ago and now rain water pours in, turning everything into a soggy, smelly mess.

Amelia McIntyre, an assistant attorney for the city of Kansas City, Mo., surveys with disgust the broken glass and old tires littering the front yard. “These houses are collapsing,” she said. “And the cost of maintenance is falling on the Kansas City taxpayer.”

The cost is high. Officials say Kansas City pays \$1.8 million annually to maintain—and in some cases demolish—many of the estimated 14,000 vacant and abandoned properties distressing the city’s urban neighborhoods. That doesn’t count millions of dollars in lost tax revenue and costly service calls to police and firefighters.

Now the city hopes to gain a better handle on its derelict properties.

A growing trend

This year the Missouri Legislature approved efforts in Kansas City to start a land bank, a mechanism that provides an expedited

process for local governments to acquire vacant, abandoned and tax-foreclosed properties, and return them to productive use again.

Land banking is a growing trend. Dozens of cities and counties across the country have started land banks in the last decade to address urban blight. Kansas City, Kan., has one form of land bank that acquires vacant lots. Officials hope to expand its provisions to include abandoned houses.

Legislation is expected to be introduced in January in Nebraska to allow land banking in Omaha. The business community sees the effort as a way to spur development. In Denver, private and nonprofit groups are collaboratively using a form of land banking to assemble vacant property on which to, among other things, build affordable housing near rapid transit stops.

The driving force is the desire “to acquire and maintain properties that are not marketable” and that have become nagging liabilities for neighborhoods and communities, says Frank Alexander, the Sam Nunn Professor of Law at Emory University School of Law and a cofounder of the Center for Community Progress, which helps cities create land banks.

Alexander says the concept supports three outcomes: allow communities to acquire titles to distressed properties; eliminate liabilities, including tax liens and questions of ownership; and transfer the properties free and clear to new homeowners in a way that supports community and neighborhood revitalization efforts.

Alexander helped Kansas City officials prepare their land-banking proposal, and he is assisting the efforts to get a land bank in Omaha.

David Park, deputy director of Kansas City's Department of Neighborhoods and Housing Services, says the idea for a Kansas City land bank was sparked, in part, by a videoconference at the Kansas City Fed that featured successes in Flint, Mich., and Cleveland, Ohio.

"I thought, 'that's what we needed,'" Park said.

Since the 1940s, vacant and tax delinquent properties in the Kansas City metropolitan area have mostly ended up in the Jackson County Land Trust. But officials began to view the land trust as outdated. For one thing, property sold by the land trust has to fetch two-thirds of its assessed value. That may have worked in the 1940s, but after decades of urban blight, many vacant properties held by the trust have little value, so they can sit vacant and unused for years.

Further, there is little control over who buys land from the land trust. Before the foreclosure crisis, some speculators acquired land trust properties, betting their values would rise. When that didn't happen, the properties were abandoned and went right back into the land trust.

"It was a revolving door," Park said.

Worse, even though the land trust is charged with maintaining the properties, it lacks the money to do so. So the city assumed the task of caring for neglected and abandoned properties, mainly because citizens expect it to. But with the foreclosure crisis and the Great Recession, the cost to care for the properties has skyrocketed.

The number of abandoned and tax-

foreclosed properties ending up in the land trust nearly doubled starting in 2008—from about 2,000 to more than 3,700. Many are vacant lots, but they still have to be mowed. Most of them will now go into the land bank.

"We needed a land bank that would give the city more authority to receive, work with and sell properties that end up in the hands of home buyers," Park said.

Nonprofit models

Land banking is not necessarily a new concept. What's new is that governmental entities have found ways to refine their use to address large-scale urban decay.

But nonprofit organizations have also used land banking—in partnership with national housing institutions, foundations, cities and lenders—to assemble and hold land for development that addresses the needs of low- and moderate-income communities.

For example, in Denver, the Urban Land Conservancy, Enterprise Community Partners and the City of Denver have led efforts to establish the first leveraged fund to preserve affordable housing and community assets near rail stops on that city's growing rapid transit system. As sole borrower of the \$15 million Transit-Oriented Development Fund, the Conservancy is acquiring properties that will support more than 1,000 affordable housing units, including existing multi-family apartments, in current and future transit corridors.

The effort was in response to investors who began buying land destined to rise in value along proposed new routes. Seeing a potential risk to lower-income populations, the nonprofit groups, working with the city, began acquiring land "so that gentrification and dislocation of current residents could be avoided," said Christi Longsdorf, operations and communications director for the Urban Land Conservancy in Denver.

"If you wait five to 10 years, that opportunity is gone," she said.

The list of Transit-Oriented Development Fund investors is impressive. It includes the Conservancy, the City of Denver, Enterprise



PHOTO BY JASON DAILEY

DAVID PARK IS DEPUTY DIRECTOR of the Department of Neighborhoods and Housing Services in Kansas City, Mo., which is establishing a land bank.

Community Partners, the MacArthur Foundation, Colorado Housing and Finance Authority, the Rose Community Foundation, Mile High Community Loan Fund, First Bank, U.S. Bank and Wells Fargo.

Enterprise Community Partners is currently leading efforts to increase the Fund to become a regional \$30 million resource that will leverage more than \$500 million in economic development activity in the metro Denver region.

The Urban Land Conservancy has also used land banking to preserve land for schools, recreation centers, a new public library and centers where nonprofit organizations share expenses and collaborate for increased community impact.

Economic development also is the reason

for starting a land bank in Omaha.

Jamie Berglund, senior director for community development for the Greater Omaha Chamber, cited the potential for available urban land that can be acquired with clear title and that can be made shovel-ready for the development of small businesses.

“When a business makes an investment, they need some degree of certainty that it will not only be protected, but that it will grow,” Berglund said.

She says that “implementing a redevelopment tool like a land bank, which will work to bring under-utilized property back to life, can only serve to promote a positive and nurturing environment for a small business to thrive.”

An aide to State Sen. Heath Mello of

Omaha said the senator plans to introduce land bank legislation in the Nebraska Legislature in January. He said a study showed Omaha has as many as 13,000 vacant and abandoned properties.

“Omaha is the next kid on the block (when it comes to land banking),” Alexander said. “And it is learning from Kansas City.”

Kansas City, Kan., also is following the lead of its big sister city across the state line in Missouri.

Kansas City, Kan., has land banked vacant lots for more than a decade. But in recent years, the number of vacant houses has steadily increased.

Instead of “babysitting” more than 2,100 vacant lots, officials are seeking ways to include abandoned and tax-foreclosed houses, says Chris Slaughter, manager for the Wyandotte County Land Bank in Kansas City, Kan.

Slaughter says officials are now studying how they can take “properties that aren’t producing revenue and put them in the hands of groups that will be able to fix them up, sell them and get families in there.”

Refining the template

The template for most modern land banks stem from the work of officials in Genesee County, where Flint, Mich., is located, and Cuyahoga County, where Cleveland, Ohio, is located.

Both counties began using land banks between 2002 and 2007. Both cities had lost thousands of residents, leaving behind acres of contagious blight. Officials wanted to reclaim or demolish abandoned houses that pulled down neighborhood values, attracted crime and piled up millions of dollars in unpaid taxes.

But acquiring the properties was challenging. Tax-lien foreclosures can take three years or more. And serving code violations on owners, who had disappeared, died or who lived out-of-state, was even harder. Determining who owned title to many distressed properties was a nightmare.

“We realized that the properties were going into the system like a fire hose,” said Gus Frangos, president of the Cuyahoga County Land Revitalization Corporation. “There was massive abandonment in Cleveland. Whole neighborhoods turned into bombed-out areas.”

Officials needed a way to funnel unmarketable properties through a mechanism that allowed the county to gain ownership and repurpose the properties.

Frangos said the model Cuyahoga came up with, and on which Kansas City based a portion of its land bank, has three main engines.

First, he says a land bank should have a government purpose but without the bureaucracy inherent in government. It should be able to borrow, lend, sell and float bonds, but not have to run every sale through a city council or a county board.

Second, he says a land bank has to be able to intervene in the tax-lien foreclosure process ahead of speculators who buy up dozens of parcels and then sit on them, or sell them to

JULIE PORTER is executive director of Greater Kansas City LISC, which helped with the organization of the Kansas City land bank.



PHOTO BY JASON DAILEY

unsuspecting out-of-state investors.

Third, Frangos said, the land bank has to make money to sustain itself.

In Cleveland, officials can claim penalties and interest charged on back taxes, as well as make money off the sale of houses. Last year, the Cuyahoga County land bank made \$7 million from penalties and interest on back taxes and \$3 million selling property.

Still refining

Kansas City officials say their land bank is still a work in progress, noting that it lacks some of the more potent features of the Cuyahoga County land bank.

For instance, though officials are able to intervene sooner in the process, they can still find themselves bidding against speculators on the courthouse steps for some of the more valuable tax-delinquent properties. City officials do have one advantage, however: They don't have to fork out as much in cash to buy the property.

