

TEN

FEDERAL RESERVE BANK OF KANSAS CITY

Winter 2010

Inside:

Livestock producers struggle

Small banks, mortgage loans

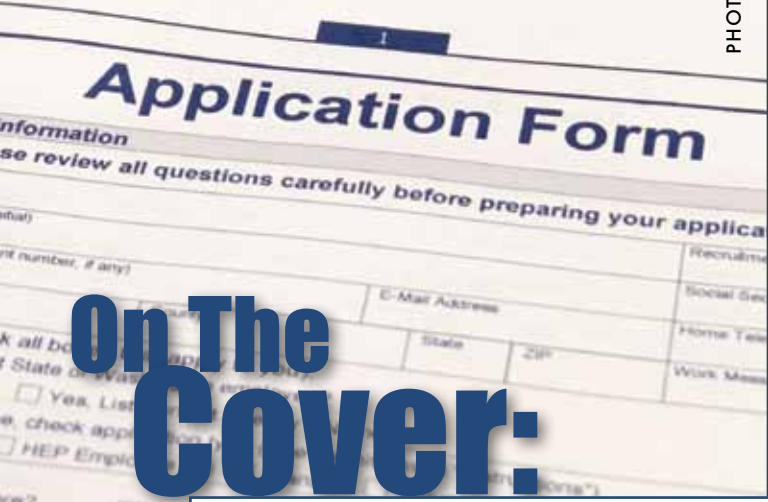
Middle-age workers boost rural economies

Voting with the FOMC

Financial resolutions help kids

LABORING TO RECOVER

As the nation's economy rebounds, unemployment continues to rise



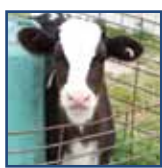
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The Federal Reserve Open Market Committee

On my first day on the job as president of the Federal Reserve Bank of Kansas City, Oct. 1, 1991, I was a participant at the Federal Reserve's Federal Open Market Committee (FOMC) meeting, and that following January, I was a voting member. As prescribed by a rotating schedule of votes, I have voted every three years since then. In 2010, in an environment of unprecedented challenges, I will again be a voting member.

The Federal Reserve has three mission areas, each focused on financial stability—financial services, banking supervision and regulation, and monetary policy. Though the Federal Reserve's broad role in monetary policy is well-known to the public, the regional Reserve Banks' role in monetary policy is less well-known or understood.

In some way this lack of understanding is not surprising as it contrasts with the Reserve Banks' local business activities. For example, the connection between our regional Bank providing local financial services to commercial banks—including the processing of currency, providing transactions accounts and supporting interbank payments—seems natural. Similarly the value of the regional structure in our regulation and supervision of nearly a thousand banks and bank holding companies located within the Tenth Federal Reserve District is pretty basic.

But where the regional structure plays its most important role is in the formation of a national monetary policy that is based on local input. In various forums, including public speeches and in past editions of *TEN* magazine, I have discussed at length the important reasons behind the Federal Reserve's innovative regional structure that links the central bank's

national policy deliberations directly to the local communities we serve. This connection is crucial in preventing the Federal Reserve from becoming an "inside the beltway," Washington-based entity. In fact, the key reason for its design by Congress nearly a century ago was the recognition that an institution viewed as under the control of Washington

or Wall Street was not a central bank the public would trust to best serve the interests of the entire nation—as evidenced by two previous failed attempts to run a central bank from the then-power center of Philadelphia. The structure of the Federal Reserve System is truly a product of the populist movement. Although the world has changed much in the last 100 years, many argue this broad representation from across our nation is even more important today than it was at the time of the Federal Reserve's founding.

History

The FOMC is responsible for the Federal Reserve's open market operations, which is the most often used of the Federal Reserve's monetary policy tools. The FOMC's decisions about its target for the federal funds rate, which is the interest rate that depository institutions lend their balances at the Federal Reserve to other depository institutions overnight, are closely followed because of the impact they have on the broader economy. Moves in the federal funds rate eventually influence borrowing costs



for everything from credit cards to mortgages, which means they can either stimulate or slow the economy.

The structure of the FOMC was created by the Banking Act of 1935, largely through the work of then-Sen. Carter Glass. Although many individuals were involved in 1913's passage of the Federal Reserve Act—including Oklahoma Sen. Robert Owen—perhaps no individual is as readily identified with the nation's central bank as Glass. As a congressman, Glass was not only the House sponsor of the legislation that created the Federal Reserve, but also a key figure in its design. Later, in the mid-1930s as the nation was emerging from the Great Depression, Glass played the key role in making sure that the Federal Reserve's regional structure—its key strength—was utilized on what some consider its most important committee. In that battle, he faced some strong opposition from an unlikely source—one that was within the Federal Reserve.

Then-Federal Reserve Chairman Mariner Eccles wanted to consolidate control of the decentralized bank under his direct authority in Washington. Eccles saw the financial crisis as an opportunity. In his landmark history of the Federal Reserve, historian and economist Allan Meltzer writes that "Eccles wanted a central bank with authority concentrated in Washington, specifically in his hands."

Glass, meanwhile, argued that centralized control was an affront to the System, designed and approved by Congress and signed by President Woodrow Wilson. Glass, it seems clear, recognized the extreme risks of such a consolidation. World history has shown time and again that monetary policy, when it is linked too closely to the political process,

becomes an extremely seductive tool for elected office holders. The lure of creating an artificial economic boom for a short-term boost in the polls is powerful and often overwhelms concerns about long-term economic consequences.

The battle between Glass and Eccles came to something of a head when Eccles testified before Glass' Senate Committee. Glass and Michigan Sen. James Couzens both asked Eccles repeatedly how the centralization he favored would have helped the nation when the stock market collapsed and the Great Depression began to take shape. Eccles was unable to come up with a response to the question and later wrote a letter admitting that the powers would not have made a difference in 1929.