In addition, the Missouri Legislature limited the Kansas City land bank's power to acquire and hold land for major redevelopment projects, bowing to conservative groups that argued land banks run counter to a free market system.

Park and McIntyre are unperturbed, saying the city may decide to go back to the Legislature in an effort to refine the land bank's authority.

Julie Porter, executive director of Greater Kansas City LISC, a nonprofit intermediary that worked behind the scene to help develop the legislation and advocate for the land bank, said it is a good start.

"Many of these investor-owned, LLC (limited liability corporation) properties were abandoned and the taxes weren't paid," she said. "Now, it is very unclear who actually owns the property. Is it the bank, the investor, who?"

But once the city acquires the land and funnels it through the land bank, "there is a method to clean the title and make it more

likely it will sell to a home buyer."

In addition, Porter said, the land bank can sell bonds, so it can provide incentives to developers and encourage redevelopment. Also, the land bank can get 100 percent of the first three years of taxes on a property after it's sold.

"That is huge," Porter said. "There will come a day the land bank, because it is putting land back onto the tax rolls, is going to become self-sustaining."

Park isn't as optimistic that the land bank will sustain itself in the near future. Still, he said, "We are in as good as shape as any city, and better than others.

"Some cities have lost so much population they will never get it back. Kansas City still has population, reasonably good housing stock and an interest in urban living. So there is hope that we can repopulate these neighborhoods."

McIntyre cautions that the land bank is not a panacea that can cure all urban ills.

But she says it is a valuable catalyst for urban change along with other tools, such as code enforcement, eminent domain and the authority to go after decayed houses that pose a community danger, like the house with the caved-in roof.

"With a land bank, the city can be more proactive about getting properties into the hands of legitimate buyers and investors, and to return a home back to the community as a home that generates revenue," she said.



PAUL WENSKE, TEN CONTRIBUTING WRITER

FURTHER RESOURCES

"Low-Income Housing Tax Credit Developments and Neighborhood Property Conditions"

by Kelly Edmiston

www.KansasCityFed.org/TEN

COMMENTS/QUESTIONS are welcome and should be sent to teneditors@kc.frb.org.

BROAD REPRESENTATION, REGIONAL ROOTS

KANSAS CITY FED RELIES ON DIRECTORS FOR INSIGHT

As designed by Congress in 1913, the Federal Reserve is an innovative blending of public and private institutions. While the Board of Governors in Washington, D.C., is a government agency with broad oversight responsibilities, there are 12 regional Federal Reserve Banks located throughout the United States that are under the direction of local Boards of Directors. In addition to oversight responsibilities for their respective Reserve Banks, the regional Fed directors serve as a critical conduit between their local communities and the nation's central bank, offering critical insight and counsel on the economy drawn from their own expertise and contacts.

This system of the independent regional Reserve Banks, which also have affiliated Branch offices, are in direct recognition of the value Americans place on limiting influence and ensuring broad representation. Prior to the Federal Reserve, the United States had made two attempts at a central bank, but large areas of the country, especially along the frontier and in the South, felt the institutions were too closely aligned with the power centers of the Northeast, and the institutions were abandoned.

The Tenth Federal Reserve District includes western Missouri, Nebraska, Kansas, Oklahoma, Wyoming, Colorado and northern New Mexico. The Kansas City Fed has three Branch offices, Denver, Oklahoma City and Omaha, in addition to its headquarters.

Here's a closer look at four Tenth District directors:

MAX T. WAKE
KANSAS CITY DIRECTOR



MAX T. WAKE

Max Wake says doing what's best over the long-term, instead of taking high risks on short-term events, provides his customers and his bank a more successful future.

Jones National Bank & Trust Co., based in Seward, Neb., provides banking, trust, insurance and personal finance services to a variety of agricultural, industrial, commercial and individual customers.

"We hope to meet our customers' needs beyond just core banking," he said.

Wake says nothing is more fulfilling than having a long-time customer tell you that your bank helped him or her succeed with their business.

"That's a pretty special thing to have someone say," he said.

His experience with his customers helps in his role as a director for the Kansas City Fed.

"We may not agree with every monetary policy decision, but community bankers understand the important role the Federal Reserve and Kansas City (Fed) plays in the economy."

Wake says Esther George is a great advocate for Federal Reserve independence, and he thinks the Federal Reserve Act is very clear about that issue.

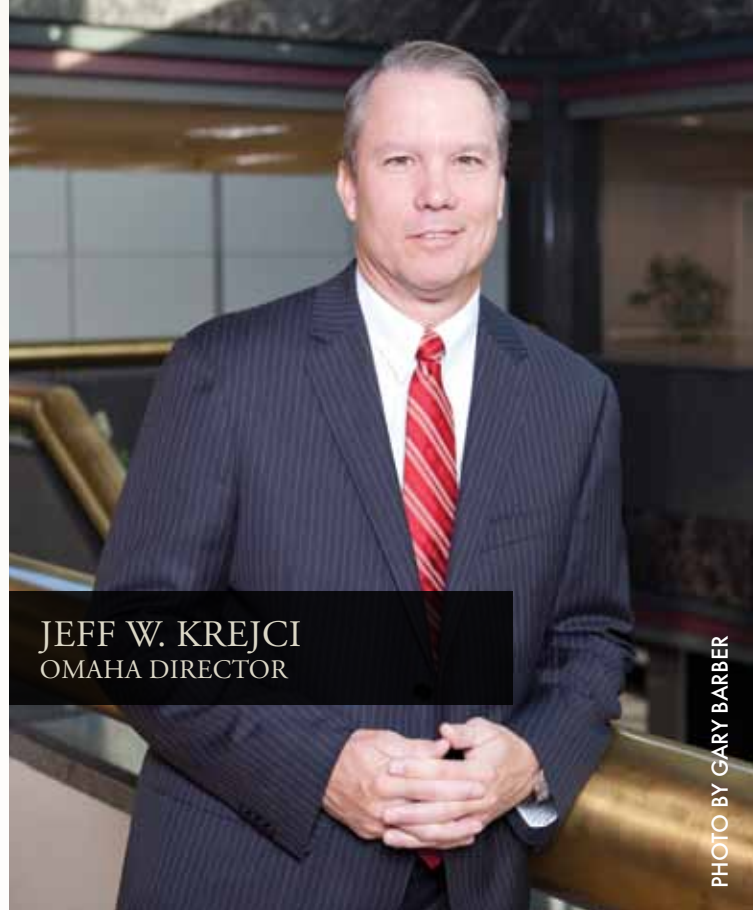
The intent of the act also allows for directors to share with the Fed real-time economic information from a variety of business sectors.

Wake is a Class A, Group Three director, which is elected by small banking institutions in the Tenth Federal Reserve District.

"They are closely held, family owned, and they like to do the right thing, and they are good to customers and staff and the communities they serve," he said of these bankers, who elected him.

Wake tries to fairly convey their concerns and thoughts, and put faces and context to the data the Fed provides. He also acts as an ambassador, explaining to the public the role and purpose of the Fed.

"It's about stewardship," he said. "In a small way I try to do whatever I can to preserve and enhance the Fed, to help it be successful."



JEFF W. KREJCI
OMAHA DIRECTOR

PHOTO BY GARY BARBER

JEFF W. KREJCI

Jeff Krejci starts his work day at the local coffee shop, talking with patrons about the latest news and events.

As president and vice chairman of the board of First State Bank in Hickman, Neb., it's important to Krejci to keep his finger on the pulse of the community.

His community goes beyond the city limits of Hickman. Krejci spends much of his time traveling; First State Bank has \$380 million in assets, 25 lenders and 17 locations in 15 communities.

"My car is my second office," he said.

Krejci and the 140 employees of First State focus on relationships and keeping the communities they serve strong. His commitment to community applies in his role as a director of the Kansas City Fed's Omaha Branch.

"I've been in banking just shy of 30 years and always was enamored with the Fed, especially the Kansas City Fed," he said.

The Kansas City Fed is an asset to the communities it serves through its banking



regulation and financial services, research and economic forums, financial education for teachers and students, fiscal literacy for adults, and other services, Krejci said.

“I enjoy the economic forums and listening to the people at the Fed who know what’s going on in the marketplace,” he said.

Krejci also likes to give the Kansas City Fed feedback.

“I give them a community bank perspective, which is based on the customers we serve,” such as ag and commercial business, he said.

He also uses those customer and community connections to promote the work of the Kansas City Fed and provide people a complete picture of how the Fed did not cause the current economic climate, but has helped improve the situation.

“I don’t think people understand the Fed sometimes and form their opinions, or perspectives, based on what they receive from the media.”

BRIAN R. WILKINSON

Brian Wilkinson’s first job interview out of college was with the Kansas City Fed’s Denver Branch office.

“I was so excited about their officer training program,” he said.

Wilkinson is a fifth-generation Colorado

community banker, who, when growing up, heard about banking and the importance of the Federal Reserve System.

He didn’t get the job, but he continued his pursuit of a career in banking, and now, several years later, he is president of Steele Street Bank and Trust in Denver.

“I have been with the bank since it opened as a De Novo in 2003 with \$10 million of capital,” he said. “Since that time, the bank has grown to three locations with \$430 million in total assets and over \$300 million in total trust assets.”

He also is a Board member at the Kansas City Fed’s Denver Branch. He accepted the role to get a better understanding of the Fed, and it gave him an opportunity to provide the Fed feedback about economic conditions his customers face.

“It is important for the Fed to get this type of feedback because it has an emotional component and affects behavior, and thus, the economy,” he said.

His perspective comes from his roots in Colorado, as a generation Xer living in a dual-working household with three children and years in the banking sector.

At Steele Street, he performs all the duties of a bank president: reading about the previous day’s events and financial reports, meeting with the senior management team and working with

new and existing customers. He also keeps his eye on the future.

“I really am a fanatic about technology and try to fully utilize my iPad, iPhone and MacBook Pro,” he said. “I am probably one of very few community bankers that is pushing for all Apple products in a community bank.”

But this doesn't mean Steele Street has forsaken the community banking model: making loans and transactions based on good relationships.

“We make individual loan decisions on all loans over \$300,000, no credit scoring at Steele Street,” he said.

And they take this concept of relationships and community beyond the bank's walls.

“Every officer at the bank is required to be involved in an outside community organization,” he said.

RICHARD K. RATCLIFFE

Education is a family trade for Richard Ratcliffe.

“We have been very fortunate to become the largest family-owned textbook business in Oklahoma with stores at several of Oklahoma's leading universities,” he said.

His father, Lee Ratcliffe, started the business in 1925, and by the 1960s, “my father

had more business than he could manage.”

Ratcliffe, who is a Board member at the Kansas City Fed, and his father began to remodel and expand the family business, which has grown to include Ratcliffe's brother, son and daughter, and now his grandson and granddaughter.

His work provides a satisfaction that goes beyond ordinary business success.

“Those of us who are fortunate enough to work near university and college campuses know the real value of working with young people all of your life,” he said.

Ratcliffe has been involved in all aspects of the business from daily operations to management of the stores in other cities. His experience as a small business owner helps him in his role as a director, providing valuable information that the Kansas City Fed and Fed System uses in setting policies and making decisions.

“As a small business man or business woman, we constantly work against a tide of legislation and public policy supporting large-population area concessions or large business interests,” he said. “We have a responsibility to make sure our voice is heard.”

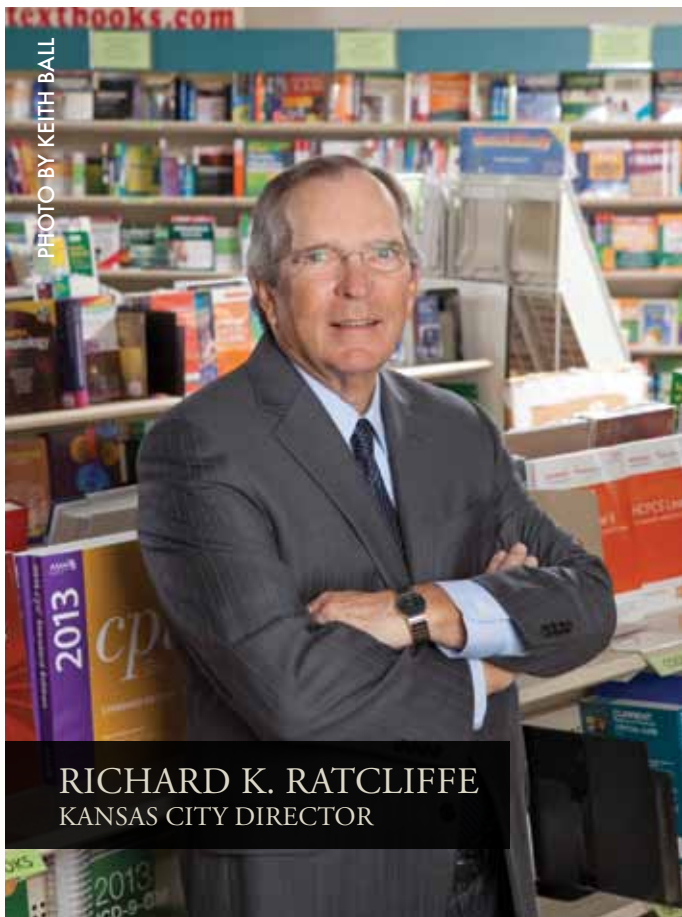
The Federal Reserve Bank structure creates an environment where all aspects of the nation's financial sectors can influence the decisions and actions that affect the country's economic future, Ratcliffe said.

“In my financial lifetime the Federal Reserve has been the pacemaker for the world with monetary policy responsibility, its payment systems and the central bank functions,” he said.

Ratcliffe first served as a member of the Kansas City Fed's Oklahoma City Branch Board and is now in his second term on the Kansas City Fed Board.

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FOR MORE INFORMATION on the Kansas City Fed's directors, including bios, visit KansasCityFed.org/aboutus/leadership.



RICHARD K. RATCLIFFE
KANSAS CITY DIRECTOR



Persistent Differences

Unemployment trends among U.S. metro areas

In his recent research, Kansas City Fed economist Jordan Rappaport says the correlation between jobs growth and unemployment declines is not necessarily true for all metropolitan areas.

“If they are below the national unemployment rate today, most likely they will be below the national rate 10 years from now,” he said. “If they are above it today, they will most likely be above it 10 years from now.”

Unemployment rates differ widely across U.S. metropolitan areas.

In 2007, they ranged from 3.1 percent or less among the 25 lowest unemployment metros to 6.6 percent or more among the 25 highest unemployment metros.

Moreover, Rappaport said, those metro areas that had a relatively high unemployment rate in one year tended to have a high unemployment rate 10 years and even 20 years later.

The city of Merced, Calif., had an unemployment rate above the median from 2000 to 2007, and then had extremely high

unemployment throughout 2007, despite being the fastest growing city in that state since 1980.

There was a subgroup of metros that showed a strong correlation between jobs growth and declines in the unemployment rate, but Rappaport said that was a small group, less than 15 percent of the metros studied. On average, more jobs or fewer jobs didn’t mean a change in the unemployment rate.

The unemployment growth rate in Omaha, Neb., remained below the median of about 1.5 percent from 2000 to 2007, and remained lower than the median unemployment rate throughout 2007. But the city also experienced low job growth during those same times.

There are several possible reasons for why some metros have persistently high unemployment and others have persistently low unemployment. One obvious reason is the long-term growth or decline of a metro area’s industries.

Among the others, the characteristics of the workforce appear to be the most important. Such people-based characteristics include

workers' industry- and occupation-based skills and experience, educational attainment, their English language skills, and their general level of work experience as in relation to their age.

While persistently high relative metro unemployment rates often do partly reflect the long-term decline of its prevalent industries, people-based characteristics also play a central role. The reason is that in response to declining metro employment, workers often can move to other metros in search of a job. Alternatively, if workers laid off from declining industries have skill sets in high demand elsewhere, businesses are likely to move in to be able to hire workers that meet their needs.

If laid-off workers have skills that are in low demand elsewhere, there would be little demand for them to move elsewhere or for firms to move in.

Rappaport argues that it is this latter mismatch between metro area worker skills and the workforce needs of employers through the remainder of the United States that accounts for persistently high unemployment.

For example, a metro area with a large share of its workforce employed in light manufacturing will naturally have a large share of its workforce with the associated skills. As light manufacturing activity gradually moves overseas, newly laid-off workers will find it difficult to find a new light manufacturing job either in the metro area itself or anywhere else. Repeated over time, this dynamic plays a large role in driving persistent metro unemployment.

Another cause of persistent unemployment among metros is the migration effect. An example is an auto manufacturing plant constructed in a metro area with a declining jobs growth rate. Most of the new employees lived elsewhere before gaining employment with the plant. So even with the new jobs, the metro area saw little change in the unemployment rate because there were more workers than available jobs.

Rappaport found that metros that had this experience usually had negative employment from 1990 to 2000 and saw no change to that status even with jobs growth in the 2000s.

And in some instances, the unemployment rate grew.

"The most important point from these decompositions is that net job changes have a relatively small effect on metro unemployment when they are positive," he said.

Moving costs may also explain why some unemployed workers tend to stay in metros with fewer job opportunities, which contributes to that metro's persistent high unemployment rate, Rappaport said.

And in some instances, firms are unwilling to pay for the relocation of workers, especially for low- to mid-level-paying jobs.

Another explanation why some metro areas may not see an increase in jobs growth is location—some metros, either due to weather, geographic location, lack of attractions and amenities or other reasons, may not attract workers or jobs.

Also, workers living in high unemployment metros may decide not to move to a metro with better job prospects because they don't want to leave behind their support networks, such as family, friends and other social ties.

Rappaport says the aforementioned characteristics show there's more to a metro area's unemployment rate than just the lack of jobs growth.

Maximizing U.S. wealth creation depends in part on achieving the best match between workers and jobs. Enhancing the geographic mobility of workers could help achieve this, Rappaport said.