In addition to making sure the regional banks had a voice in open market operations, Glass also made sure that the individuals who provided that voice—the regional Reserve Bank presidents—were free of Washington influence. At Glass' direction, the 1935 Act includes language that says the regional Federal Reserve Bank Boards of Directors, who come from local communities within each District, appoint presidents and other officers of their respective Federal Reserve Banks.

Structure

By design, there are 12 members who vote at each FOMC meeting; they include all seven members of the Federal Reserve's Board of Governors as well as presidents from four of the 11 regional Federal Reserve Banks on a rotating basis. The New York Federal Reserve president was designated as a permanent voting member of the FOMC on the premise that it has a special role in the markets. This structure

carefully balances public and private interests by giving a majority of the 12 votes to the seven Federal Reserve governors, who are presidential appointees who have been confirmed by the Senate. In recent history, however, that has not been the case. Due to a lack of presidential appointments, there has not been an FOMC meeting involving seven governors for almost five years, and for much of the time since spring 2005, the Board of Governors, which also has broad oversight for the entire Federal Reserve System, has had two vacancies.

The intent of the lengthy terms of the governors (14 years for members and four years for the chairman and vice chairman) and the independent status of Reserve Bank boards and presidents provides the System with a needed degree of independence to resist pressure for

short-run decisions based on Washington's two-, four-, and six-year election cycles. The central bank must be free to make decisions that it judges to be in the long-run best interest of the national economy.

Media coverage of the regional Reserve Bank presidents often notes if they are a "voter" or "non-voter" on the FOMC. In terms of policy deliberations, the distinction between the two is perhaps less substantial than some might assume.

All Federal Reserve Bank presidents participate in all FOMC meetings. Both voters and non-voters provide the committee with information about business activity within their regions. During the first of two go-rounds that are the key elements of each FOMC meeting, the presidents each provide



PHOTO BY BRITT LECKMAN

the full committee with a brief but important report on local economic conditions. These reports are based on firsthand accounts that the regional Reserve Banks receive from business and banking contacts within their Districts. Through their comments, the presidents weave an insightful tapestry of the U.S. economy for the FOMC. It is a picture that is more current than even the most recently available data, which can be weeks or even months old. Because this is firsthand information, rather than being backward looking, it is focused on immediate conditions and future concerns. Often, these accounts are the first indications of changing economic conditions or emerging issues. It is perhaps impossible to overstate the valuable role this insight can have in our policy deliberations.

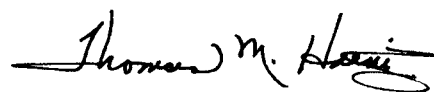
The regional Bank presidents, of course, offer much more to the monetary policy process than reports about their Districts. All members, regardless of voting status, analyze national trends and offer comments on the national and international outlook. They ask questions of other Reserve Bank presidents and the governors. And during a second go-round, each president discusses the possible policy action and has ample opportunity to offer his or her insights and opinions regarding policy to the full committee prior to the vote. All participants play a vital role in the process.

Voting

Having said all this, I do not want to downplay the significance of being a voting member. It is, in fact, among the key responsibilities of a regional Federal Reserve Bank president and it is certainly one of the most important components of our System.

There are some who believe very strongly that the Federal Reserve must always present a united front in terms of policy action or risk weakening its stature. I strongly disagree with that position, and the structure supports my position.

If there was no room for dissent, then why would the FOMC vote on policy actions? If the goal was to keep differences in opinion a private matter, why would the outcome of those votes be made available to the public? The Federal Reserve's founders, as well as those members of Congress involved in forming the FOMC during the crisis of the 1930s, recognized that an institution with room for dissent and a willingness to entertain contrasting opinions is stronger overall and more worthy of public trust. Although these disagreements or dissenting votes may be portrayed by Federal Reserve watchers as signs of weakness or a struggling central bank, to me they are a mark of strength and evidence that the system is functioning exactly as it was designed.



THOMAS M. HOENIG, PRESIDENT
FEDERAL RESERVE BANK OF KANSAS CITY

For more information, read:

- "Presidents, Governors & the FOMC: Regional Bank Leaders Provide Long-term Stability"
 - "Twelve Banks: The Strength of the Federal Reserve"
 - "The Federal Open Market Committee"
 - "The Balance of Power: The Political Fight for an Independent Central Bank"
- KansasCityFed.org/TEN

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Laboring to recover

As the nation's economy rebounds, unemployment continues to rise



Although John-Paul Maxfield lost his job at a private equity firm during the most severe economic recession of his lifetime, the 29-year-old has a different view than most who have also been looking for work in the midst of escalating unemployment.



his is the best thing that's ever happened to me," Maxfield (pictured left) says. "In this recession, I saw an opportunity."

After weeks of scouring a "dismal job market" in the fall of 2008 didn't turn up any interviews, Maxfield tried a new approach: "I was writing my business plan at night and searching for work during the day."

He was told he was crazy to start a business in such an economy, but Maxfield cashed in his retirement fund; traded his Volvo for a truck; and, by February '09, opened Waste Farmers, a commercial recycling and composting business in Denver.

So far the operations are small—just Maxfield; his wife, Carrie, who is a third-grade teacher; and his business partner. Clients include hospitals, hotels, schools and the like. Maxfield not only wants to expand the business, but also change the way companies handle their waste, which often can be recycled rather than dumped in a landfill. He wants to make a difference.

Still, with Waste Farmers less than a year old, Maxfield's entrepreneurial vision is lined with a little self-doubt about being his own boss.

"I put everything we have into this business," he says.

And times are tough. It is uncertain how quickly jobs lost during the most recent recession will come back—or whether some of those lost jobs will ever return. Although Federal Reserve Chairman Ben Bernanke said in mid-September the downturn was "very likely over," he added that "it's still going to feel like a very weak economy for some time."

By November—almost two years after the recession began in December '07—the unemployment rate was 10 percent, according to the Labor Department. The typical rate of unemployment when the economy is not in recession is about 5 percent.