This may take government assistance, which is something voters may not agree with, he added. It also may take businesses investing in training of workers to fit hiring needs and paying for workers' moving costs.

FURTHER RESOURCES

"Why Does Unemployment Differ Persistently Across Metro Areas?"

by Jordan Rappaport

www.KansasCityFed.org/TEN



Kansas City Fed President Esther George, center, is pictured with faculty and staff of Kansas State University's College of Business Administration on Nov. 6, 2012.



DAVE MAYES / KANSAS STATE UNIVERSITY

George speaks to Kansas State University students and community members as part of the College of Business Administration's 2012 Distinguished Lecture Series.

George, center, participates in a meeting on banking regulation in Panama City, Panama, hosted by the Bank for International Settlements and the Association of Supervisors of Banks of the Americas on Nov. 16, 2012.



MAKING A CONNECTION



James Neiman and Esther George look at operations at the Devils Tower Forest Products, Inc. location in Hulett, Wyoming.



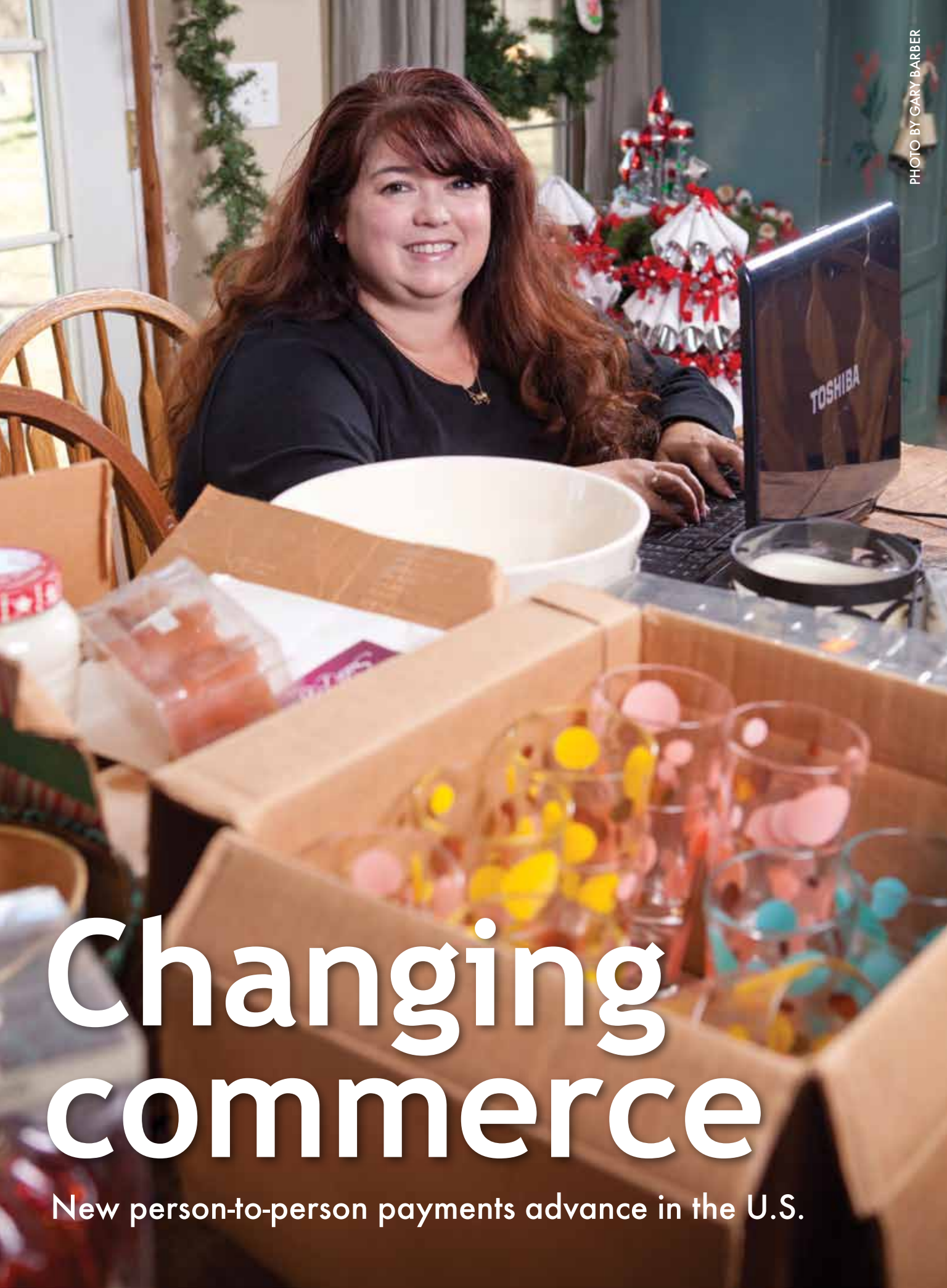
Esther George recently spoke to students, academics and business leaders at the University of New Mexico Anderson School of Management in Albuquerque, N.M.

Regional Federal Reserve presidents serve in several capacities, one of which is a conduit between their Federal Reserve Districts' communities and the nation's central bank. Presidents also use their expertise to help communities outside their district. As a person who has worked in banking regulation for more than 30 years, Esther George has participated in international discussions about bank regulatory issues of mutual concern.

In fulfillment of her role, George made recent visits to communities in the Tenth District, Panama and China.



George addresses a financial stability and banking supervision forum in Beijing, China, on Sept. 28, 2012. At the forum, hosted by the Bank for International Settlements and the China Banking Regulatory Commission, George discussed the need to address policies that shift financial losses away from those responsible.



Changing commerce

New person-to-person payments advance in the U.S.



Suzie Eads worked in sales, mainly selling cars, before she started a business in the 1990s. Her business was a creation of the dot-com bubble, when young entrepreneurs developed new avenues of doing business, relaying information and connecting with people. She found her niche with the online auction company eBay and became a micro-merchant.

Online person-to-person payment methods were new at the time. Eads took checks and money orders by mail at first. She had to wait for checks to clear her bank and there was a risk with fraudulent money orders, she said. Eads started using X.com out of California, which later rolled into PayPal, headquartered in California. Nonbank payment services startups like X.com were starving for customers, so much so the company paid Eads \$50 to join and an additional \$10 for every person she recruited as a new member.

Eads used other merchant services such as Amazon and operated her own website. As she began using these new online merchant and payment services for transactions, her bank became suspicious when she transferred money from her online accounts into her bank account.

“They called me and asked what this transfer from Amazon was about,” she said. “They don’t even think anything about it now.”

Before this century, person-to-person payments (in the United States) were almost entirely by cash and check, said Terri Bradford, a payments system research specialist at the Kansas City Fed, and William Keeton, a former vice president and economist for the Kansas City Fed, in their new research, “New Person-to-Person Payment Methods: Have Checks Met Their Match?” And today, the use of checks for person-to-person payments is quiet strong, they said.

Time and inconvenience were the costs associated with making cash transactions, they said, and the risk was the possibility of accepting counterfeit currency. Checks came with a cost—the seller didn’t know if the check was good, and the buyer, when making a purchase, such as through the mail, didn’t know whether the seller would deliver the goods. Banks also began to charge fees for the amount of checks an account holder wrote and the cost of maintaining a checking account.

Nonbank person-to-person methods existed before the technology boom. Western Union and other companies provided wire cash transfers for a fee, but buyers also were

required to visit a brick-and-mortar branch of the company.

As the 20th century came to a close, the spread of the Internet made it possible for consumers to make such payments from their personal computers.

The first commercial bank website launched in 1995 and provided customers the opportunity to make transactions online. By 2000, 53 percent of commercial banks had websites, and by 2011, it was 90 percent. Smaller banks were slower to provide such services; by 2011, only 40 percent of banks under \$25 million in assets offered transactional websites.

Bradford and Keeton said the Internet also ushered in the rapid growth of online auctions and direct-purchasing and further Internet expansion and advances in mobile devices and applications spread the use of bank and nonbank financial services in the 2000s.

New methods of making person-to-person payments developed from the simple market principle of supply and demand. On the

demand side, the driving influences have been the emergence of new forums for commerce, such as online auctions and the increasing desire by consumers to monitor and control payments. On the supply side, the main elements have been technological advancements, such as faster Internet speeds, increased computing power and now smartphones.

Bradford and Keeton looked at these various methods and consumers' attitudes toward them. They found that these distinct models for person-to-person payments have emerged: nonbank-centric, bank centric and card-centric.

Some of the new methods are faster than checks, especially the card-centric methods that give cardholders immediate access to funds, and the bank-centric methods that require only a single payment between bank accounts. In addition, because the new person-to-person payments are electronic and can be used with mobile devices, the methods have lower resource costs and greater convenience than the

NEW PERSON-TO-PERSON PAYMENT METHODS such as PayPal, which is owned by eBay, have made it more convenient and secure for consumers to shop online.



PHOTO BY GARY BARBER

traditional person-to-person payments.

Most consumers have taken advantage of the card-centric and bank-centric payment methods and online banking and consumer services like Western Union, but this doesn't mean the check is obsolete.

For Eads, the advancement in technology and person-to-person payments gave her and many other micro-merchants the ability to start their own businesses at a very low startup cost.

Eads was pregnant with her third-oldest child when she started on eBay, hoping that her extra income would help build a new family home. Four more children and 50,000 transactions later, Eads now gives advice to users on how to navigate eBay and PayPal. She has written her advice column, "Ask the eBay Queen," since 2004.

"I'm sure I wouldn't have started a business if it wasn't for eBay and PayPal," she said.

Eads oldest daughter, Rachel, also helps with the business, taking photos of items, posting online, tracking inventory and shipping sold items to customers—all done from their home that the family built outside Rantoul, Kan., about 40 miles south of the Kansas City metro area.

Eads still uses her community bank just down the road from her house, but she also uses her PayPal card, which she receives 1.5 percent cash back on every purchase. And though most of her business is done online and through PayPal, which is owned by eBay, she still wouldn't turn down a check. She sees a day, however, when the conveniences and securities of new payment methods could make the check obsolete.

PayPal and other person-to-person payment services, such as 2Checkout, have made it safer to conduct online transactions, Eads said.

Bradford and Keeton say the new person-to-person payment methods are more secure than checks "in the sense of protecting account information." And bank-centric and card-

centric methods "have the additional advantage of securely verifying the payer's identity." New payment methods will continue to move forward with advances in technology—online, cards and mobile applications—but consumer and merchant acceptance for the new payment methods is the main obstacle in the United States.

In a survey of major credit card customers, Lightspeed Research found that most customers thought the ability to make payments from a smartphone as unimportant.

Within the area of mobile payments, the United States is far behind other countries in its acceptance. The Bank of Japan reported that \$22 billion in contactless mobile payments were made in 2010. Consumers in the United States, with a larger population, made \$1.5 billion in contactless payments in 2009.

Eads views the new technology and payments methods as opportunities for doing business, whether online or in a store. It also fosters an entrepreneurial spirit, providing a way for people to create new businesses and making it more convenient for consumers, she said.

"To pay someone with an (online account) or a PayPal card seemed a little screwy at first, but it's pretty savvy now," she said.



KEVIN WRIGHT, EDITOR

FURTHER RESOURCES

"New Person-to-Person Payment Methods: Have Checks Met Their Match?"

by Terri Bradford and William R. Keeton
www.KansasCityFed.org/TEN

COMMENTS/QUESTIONS are welcome and should be sent to teneditors@kc.frb.org.



COMMUNITY BANKS

REMAIN RELEVANT IN TODAY'S **BIG-BANK** ENVIRONMENT



Despite the changing regulatory environment, community banks' resiliency and ability to adapt gives them opportunity to compete in today's big-bank climate.

Community bankers, however, will need to take advantage of new markets and technological advancements in order to entice younger, technology-driven customers, while still providing that personal touch to their existing customers.

Speakers discussed these topics and other related issues at the 2012 Community Banking Conference, which more than 100 community bankers and regulators attended Nov. 2 at the Kansas City Fed.

"Through outreach events like these, we are able to share ideas and perspectives outside of an examination setting," said Kevin Moore, senior vice president of the Kansas City Fed's Supervision and Risk Management Division.

Community bankers will have to pay more attention than ever to the newest regulations and policies that result from the Dodd-Frank Act and Basel III rules, said Mary Beth Guard, executive editor of BankersOnline.com and CEO of Glia Group, Inc., and keynote speaker at the conference.

What's in the new regulations is extensive, repetitive and redundant, Guard said, and it will take competent people to make sure banks comply.

"The level of knowledge for a compliance officer is greater than ever before," she said. "You can't hire someone off the street and train them anymore. I'm telling you, be nice to the ones you have now."

Esther George, president of the Kansas City Fed, has her own concerns about the current direction of regulatory policy and how it affects the ability of community banks to be competitive and serve the credit needs of their communities.

"We often hear from community bankers that they do not expect this changing environment to work well for them," George said. "These bankers anticipate being hit with significant regulatory costs for a crisis that originated in other parts of the financial system."

Well-run community banks have always found a way to navigate new regulations and thrive in a changing banking environment, George said.

"To be sure, the community bank business model has proven resilient and able to withstand significant challenges when boards of directors



KEVIN MOORE, SENIOR VICE PRESIDENT of the Kansas City Fed's Supervision and Risk Management Division, introduces Community Banking Conference keynote speaker Mary Beth Guard, executive editor of BankersOnline.com and CEO of Glia Group, Inc.

and their management teams demand strong performance and are willing to be flexible and ready to capitalize on new opportunities," she said.

Guard said there's much of Dodd-Frank yet to come, but she's confident banks and financial institutions can handle the new climate.

In the past 30 years, community banks saw restrictions lifted on multibank holding companies and interstate banking practices, the removal of deposit interest rate ceilings, and certain lending and product markets shift to larger institutions, captive finance companies, credit unions and the capital markets.

Some of those changes allowed community banks to expand services and stay competitive in a changing financial market.

Steve Goodenow, president and CEO of Bank Midwest, Spirit Lake, Iowa, said his bank made the decision to become a financial

services holding company and pursue other noninterest revenue sources to diversify and grow revenue.

"We added complexity, regulatory second looks and most importantly, new revenue," he said.

The newest changes will provide more challenges and force community banks to reassess their game plans and to create a proactive business model, said Dan Musso, president and CEO of FinPro, Inc., in Liberty Corner, N.J.

"You must avoid the mistakes of the past and change your business model to reflect today's reality," he said.

He encouraged bankers to use enterprise risk management to their advantage and make sure their plans take a realistic look at capital, asset quality, management, earnings, funding, people and delivery channels.

Another change for community bankers

said Steve Brown, president and CEO of Pacific Coast Bankers' Bank, Walnut Creek, Calif., is the rapid technological developments within the banking sector.

"The first recorded bank loan was in 350 A.D., and pretty much nothing changed in the next 1,500 years."

But as the 20th century moved toward the new millennium, technology developments such as ATM networks, online banking, automation of banking operations, new financial instruments and risk-management models changed the way consumers bank.

"There are many tech opportunities for community banks to help them grow their services and customer base," Brown said.

From tablets to smartphones, community banks can develop services that meet their customers' needs, and the costs for new technology will pay for themselves if done correctly, he said.

Brown cited a study that showed customers receiving e-alerts about loan payments were 70 percent more likely to make a payment on time. And given the growing consumer climate for e-banking, Brown says community banks must invest in new banking technology. Currently, a majority of consumers 29 years and younger bank with the four big banks: Wells Fargo, Citigroup, Bank of America and JPMorgan Chase, and a majority of that group owns and uses smartphones and other technology for banking.

"We've (community banks) got to figure out how to get them back," Goodenow said.

A Kansas City Fed study shows that while many now claim that the value of customer relationships is declining with the use of credit scoring and credit risk models, there is real value in relationship lending and in the soft personal information on customers that community bankers typically have, George said.

"History has shown that well-managed and innovative community banks are in the best position to handle the challenges of the future and to take advantage of new opportunities,"

she said. "The new regulatory challenges, though, may be a different type of battle."

George has encouraged regulators to ensure that community banks are not put at a disadvantage by laws and rules meant to fix problems that do not exist in community banks.

"This Reserve Bank is fully committed to this objective, and I encourage all of you to share your thoughts with us and with other regulatory agencies at every opportunity," she said.

Community banks, whether large or small, will need to invest in people who are contextual thinkers, who are detail oriented, who give advice up front and think about business implications from multiple perspectives, Guard said.

Even with the downturn in the economy and loss of some banks, Mark Moylan, deputy regional director with the FDIC in Kansas City, Mo., remains optimistic about the future of community banks.

"I'm highly cognizant of the well-run institutions and their capabilities of overcoming the changes within the industry," he said.

Moore said the conference was part of the Kansas City Fed's continuing efforts to reach out to community banks.

"The dialogue and questions we receive from community bankers are important in helping us understand the impact of proposed policies and regulations on their operations."



KEVIN WRIGHT, EDITOR

To read Esther George's full remarks at the conference, see Page 1. For more information on the conference, and for guest speaker and panel presentations, go to <http://www.kansascityfed.org/eventinfo/banking/2012-com-banking-documents.cfm>



WHERE JOB AND LIFE CONVERGE

Personal experience gives meaning to Kansas City Fed's rural focus

Jason Henderson strolls through the livestock pens at the 2012 World Dairy Expo. Though his presentation on opportunities in the international agricultural export market is still fresh in his mind, one thing keeps his focus as he admires the bovine: the scents.

“The mixture of smells brought back some really nice memories,” he said.

Before he was the Omaha Branch executive and lead ag economist for the Kansas City Fed, Henderson was a farm kid. His family milked 50 head on a 320-acre plot in northeast Iowa.