It may seem counterintuitive that the economy is rebounding yet unemployment continues to rise. The economy and unemployment have recovered simultaneously

following some past recessions—but not all, says Ed Knotek, a senior economist at the Federal Reserve Bank of Kansas City, who recently researched how unemployment will fare in the aftermath of the most recent recession. He examined changes in the labor market during the past 20 years and the effects of banking crises on unemployment.

“These two factors raise the likelihood that unemployment will recover much more slowly this time compared with past severe recessions,” Knotek says. “For some workers, this may mean a longer period of unemployment, especially for those looking for employment in a new field. For others, this could mean postponing retirement and staying in the workforce longer.”

Many are trying to make the most out of a bleak situation. Data for the past few years show increased enrollment at community colleges and more small-business start-ups, like Waste Farmers.

“It’s all about perspective,” Maxfield says. “Challenging times are opportunities.”

A look back

Historically, severe recessions were followed by strong recoveries and mild recessions were followed by weak recoveries.

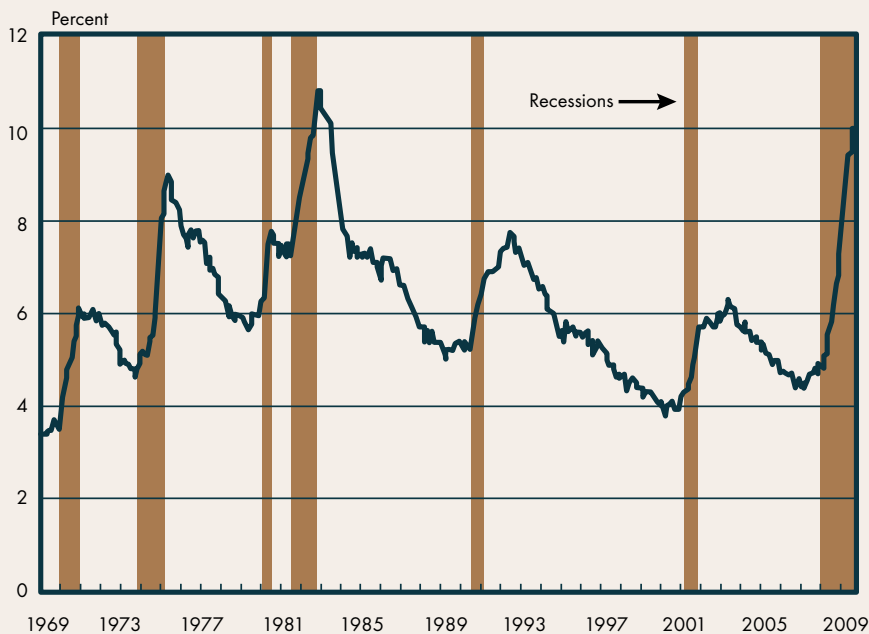
“In general, the more unemployment increased during a recession, the more it fell the year afterward,” Knotek says.

In many ways, the most recent recession has been similar to two of the most severe U.S. downturns: the recessions of 1973-75 and 1981-82. Each of these three recessions:

- lasted longer than the average downturn of 10 months;
- experienced greater drops in the nation’s gross domestic product (GDP) than the average 1.7 percent decline; and
- saw strong increases in unemployment during the recession.

“Following the recessions of ’73 and ’81, unemployment fell sharply within a year after the recession’s end and then drifted down slowly for several years,” Knotek says. “These similarities could mean unemployment will

U.S. Unemployment Rate



The nation’s jobless rate was 10 percent in November 2009, according to the Labor Department. Although the economy is thought to be recovering from the recession that began in December 2007, unemployment is still on the rise. In the aftermath of past severe recessions, the economy recovered quickly and unemployment declined quickly. This time may be different because of changes in the labor market and the coinciding banking crisis.

take a similar path during this recovery. But there are other factors affecting unemployment, too.”

Changes in the labor market

The two recessions prior to this one (in 1990-91 and 2001) raise the possibility that unemployment is less likely to fall quickly during the current economic recovery.

“Changes in labor markets since the 1980s may have altered the behavior of unemployment after recessions,” Knotek says. “This could be something unique to these two recessions, or a new trend.”

During the '90 and '01 recessions, unemployment continued to rise substantially long after the recessions ended and GDP resumed growing. An economic recovery paired with an increase in unemployment—known as a jobless recovery—may occur for several reasons:

- Long economic expansions—such as those during the '80s and '90s—give businesses incentives to delay organizational restructuring until the next recession. Because the '90 and '01 recessions were relatively short, firms may have needed more time to complete their restructurings, leading to a period in which unemployment was still increasing even though the economy had resumed growing.

- Mild recessions, like those in '90 and '01, are often followed by weak recoveries.

- Labor market trends since the early '80s—including shifting from temporary to permanent layoffs, and relying more on overtime, part-time and temporary workers as well as outsourcing—have made firms more cautious to hire permanent, full-time workers following recessions.

“The nature of layoffs distinguishes recent recessions from earlier ones,” Knotek says. “During the three most recent recessions, layoffs have been mostly permanent whereas earlier recessions experienced a split between permanent and temporary layoffs.”

This is significant because unlike temporary layoffs, permanent layoffs can't be



reversed quickly, which delays hiring during a recovery as firms search for new employees. An increase in permanent layoffs can slow the overall recovery because consumers, especially those who aren't working, will be cautious with their spending.

“However, in spite of the parallels between the most recent and past recessions,” Knotek says, “one key difference remains: the ongoing banking crisis.”

Banking crises, looking abroad

The most recent recession is somewhat unique for the United States because it coincides with a banking crisis. Because this country has not had many banking crises (the most recent was the less severe credit crunch during the Savings and Loan Crisis in the '80s and the Great Depression decades earlier), Knotek took a look at unemployment in the aftermath of banking crises in many foreign countries.