Though his background may make him stand out among his peers across the Federal Reserve System, Henderson is by no means an anomaly in the Kansas City Fed ranks. Rural economies are a focal point for the Kansas City Fed because of its location, but the passion behind the focus has a lot to do with the personal experiences of its employees.

Research specialty

With a large swath of the Great Plains and Mountain States falling within the borders of the Tenth Federal Reserve District, the Kansas City Fed has emerged as a leading resource of agriculture-related economic research. Henderson and his colleagues study trends in rural economies and report their research in Kansas City Fed publications such as the Survey of Agricultural Credit Conditions, the Nebraska Economist and The Main Street Economist.

In 2010, under Henderson's leadership, the Kansas City Fed took over compiling national trends in farm lending for the quarterly Agricultural Finance Databook, which was previously managed by the Federal Reserve Board of Governors in Washington, D.C.

Henderson's focus on ag issues, particularly as they pertain to finance, has put him before Congress to testify—twice.

Perhaps better than anyone, Henderson appreciates the Kansas City Fed's long tradition of ag research.

He was attracted to the Kansas City Fed for its ag specialty, starting as a junior-level research associate in 1996. He speaks highly of the economists who helped him hone his skills.

"I am just one person in a chain of really strong ag economists," Henderson said. To him, the tradition began in the 1970s with former Kansas City Fed economist Marv Duncan. It was Duncan who started an annual conference—at the time slanted toward ag topics—that evolved into the Kansas City Fed's renowned economic symposium in Jackson Hole, Wyo.

Today, the Kansas City Fed hosts an annual Agricultural Symposium that brings together leaders in ag research, policy and business from across the globe. The 2012 symposium centered on whether ag could escape its historical cycles of boom and bust.

The Kansas City Fed's roots in agriculture, however, run deeper than its geographic location and the subsequent research focus. The most recent issue of the Agricultural Finance Databook highlighted the unfolding economic impact on farmers of 2012's historic drought, showing farm operating loans taking its highest jump in five years. It's a trend that Henderson and his colleagues, many of whom are also from rural areas, can relate to personally.

Living it

Among the Kansas City Fed's 1,400 employees are personal stories of rising before dawn to bucket-feed calves in the freezing rain, the satisfying feeling of sweat on your neck when you call it a day, memorizing the 4-H pledge, and learning to drive a tractor before learning to drive a car.

President Esther George balances a demanding Fed schedule and weekends at the family farm outside St. Joseph, Mo.

Evan Richter, a bank examiner in the Omaha Branch, hails from a family that owns roughly 1,800 acres in southwestern Nebraska. They raise wheat, corn and crossbred beef cows—a small contingent of which he



GROWING UP ON A FARM during the 1980s financial crisis helped shape both a career path and a world view for Kansas City Fed ag economist Jason Henderson (at left in family picture above).

purchased himself several years ago while in college.

"In a perfect world, if they paid me as much, I would be a farmer," he said. "Ag was always my first love."

Richter returns to the farm as his job allows. "I especially try to make it back when something big is going on."

"Big" in farming terms invariably encompasses the fall harvest season. After the drought, Richter said there wasn't much harvest to speak of on his family's land. Their plot is mostly dryland with some irrigation, which translates into a lot of lost crops. His experience is perfectly anecdotal of the recent research on the drought Henderson and his colleagues published.

"It's definitely something I've seen firsthand," Richter said of the research. "I feel for people when I read the research [on the drought]."

His robust understanding of ag enhances his bank examiner role. The Tenth District is home to the nation's largest population of community banks, often located in rural areas largely dependent on the economic well-being of agriculture.



JASON HENDERSON, vice president and branch executive of the Kansas City Fed's Omaha Branch, meets regularly with the Branch's Board of Directors.

“There won’t be so much of a learning curve when I start working on ag loans,” he said. “Having that understanding will be even more important as I move on in my job.”

In the Kansas City office, Cherie Gordon’s job frequently puts her in contact with bankers experiencing the peaks and valleys of farmers’ credit needs, something she relates to personally. Each summer of her formative years, she left the bustle of the city for the breezes of the plains. Her grandfather’s farm was a gathering point for the family. She rounded up cattle on

horseback, chased the pigs out of the mud and tended the fields alongside her dad and cousins.

“That’s where I learned to drive—driving grain trucks,” she said. “I drove the grain trucks around the fields while they filled them up.”

When Gordon reads the ag research published by the Kansas City Fed, she can picture the people and places she knows behind the data.

Today she lives with her husband, kids, their chickens and their horses at the intersection of two gravel roads deep in the

WHERE TO FIND THE KANSAS CITY FED AG RESEARCH

Find links to the Kansas City Fed’s agriculture-related research at KansasCityFed.org/Research/RegionalEconomy.

You can also sign up to receive e-alerts when new ag research is released. Enter your email address at KansasCityFed.org/ealerts and select publications such as Main Street Economist and Survey of Agricultural Credit Conditions.

Follow us on Twitter @KansasCityFed



Missouri countryside. Though her commute to downtown Kansas City is 45 minutes on a good day, she is in love with the “wide open feeling of being outside.”

Any hassle with the distance is “well worth it” to expose her children to the work ethic and delayed gratification of a rural environment.

“It’s just a different mindset,” she said.

It’s a kind of mindset that attracted self-described city girl Linda Foos away from the bustle of Denver, where she works in the Branch office, to the outskirts of Palisade on the Western Slope, about three-and-a-half hours from the Mile High City.

For their retirement years, she and her husband purchased a five-acre orchard where they harvest about 21,000 pounds of sour pie cherries each year.

From April until October, she and her husband split time between their Denver metro



PHOTO SUBMITTED BY CHERIE GORDON

CHERIE GORDON, at her farm in Missouri, understands what bankers experience with the peaks and valley’s of farmers’ credit needs. Gordon works in Statistical Services at the Kansas City Fed.

home and Palisade.

“We’re kind of weekend farmers,” she said. But only until they are both retired. “Eventually we hope to build a house on (the plot).”

Shaping a world view

In the mid-1980s, with the country plunged into a financial crisis, Henderson’s father came to the dreaded decision point so many of his fellow family farmers did: hold fast or sell. It was time for “the talk” with his sons. In that conversation, both young men declined a career in farming. The farm was sold. The family moved to town.

Though the crisis ended several years later, the experience was a seed for Henderson.

“That’s what I grew up in,” he said. “It’s what shaped my world view.”

Initially he did not think his career path would intermix with ag. But while pursuing his master’s in economics at Purdue, he was drawn to rural development. He attributes the attraction to his upbringing.

“I got into ag because I wanted to answer two essential questions about the 1980s crisis: What caused it? And could something have stopped it?” he said.

He has been watching economic trends in ag ever since. His goal is to give people in rural communities the necessary information to make better decisions about their farms, ranches and businesses.

“I want to be able to provide them that ten thousand-foot view,” he said.

Understandably, for Henderson and others at the Kansas City Fed, the intellectual pursuit of the data is only one side of the double helix. The other side is the real-life connection.

“That personal side bubbles up,” he said.



SARA BRUNSVOLD, EDITORIAL ADVISER

COMMENTS/QUESTIONS are welcome and should be sent to teneditors@kc.frb.org.



Becoming a Conscious Consumer

Michele Wulff is a former public school educator of 30 years and a 2007 recipient of the peer award “Excellence in Teaching Economics.” As an economic education coordinator with the Kansas City Fed, she works to heighten financial literacy throughout the seven states of the Tenth District.

Picture a child on a shopping spree with a wad of holiday cash. Are you visualizing a thoughtful comparison shopper? One who buys store brands instead of designer labels? If the child is like most, just the opposite comes to mind: an impulsive spender looking to blow the bucks quickly on whatever appeals to him or her. And it doesn't help that the retail industry often promotes this reckless spending through their marketing to kids.



One of our tasks as parents or adults in children's lives is to teach them how to become conscious consumers. Being an aware and careful buyer is key to developing life-long responsible spending habits. If these habits are not instilled early, children may grow up purchasing luxuries first, with little left over

for necessities. And life on their own as adults could prove to be a financial nightmare.

So prepare to become a consumer coach and help kids practice conscious spending. Set the stage by teaching a little Economics 101: money is a scarce commodity. In other words, there is not enough money to buy everything they want. So kids must make wise choices in spending their cash to satisfy their wants. Those wise choices should be made on the basis of need first (such as jeans before a video game) And a portion of their income should be saved for the future—you never know what new needs may develop.

Before you head to the mall, take a time out to discuss some conscious consumer tips. Coach them by sharing the following ideas:

- Make a shopping list and stick to it. It will keep you from buying impulsively and having regrets later. Give a “buyer's remorse” example from your own life to make this point.
- Research the products you want to buy, either online, through ads, or in the stores. Do price comparisons to get the best value for your dollars.
- Set a budget or limit on the amount of dollars to be spent. Once you reach that magic number, you're done.
- Buy only items you love, so you will wear or use them over and over again. Just being “on sale” is not a reason to buy it.
- Do you need to buy it today? Really? If you can delay the purchase until next time, you may appreciate it more—and have money left for priority items today.
- When you buy products with designer labels, you are paying for the label as well as the product. Is it worth the price to you?
- Watch out for shopper's envy. Just

because your BFF has a new smartphone doesn't mean you have to buy one. Be an original shopper, rather than imitating others.