“Looking abroad, banking crises that coincide with recessions typically have an even worse outcome for unemployment than other recessions,” Knotek says.

The United States' experience somewhat resembles those of other countries in that they

were preceded by easy access to credit, high levels of consumer spending, low levels of personal saving and fast asset appreciation. Once the crisis hit, these imbalances reversed, and the countries saw large increases in unemployment for some time after the downturn. For example, in Sweden after a severe banking crisis in the early '90s, unemployment increased by 8 percentage points and remained high for 10 years.

Banking crises tighten access to credit, which may prompt businesses to conserve cash flow, in part, by not rehiring permanent employees although the economy is showing signs of recovery. Knotek explains that from a household perspective, the loss of wealth not only means reduced consumer spending and a slower recovery, but also may mean a delay in retirement in some cases. This, in turn, doesn't

free up jobs for new workers, who already face reduced hiring in general.

Effects

More than seven million jobs have been lost nationwide since the beginning of the recession. In the Tenth Federal Reserve District, which includes western Missouri, Nebraska, Kansas, Oklahoma, Wyoming, Colorado and northern New Mexico, major employers were no exception. Sprint Nextel Corp., based in Overland Park, Kan.; Harley-Davidson Inc., which has a plant in Kansas City; Colorado computer technology company Sun Microsystems Inc.; and Tulsa-based aerospace manufacturer NORDAM Group recently have all laid off workers.

Analysts say some jobs are gone for good. Others that have proven strong historically, like

SUSAN AND RON BRUNSVOLD shop for Christmas gifts for their grandchildren at U.S. Toy in Leawood, Kan. The couple is cautious with their spending, diligently budgeting and waiting for sales. Ron retired prior to the most recent recession, but after the downturn began and their savings took a hit, Susan, 66, decided to delay her retirement. "I think there's a lot of people hanging on a little longer, just waiting to see what will happen with the economy," she says.



health-care and education positions, likely will continue to grow, and sectors that have taken a hit, such as construction, may take years to recover. Many are waiting out the job market slump as students, or have returned to the classroom with the intent to switch fields.

In Kansas City, Mo., enrollment at the Metropolitan Community College's five campuses increased by 10 percent this fall, says Tom Vansaghi, associate vice chancellor of college and community relations. The student body is nearly 19,000.

"We've experienced across the board increases in all of our programs, but mostly general education, or the classes that students would transfer to a four-year university," he says. "Because of budget cuts, we weren't able to hire any full-time staff, but we have hired additional adjunct faculty to teach the additional classes."

Others are trying self-employment. The number of new business start-ups increased in 2008 from the year prior, according to research from the Ewing Marion Kauffman Foundation. However, according to the Small Business Administration, the majority of existing small businesses report declining profits.

And for some, economic conditions are keeping them punching the clock after they had planned to retire. According to the U.S. Bureau of Labor Statistics, two-thirds of those ages 55 to 64 currently are in the workforce. This is the highest rate since the bureau started tracking in 1948.

Years ago, 66-year-old Susan Brunsvold of Topeka, Kan., thought she would've retired from her job as a service representative with AT&T by now. But that could still be months or even years away.

"After the stock market really started to tank, we lost about a third of what we had saved," Brunsvold says. "So why leave (the workforce)? It's about finances, plain and simple."

That means not joining her husband, Ron, who retired prior to the recession, and postponing her plans to spend extra time with

their grandchildren, or other activities she enjoys, like sewing, knitting and reading.

Meanwhile, Brunsvold carefully spends discretionary money, actively manages the couple's stock portfolio and dutifully stays apprised of the economic climate. She says she's not bitter though.

"I would rather be in this job than out and looking" for work.

What lies ahead?

Considering the length, depth and breadth of the most recent recession, the downturn has been severe, although it is likely over, Knotek says. However, two factors—labor market trends and international evidence on banking crises—suggest that unemployment could remain high as the economic recovery progresses.

He projects unemployment will continue to rise into 2010 and drift down a little in 2011 before the recovery begins to pick up speed. However, unemployment may not return to pre-recession levels until 2015 or later. That said, several factors could expedite the turnaround: the United States' labor market is more flexible than that of other countries; the government's fiscal and monetary response have been considerable; and jobless recoveries after a recession are a relatively new phenomenon.

"Still," Knotek says, "it's likely the labor market is on a long road to recovery."



BY BRYE STEEVES, SENIOR WRITER

FURTHER RESOURCES

"HOW WILL UNEMPLOYMENT FARE FOLLOWING THE RECESSION?"

By Edward S. Knotek II and Stephen Terry
KansasCityFed.org/TEN

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

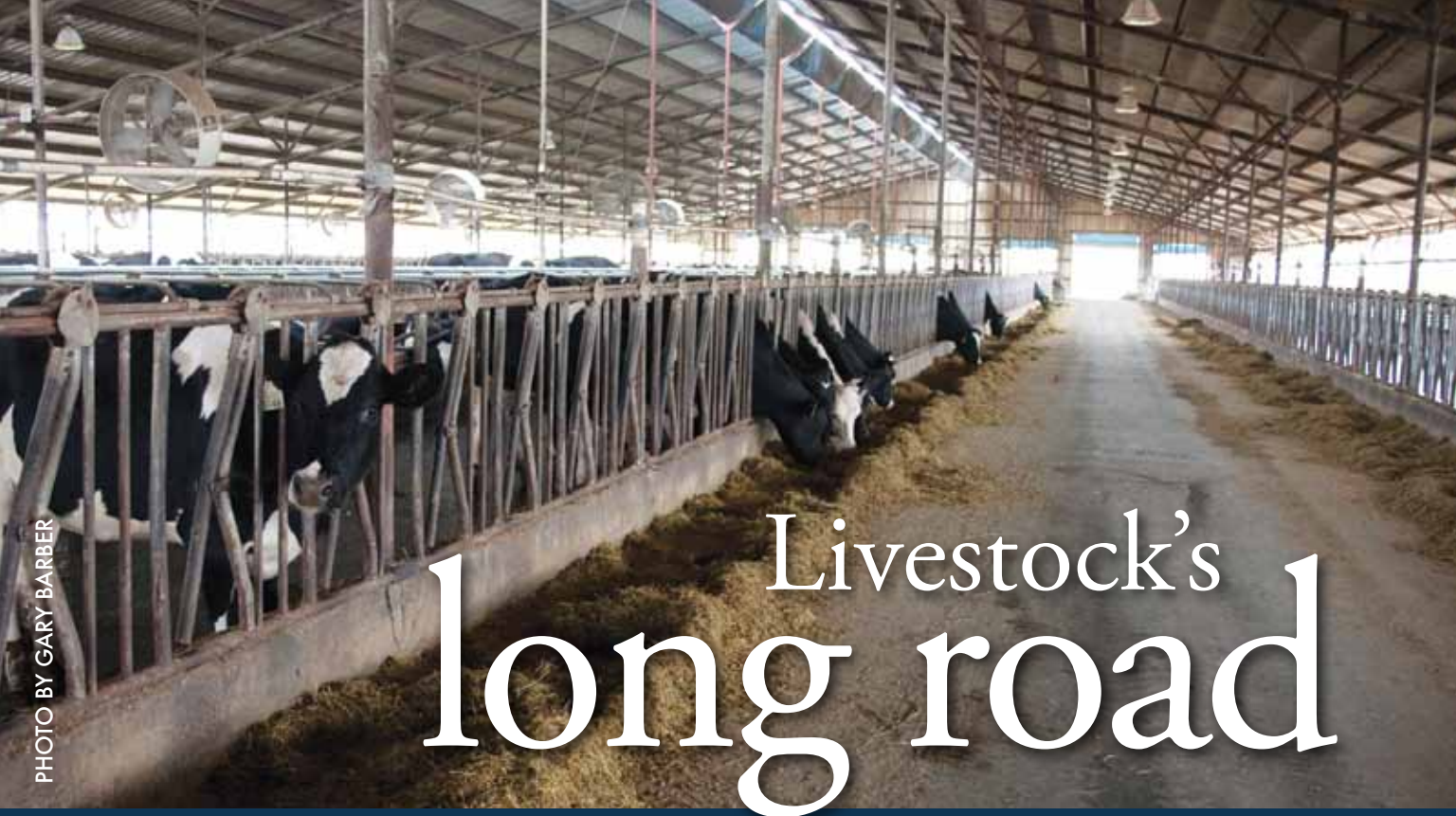


PHOTO BY GARY BARBER

Livestock's long road

Recession, global pullback weigh on producers

Last summer on a road trip to sell pure-bred Holstein bulls, Steve Strickler saw many reminders of the new pressures faced by livestock and dairy producers.

On a single rural highway in western Kansas, Strickler counted four bankrupt dairy farms. Across the state border, the story was similar: At least six dairies in Colorado had also recently declared bankruptcy.

A dairy farmer himself, Strickler has personally experienced the toll of rapidly declining milk prices, rising feed costs and weaker consumer demand caused by the recession. The market pressures are hard to avoid, but by selling bulls to other farmers, he has been able to limit some of the pain.

"It just drove home once again how dire the situation is," Strickler says of the bankrupt dairies. "So much has changed in just the last couple of years. 2007 was one of our best years, and 2009 is easily the worst."

At Strickler's dairy farm in Iola, Kan., the numbers tell the story. Last fall, he estimated

that it cost his farm about \$15 to produce one unit of milk, known as a hundredweight. With market prices topping out at \$13 per hundredweight at the time, Strickler has been forced to find innovative ways to deal with his farm's losses.

"I'm lucky that I have another source of income by merchandising bulls, but even that market has been severely impacted," Strickler says.

Similar declines across the livestock industry last year also have put hog and cattle producers in a tough spot, with many operations going out of business or taking losses that can add up to thousands of dollars a day.

For farmers like Strickler, who are used to dealing with the ups and downs of the agricultural market, the sudden disappearance of profits has been a unique challenge complicated by the recession and shifting consumer patterns, according to Brian Briggeman and Jason Henderson of the Federal Reserve Bank of Kansas City.

Briggeman, an economist at the Bank's Omaha Branch, and Henderson, an economist, Omaha Branch executive and vice president, recently explored the problems livestock producers face as they deal with higher production costs and lower demand.

"The livestock industry's profitability has really taken a hit in the last year," Briggeman says. "The likelihood of sluggish consumer spending coming out of the recession could be another issue for livestock producers in the near future."

During past recoveries, it has taken a while for protein consumption to bounce back, Henderson says.

"That could also be the case this time because there have been fundamental changes in the labor market, forcing people to change their protein consumption by choosing lower-cost products," he adds. "Slower income gains and higher unemployment levels are limiting U.S. consumption."

According to the economists, the best opportunity for U.S. producers to capture new profits lies in rising global demand.

Vanishing profits

As recently as 2007, livestock producers enjoyed strong profits as protein demand increased worldwide amid balanced supplies. Dietary fads, such as the low-carb Atkins Diet, boosted consumer spending on red meat. Meanwhile, rising incomes in developing countries pushed worldwide demand for protein higher as consumers in countries such as China, India and Brazil spent more on meat products.

Livestock producers responded by increasing their production, Briggeman and Henderson found. According to the U.S. Department of Agriculture, red meat and poultry production rose 10 percent from 2004 to 2008, while milk production rose 11.2 percent during the same period.

Unfortunately for livestock producers, the peak came just when the recession arrived. In 2009, U.S. consumer spending on food items

fell 1.5 percent as consumers spent less on food away from home. For livestock producers, the decline in consumer spending on beef, pork, poultry and milk was slightly larger at 1.65 percent.