- Be aware of marketing tricks. If you have to buy two birthday cards to get one free, you now have three cards when you only needed one.

Now it's time to get in the game. Take your shopper out to practice his or her skills as a conscious consumer. Remember to lead by example. You should model responsible spending by following the coaching tips yourself. Point out situations where you're tempted to buy, but resist and practice being a

conscious consumer instead.

Realize that shopping mistakes may be made on the way to developing responsible spending habits. Conscious consumers are not built in a day. Keep reinforcing your coaching tips and watch for gradual improvement in financial decision-making. You'll know they've arrived when these new habits become second nature and they question YOU on a purchase.



Financial Education Resources

The Kansas City Fed is committed to promoting economic and financial literacy and greater knowledge of the Federal Reserve's role by providing resources for teachers, students and the public. Visit our website at KansasCityFed.org for more information.

Federal Reserve Resources

"Kids and Money: Teaching Children to Manage Their Finances"

This guide shares budgeting and smart shopping activities. For ages 6-12.

"Great Minds Think: A Kid's Guide to Money"

This booklet gives spending and budgeting tips. For ages 8-12.

Online Resources

"You Are Here"

A Federal Trade Commission website with a virtual mall where kids learn consumer concepts as they visit local businesses. For ages 10-14. (<http://www.ftc.gov/bcp/edu/microsites/youarehere>)

"Smart Shopping"

A website from the Mint that gives tips to teens on ways to stretch their dollar while shopping for clothes, entertainment, electronics and sporting goods. (<http://themint.org/tweens/smart-shopping.html>)

Fiction Books

"Pigs Go to Market" by Amy Axelrod

Mrs. Pig wins a shopping spree at the market. Will she and the piglets make wise shopping choices? For ages 4-7.

Nonfiction Books

"Smart Money Moves for Kids: A Complete Parent's Guide" by Dr. Judith Briles

This book helps parents teach the wise use of money to preschoolers through teens. It includes quizzes, games and money-smart activities. For adults.



Advertising in Action:

Take the Consumer Challenge

Conscious consumers need to be aware that advertisers use different approaches to persuade them to buy their products. Read each advertising approach below and give an example of a commercial or ad you've seen with this approach.

Celebrity Approach: This ad shows a famous person in TV, movies or sports using a product, such as a basketball star wearing a brand of athletic shoes.

My example:

Authority Approach: This ad shows a knowledgeable person, such as a doctor, advertising a product related to their occupation. For example: the best medicine for a headache.

My example:

Bandwagon Approach: This ad convinces you that everyone is using their product, so you should too. Computer or cellphone commercials often use this bandwagon approach.

My example:

Quality Comparison Approach: This ad compares two products and gives reasons why one is better than the other. Car or truck commercials often use this comparison approach.

My example:

Extra Consumer Credit: Find examples of each approach in magazines or newspapers and cut them out to make a "consumer collage!"

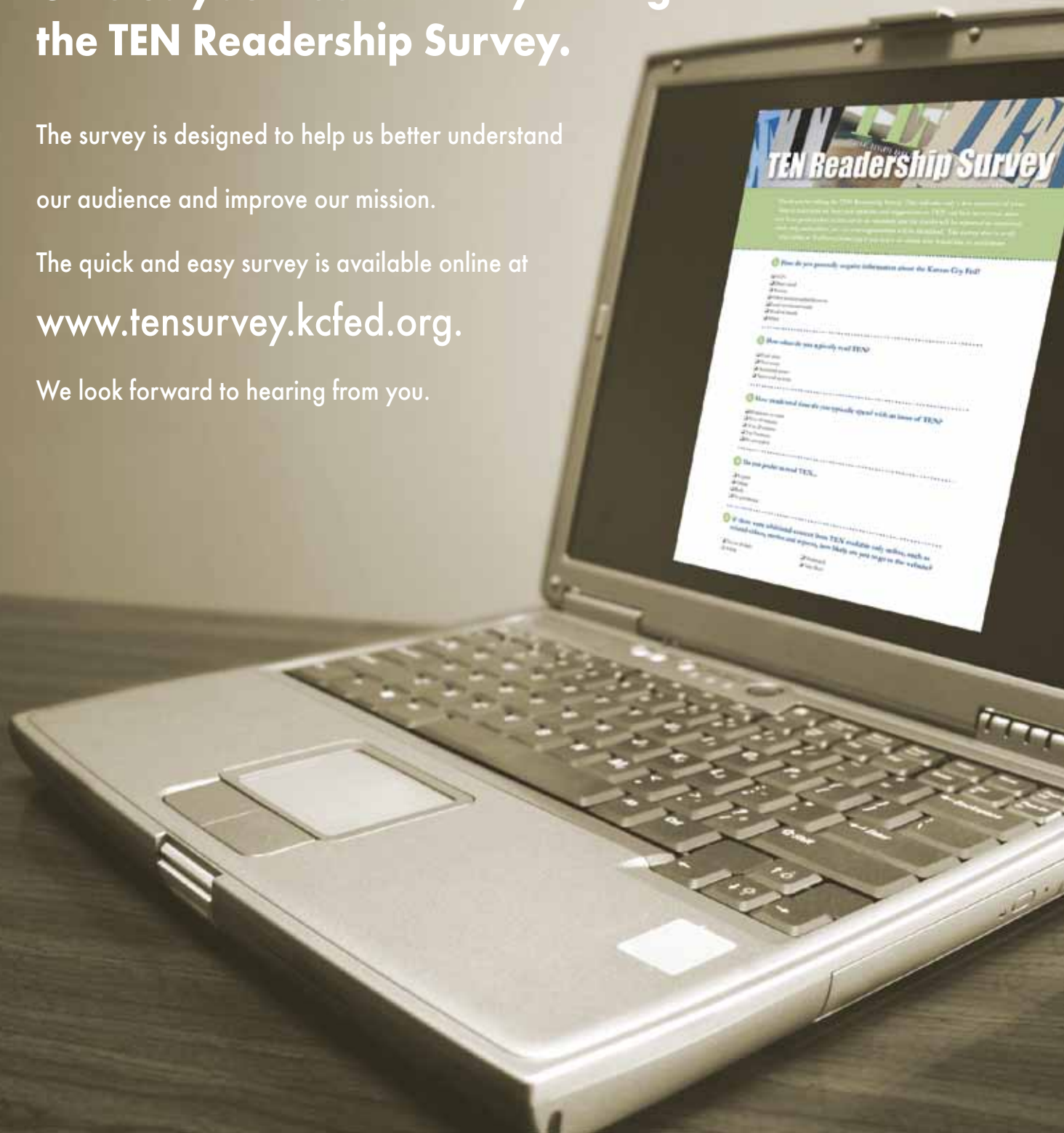
TEN Readership Survey

Give us your feedback by taking the TEN Readership Survey.

The survey is designed to help us better understand our audience and improve our mission.

The quick and easy survey is available online at www.tensurvey.kcfd.org.

We look forward to hearing from you.



2012-13 Student Board of Directors program begins

The Kansas City Fed has begun its 2012-13 Student Board of Directors program and has expanded it this year to three additional Tenth District cities: Denver, Oklahoma City and Omaha. The goal of the Student Board of Directors program is to propel students forward in their personal and professional growth, while equipping them with knowledge and understanding of the Federal Reserve and its functions.

The Kansas City Fed launched its Student Board of Directors program in 2011 with 24 Kansas City high school students. A total of 44 students from the Kansas City, Kan., Kansas City, Mo.; Omaha; Oklahoma City; and Denver public school systems will participate in this year's program.

The students meet monthly throughout the academic year to learn about the Kansas City Fed and participate in financial education lessons. Additionally, students attend sessions about career paths and tour area businesses to learn more about the local economy.

“We are pleased to be able to offer this program to an extended group of young people,” said Kansas City Fed Vice President Krissy Young, who oversees the program. “The strength of this program comes from the access the students have to experts at the Federal Reserve Bank of Kansas City who act as mentors and provide perspective to help them prepare for college and their futures.”



Federal Reserve unveils new Financial Services strategic plan

The Federal Reserve System recently rolled out a new four-year strategic plan that focuses on the Fed's goals in light of the changing payments landscape. The plan is an update to previous plans, the first of which was released in 1995.

In accordance with the plan, the Kansas City Fed will continue to advance its long-standing financial services mission, acting as service provider and balancing service enhancements with safety and security to maintain public confidence in the U.S. payments system. The Fed also will continue to recover costs for each service.

If the plan is successful, by 2016, the following progress will have occurred:

- The large-scale technology projects in Check, FedACH[®], Fedwire[®] and FedLine[®] will have been successfully completed and implemented, providing flexible and efficient platforms for innovative product development that support continued payments evolution.