Livestock producers also had to deal with a decline in export volume as the recession's effects were felt worldwide. In the first five months of 2009, meat and dairy exports fell 23 percent from a year earlier.

Another factor that came into play last spring was the rise in fears related to the H1N1 virus and its associated name, "swine flu." In the spring of 2009, China banned U.S. imports of pork based on the belief that the virus can be transmitted by eating contaminated pork products. No link has been found, and in late October, Chinese officials agreed to lift their pork ban. But the damage was done.

"The weak demand and oversupply resulted in many producers operating in the red throughout 2009," Briggeman says. "Livestock prices dropped below break-even levels, and profits vanished."

Producers also faced higher input costs, especially for feed. Rising crop exports and higher demand for corn to produce ethanol helped push feed costs up 48 percent above 2007 levels. The combination of higher feed costs, lower exports and declining domestic demand resulted in what Strickler calls a "triple whammy."

"The feed cost is really something that seriously impacted us," Strickler says. "It's probably about 50 percent of the total production cost. It really hurt."

Herd liquidation

At the Klausmeyer Dairy Farm southwest of Wichita, Kan., school buses drop off children during the week to give them an idea of a working dairy farm. The children can watch cows getting milked and take turns feeding baby calves.

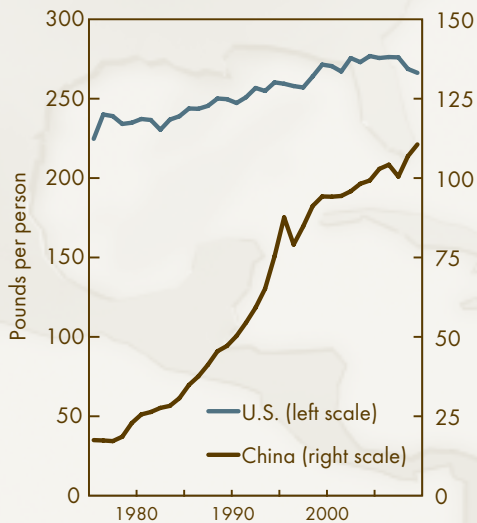
The tours provide a welcome second source of income for owners David and Debbie Klausmeyer. David has been working on dairy



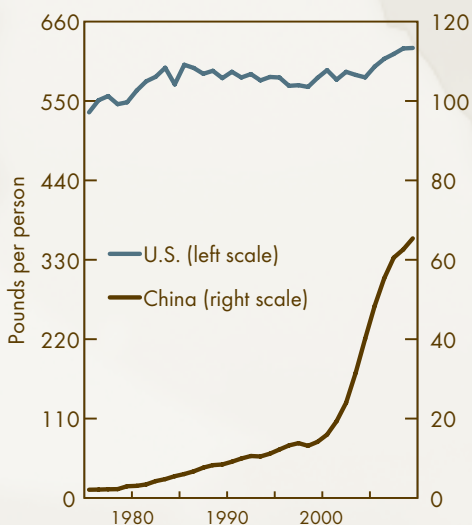
U.S. and Chinese consumption of meat and milk

While consumption of protein and milk has fallen in the United States because of the recession, consumer demand for such products continues to grow in China, providing an opportunity for U.S. exporters.

Beef, Pork and Poultry Consumption



Milk Consumption



Source: Calculations based on Foreign Agriculture Service data.

farms for as long as he can remember.

“The market has been pretty hard on us,” David Klausmeyer says. “I did away with any hired help and do the milking by myself. The tours are basically keeping us above water.”

The Klausmeyers have also been forced to liquidate some of their herd. The farm’s herd has dropped from about 90 head of cattle to 60 in the last year.

“We’ve culled real hard since the milk prices have gone down,” David Klausmeyer says. “The fact is, until the industry gets rid of more cows, the production is going to be too great.”

According to Briggeman and Henderson’s research, the livestock industry has been cutting herds steadily since the downturn began. The number of cattle being fed has declined 6.6 percent, according to one recent estimate, while the number of hogs used for breeding is down 2.7 percent.

A dairy industry program called Cooperatives Working Together has been focused on buying cows from producers in an attempt to remove some of the oversupply in milk production. In four herd-retirement auctions since June 2008, the program has removed more than 250,000 cows representing some 4.8 billion pounds of milk production. The program announced another herd retirement last fall and says it is starting to make an impact on the dairy market.

“Those efforts have helped adjust the supply of milk more in line with demand,” says Jerry Kozak, president and CEO of the National Milk Producers Federation, which manages Cooperatives Working Together. The herd retirements “along with a stabilizing global economy should further accelerate the recovery in dairy farmers’ prices.”

But despite the production cuts so far, more may be needed.

“The herd and flock liquidations have helped narrow losses,” Henderson says. “But analysts are suggesting that more cuts need to be made, especially in dairy and pork production.”

Overseas opportunities

Briggeman and Henderson say the biggest opportunity for a return to profitability in the livestock industry likely lies overseas, as developing countries are set to experience stronger gains during the economic recovery. Much of these gains will be felt in the countries' middle class populations, which bodes well for protein consumption.

"For example, China has seen a rapid rise in its median income, and that has coincided with consumers adding more protein to their diets," Briggeman says. "If China and other developing countries grow as expected, they will outpace their livestock production capacity, leading to export opportunities for U.S. producers."

But as the effects of China's ban on U.S. pork products show, capitalizing on those potential export opportunities could be difficult in practice. Briggeman and Henderson say several trade barriers related to food safety still pose an obstacle for U.S. producers.

The H1N1 scare last year wasn't the first health-related problem for U.S. livestock exporters, Henderson says. In 2003, Mad Cow Disease was found in a slaughtered dairy cow, closing off some foreign markets to U.S. beef.

"The markets were slow to re-open afterward, and the demand for U.S.-produced beef slowed significantly in foreign markets," Henderson says.

Organizations such as the Denver-based U.S. Meat Export Federation (USMEF) have been working to promote U.S. livestock as safe and healthy in foreign markets. Earlier in 2009, the USMEF sponsored a trip to South Korea and Japan to help Midwest cattle farmers connect with distributors, packers and retailers in those countries.

David Hamilton, a beef producer from Thedford, Neb., traveled with the group as a representative of the Nebraska Beef Council. He says Japanese consumers seem to have accepted American beef as safe, but there are still challenges in South Korea.

"Their impression (in South Korea) is that we export different beef than we feed to our

own families, which is obviously not the case," Hamilton says.

However, Hamilton still sees "tremendous potential for beef sales" in Asian markets, including South Korea, as Asian consumers learn more about American beef.

Henderson and Briggeman say the livestock industry has previously found innovative ways to meet changing consumer tastes in the United States, such as offering pre-packaged and pre-cooked meals. That drive to find solutions seems to be taking hold in overseas markets as well.

In Japan, the recession has led to an increase in the popularity of bento boxes, which are quick and affordable lunches sold in Japanese convenience stores. With the help of the USMEF, American beef has become a main ingredient in these products, providing a new export market for producers and helping to re-establish Japanese consumers' trust in American beef.

"There are challenges for producers trying to compete in a global market, and producers can penetrate foreign markets by targeting global tastes," Henderson says. "The opportunities exist, but the industry must continue to create new products for new consumers."



BY BILL MEDLEY, SENIOR WRITER

FURTHER RESOURCES

"THE SLOW ROAD BACK FOR THE U.S. LIVESTOCK INDUSTRY"

By Brian Briggeman and Jason Henderson
KansasCityFed.org/TEN

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



Coming home

Resurgence of working-age residents
may boost rural economies



When Kara Weander-Gaster left rural Nebraska in her early 20s for New York, she vowed she'd never live west of the Mississippi River again.

“I was looking for something bigger. I wanted to go out and see the world a little,” she remembers. “I loved where I grew up, but I didn't feel like it had anything for me.”

Headed to grad school to study art history, Gaster craved the culture she thought only a bigger city could offer her. Eventually she found exactly what she was looking for—and more—right back in Norfolk, Neb., as one of its 25,000 residents.

Now, at 37 with a husband, two daughters and a career as the executive director of the Norfolk Arts Center, Gaster (pictured left) says, “I can't imagine ever leaving again.”

Young adults moving out of their rural hometowns certainly isn't a new phenomenon, but the growing number returning later in life—and the economic implications—may be. Recently, the region has seen a resurgence of older residents, which could rejuvenate small-town economies that have long struggled with dwindling populations, says Jason Henderson, an economist and vice president at the Federal

Reserve Bank of Kansas City's Omaha Branch.

Migration patterns shape the economic growth potential of communities. The out-migration of young adults, especially those with higher levels of education, cuts a community's economic potential by shrinking the supply of workers and, more importantly, by reducing productivity when they take their skills elsewhere. However, the return of middle-aged workers can help offset these challenges. Not only do they boost the number of working-age residents, but also bring knowledge, experience and connections that can enhance productivity gains.

Henderson, who also oversees the Omaha Branch as its executive officer, and assistant economist Maria Akers recently researched these migration patterns and their economic effects for rural communities in the Tenth Federal Reserve District. This area

includes western Missouri, Nebraska, Kansas, Oklahoma, Wyoming, Colorado and northern New Mexico.

“Rural areas will likely always be challenged by an aging population and loss of young adults,” Henderson says, “but the in-migration of middle-aged residents—and the skills and the family members they bring—raises a new question for economic development: Should rural America focus on recruiting these residents to their communities?”

Henderson and Akers’ research shows counties with high populations of retirees often have slow economic growth as the workforce there shrinks and young workers move elsewhere. Those with a strong in-migration of middle-aged adults see stronger economic growth.

“The attraction of middle-aged adults

presents a new opportunity for economic growth,” Akers says. “Rural communities that enhance their quality of life may be in the best position to attract residents.”

Many rural communities are in fact actively working to entice new residents through jobs and amenities, such as school systems, health care services and recreation. In Oklahoma, for example, the Department of Commerce helps rural communities with business retention, expansion, attraction and more. Some small towns, like Chetopa, Kan., even offer free land.

For Gaster, it’s the quality of life that lured her back to Nebraska. She wanted the sense of peace she feels when she smells the crops and hears the locusts. And she wanted to be near her extended family.

“This is where I’m from,” she says. “This is who I am.”

ALTHOUGH SMALL TOWNS will probably always see an out-migration of young adults, many are trying to offset that loss by recruiting new residents. In Chetopa, Kan., the city offers free land to new residents who buy the home built on it. George Davis, Chetopa’s chamber of commerce president, city council member and lifelong resident, says the benefits of new residents outweighs the cost of giving away property.



Aging populations vs. economic growth

Henderson says there are three demographic changes in rural areas of the District that could shape these communities:

- The retirement of baby boomers strains pools of workers by reducing workforce participation;
- The flight of young adults challenges workforce levels, especially for high-skilled positions; and
- The return of middle-aged adults could partially offset declines in the workforce.

In the District, with its large rural geographic area, there is a high concentration of older residents. During the past 40 years, retirement-age residents (those 65 and older) in the District have increased from 12.9 percent of the population in 1970 to 15.6 percent in 2008. By comparison, metro areas saw a rise from 9.5 percent to 11.5 percent.

“So while aging populations in general slow economic growth,” Henderson says, “rural migration patterns are both accelerating and mitigating this trend.”

An area’s economic growth potential emerges from a couple of components: population growth and workforce participation.

The Census Bureau projected the District’s adult population (those 16 and older) to grow just 0.4 percent annually through 2020, potentially trimming economic growth by 0.7 percent. Meanwhile, the number of retirement-age residents has increased substantially in the District since the 1970s. The District workforce participation rate is projected to fall 0.27 percent annually through 2020, reducing the potential growth of District output, or GDP.