- Long-term cost recovery will be met through aggressive cost management, delivery of new products and services that are responsive to customer demand and effective marketing, pricing and sales efforts.

- Reserve Bank operations and infrastructure, as well as the end-to-end payments infrastructure, will remain secure and resilient in spite of escalating cyber threats.

- Significantly more payments will become digital end to end, and a much higher proportion of these will be same-day or real-time. The migration of business-to-business and person-to-person payments from paper to electronics will have accelerated.

- The migration of government payments and collections from paper to electronics will be substantially complete.

Visit the Federal Reserve Financial Services website, www.frbsservices.org/communications/index.html for more details.



New members join Kansas City Fed's boards of directors

The Kansas City Fed recently announced the appointments of new directors on its Kansas City head office and branch boards of directors.

The Board of Governors of the Federal Reserve System appointed the following to the Kansas City head office board: Steve Maestas, managing partner of NAI Maestas and Ward Commercial Real Estate, Albuquerque, N.M., was appointed for a three-year term; and Rose Washington, executive director of the Tulsa Economic Development Corp., Tulsa, Okla., was appointed for an unexpired portion of a three-year term ending Dec. 31, 2013. The Board of Governors also designated Barbara Mowry, CEO of GoreCreek Advisors, Greenwood Village, Colo., as chair of the Kansas City Fed's board and Maestas as deputy chair for 2013.

At the Denver Branch, Lilly Marks, vice president for health affairs at the University of Colorado and executive vice chancellor of the Anschutz Medical Campus, Aurora, Colo., was appointed to serve a three-year term ending

Dec. 31, 2015.

At the Oklahoma City Branch, Paula Bryant-Ellis, chief operating officer, BOK Financial Mortgage Group, Tulsa, Okla., was appointed to serve an unexpired portion of a three-year term ending Dec. 31, 2013, and Michael C. Coffman, president and CEO of Panhandle Oil and Gas Inc., Oklahoma City, Okla., was appointed to serve a three-year term ending Dec. 31, 2015.

At the Omaha Branch, Anne Hindery, chief executive officer of the Nonprofit Association of the Midlands, Omaha, was appointed to serve an unexpired portion of a three-year term ending Dec. 31, 2013, and Brian Esch, president and CEO, McCook National Bank, McCook, Neb., was appointed to serve a three-year term ending Dec. 31, 2015.

Members of the Kansas City Fed's head office and branch boards of directors represent the Tenth Federal Reserve District: Colorado, Kansas, western Missouri, Nebraska, northern New Mexico, Oklahoma and Wyoming.



MICHAEL COFFMAN



PAULA BRYANT-ELLIS



BRIAN ESCH



ANNE HINDERY



STEVE MAESTAS



LILLY MARKS



ROSE WASHINGTON



Federal Reserve Consumer Help celebrates five years

Consumers need a resource to turn to when they have questions about their financial institutions. The Federal Reserve System addressed this need when it created Federal Reserve Consumer Help five years ago. The function streamlines the intake of consumer complaints and inquiries.

Federal Reserve Consumer Help is a joint effort of the Kansas City and Minneapolis Feds. More than 200,000 consumers have contacted the service since its inception on Oct. 7, 2007. Staff assist with specific consumer compliance protection laws and regulations, quality reviews, and complaint processing. The staff also directs consumers with complaints to the proper federal or state regulators.

The callers help the Federal Reserve, too. Consumer complaints and inquiries provide a wealth of information to the Federal Reserve. They often reveal emerging consumer-protection issues and trends in banking practices. Some of the data has been used to determine areas of focus for consumer compliance examinations and identify topics for Federal Reserve System materials that educate consumers about trends in banking products and their rights.

Find out more at www.FederalReserve-ConsumerHelp.gov/

Kansas City Fed launches Pinterest account for economic education

Pinterest is the latest social media avenue for the Kansas City Fed to use in its outreach efforts.

The Kansas City Fed will use its new Pinterest site to raise awareness about free tools available from KansasCityFed.org, including lesson plans, personal finance tips, consumer education tools and classroom resources. The virtual outreach is part of the Kansas City Fed's commitment to promoting economic and financial literacy and greater knowledge of the Federal Reserve's role in the economy by providing resources for teachers, students and the public.

The organization is also active on Twitter, LinkedIn and YouTube.

View the Kansas City Fed's Pinterest account at www.Pinterest.com/KansasCityFed, or learn more about the Kansas City Fed's free economic and personal finance resources at KansasCityFed.org/education.



Kansas City Fed conducts Hispanic Roundtable

The Kansas City Fed brought together leaders from local Hispanic community organizations for a roundtable discussion in the fall. The goal of the roundtable was to better understand the growing Hispanic constituency in the Tenth District and how the Kansas City Fed can better serve them.

Eleven community leaders offered insight at the roundtable. Organizations represented include:

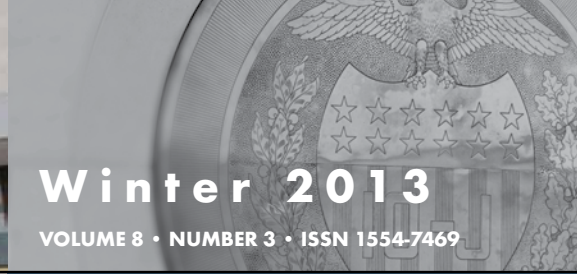
- Guadalupe Centers
- Kansas City Hispanic Chamber of Commerce
- Mattie Rhodes Counseling and Art Center
- LULAC National Educational Services Centers – Kansas City
- Westside Housing
- Brotherhood Bank
- Hispanic Economic Development Corporation
- Kansas City Chamber of Commerce
- Commerce Bank

“We are grateful for the participants taking the time to talk with us,” said Tammy Edwards, Kansas City Fed vice president and community affairs officer. “The roundtable was a first step in creating additional products and services for the Hispanic community. We have taken the insight to heart and will continue to work directly with these leaders and their peers to ensure we are filling gaps we have the capacity to fill.”



The following banks in the Tenth Federal Reserve District are celebrating one, five, 10, 20 or more years as Federal Reserve members in January, February or March.

Colorado B&TC of La Junta	La Junta	Colo.	89
Lusk State Bank	Lusk	Wyo.	79
St. Mary's State Bank	St. Mary's	Kan.	77
Community B&TC	Neosho	Mo.	71
Bank at Broadmoor	Colorado Springs	Co.	33
First State Bank	Wheatland	Wyo.	32
Freedom Bank of Oklahoma	Tulsa	Okla.	21
Centennial Bank	Centennial	Colo.	21
First Bank of Fairland	Fairland	Okla.	20
Auburn State Bank	Auburn	Neb.	10
Platte Valley Bank	Scottsbluff	Neb.	5
Interbank	Oklahoma City	Okla.	5
Tri-City Bank	Cheyenne	Wyo.	5
Verus Bank	Derby	Kan.	1



Winter 2013

VOLUME 8 • NUMBER 3 • ISSN 1554-7469

The Federal Reserve System

Congress created the Federal Reserve in 1913 to bring financial stability after a number of banking panics. It is the nation's third central bank. The first, established in 1791, and the second, created in 1816, were each operational for 20 years. In both cases, its charter failed to be renewed and the banks closed.

With the Federal Reserve Act, Congress sought to create a central bank the public would be more likely to support by making it "decentralized" with more local control. This new structure was designed to overcome one of the primary weaknesses of the previous central banks: public distrust of an institution that many felt could potentially be under the control of either government or special interests. The new central bank is a network of 12 regional Federal Reserve Banks, located throughout the country and under the leadership of local boards of directors, with oversight from the Board of Governors in Washington, D.C., a government agency.

The Federal Reserve is considered to be independent within government and broadly insulated from political pressures. While members of the Board of Governors are nominated by the president of the United States and confirmed by the Senate, the Federal Reserve's regional structure, including local boards of directors and advisory councils, ensures that views from a broad spectrum of the public nationwide contribute to the central bank's deliberations.

President Woodrow Wilson signed the Federal Reserve Act on Dec. 23, 1913, and the 12 regional Federal Reserve Banks opened on Nov. 16, 1914.

The Federal Reserve Bank of Kansas City

The Federal Reserve Bank of Kansas City and its Branches in Denver, Oklahoma City and Omaha serve the Tenth Federal Reserve District, which encompasses Colorado, Kansas, western Missouri, Nebraska, northern New Mexico, Oklahoma and Wyoming. As a part of the Federal Reserve System, the Bank participates in setting national monetary policy, supervising and regulating numerous commercial banks and bank holding companies, and providing other services to depository institutions.



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TEN magazine is a quarterly publication of the Federal Reserve Bank of Kansas City focused on the connection between the Bank's research and the Tenth Federal Reserve District. **TEN** also features articles on the Federal Reserve's history, structure and operations.

The views and opinions expressed in **TEN** are not necessarily those of the Federal Reserve Bank of Kansas City, the Federal Reserve System, its governors, officers or representatives.

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