The continued reduction in population growth as young residents move, coupled with weakened workforce participation as workers retire and slower productivity growth, could slow the District’s annual economic growth from about 3 percent to less than 2 percent by 2020. This would limit personal income growth for rural residents.

“However, small communities are not necessarily doomed to a shrinking workforce and dwindling economic growth,” Akers says. “Refocusing their resident recruitment efforts could be the key.”

Shift in strategy: attraction, retention

As an added incentive to move to the “nice, friendly little town” of Chetopa, Kan., incoming residents can also receive free land.

“We want new people,” says George Davis, chamber of commerce president and city council member, adding, “It benefits the city” through an increased tax base, workforce, local consumer spending and more, which outweighs the cost to the city of giving away its property.

Several years ago Chetopa dedicated seven acres of the school district’s land to build 13 new homes, known as the Hornet Addition. The plots are free; residents purchase the homes (a three-bedroom house is priced in the low \$70,000s). Six have been built and five are occupied—all have families with children, which ultimately could increase the town’s young adult population. Just 7.2 percent of the town population is between 18-24 years old, and the median age of residents is 44, according to census data.

“It’s working,” Davis says of the recruitment effort, though the town’s population hasn’t greatly fluctuated as a result. But it hasn’t declined either. There is potential to increase the number of free plots in the future, he says.

Located in the southeast corner of Kansas, Chetopa has nearly 1,300 residents. Residents call the town the state’s “pecan and catfish capital” and it’s surrounded by wheat, soy beans, corn and cattle. The largest employers in town are the kindergarten through 12th-grade school and a charcoal manufacturer.

“I’ve been here all my life,” says Davis, 74. “I just like it here.”

People, of course, move to communities for job opportunities, but, increasingly, are also

in search of a high quality of life.

“While rural communities need to develop their business environments, it is important for them to offer education, health services, recreation and other amenities,” Henderson says. “The goal of economic growth, after all, is to enhance the quality of life for people of all ages.”

Rural communities often overlook the benefits of the in-migration of middle-aged residents. Because middle-aged adults are in their prime working years and usually experience the largest increases in personal wealth in the workforce, areas that have seen population gains among this demographic also have seen strong economic gains.

The small but noticeable increases in middle-aged residents partly off-set the out-migration of younger residents in the District, Henderson says. Farm-dependent counties in particular have experienced some of the largest losses of young adults, but have also seen a rebound in middle-aged adults. Since 1990, their numbers of late baby boomers have risen roughly 14 percent.

Some rural communities in the District actively are recruiting residents through natural amenities. For example, retirement destinations in New Mexico, Colorado and southern Missouri’s Ozark Mountains lure older residents with mild weather year-round and geography ideal for recreation, such as water or mountains.

For many communities, recruitment efforts need to be both intentional and personal, says Jeff Yost, president and CEO of the Nebraska Community Foundation. The Lincoln-based nonprofit provides financial management and development assistance to local leaders throughout the state who are building community endowments for reinvestment in long-term viability.

For example, the Norfolk Area Recruiters recently was established with a mission to attract natives back to the community. The group says the Norfolk area is seeing a surge in new business and job opportunities.

Generally, it’s a combination of factors



PEOPLE OFTEN MIGRATE TO NEW COMMUNITIES for job opportunities, but also are increasingly moving for a higher quality of life. In Chetopa, Kan., residents build a sense of community by gathering for the town’s ninth annual Pecan Fest. The day-long celebration included pecan harvesting, a car show, arts and crafts, cooking contest, live entertainment and more.

that draw people to communities, Yost says, and rural towns can entice new or returning residents by developing these attributes. This customized attraction may include jobs, schools and social networks within the communities. It’s important for efforts to be long-term and regional to maximize the effects. Recruiting and retaining residents is vital to building and sustaining rural economies, he says.

“You have to have a next generation,” Yost says. “You can’t just age as a society and continue to have a society.”

Effects of age on populations

There are roughly 83 million baby boomers, ranging in age from 45 to 63. This is about one-quarter of the U.S. population and means there has never before been such a large portion of workers approaching retirement.



This also means as they retire and migrate, baby boomers may significantly increase rural populations, shifting small-town demographics even more so. With this brings many economic implications, Akers says, including shrinking the U.S. workforce and reducing economic growth in small towns in particular because they have a higher concentration of older residents.

In addition, Yost points out that retaining wealth in rural America also is affected. Communities with aging populations could see significant amounts of money leave the area as it is transferred to heirs who live elsewhere, often in larger cities. The Nebraska Community Foundation estimates about \$1.9 billion in rural wealth will leave the state annually during the next five decades. In an effort to keep residents' wealth local, the nonprofit works with communities to build endowments. Nearly 90 of NCF's community-based affiliated funds are building endowments.

"There actually could be a greater benefit for rural communities to encourage middle-aged adults and their families to return, rather than trying to keep young adults from leaving," Henderson says. "Demographic change is a cornerstone of economic growth."

One of the reasons Kara Weander-Gaster ultimately stayed in Norfolk was the feeling that her work could make a difference in the community. It was family, though, that drew her back initially.

While she was studying in New York, her father was diagnosed with cancer.

"I didn't want to be half a country away. I was going to put my life (in New York) on hold, deal with this situation, then move," Gaster remembers. "It was quite a shock when I moved back, going from Syracuse to small-town Nebraska. It was a culture shock."

But, living in Nebraska again felt right and, after awhile, she didn't think about leaving.

"During that time period, I met a young man," Gaster says. "I met David."

Shortly after Gaster lost her father, she and David were married. Not long after that, the director's position at the Norfolk Arts Center—an art gallery, performing arts host and educational facility—became available. It occurred to her, "I can be the person expanding arts in northeast Nebraska."

Looking around town, Gaster says, "There are some absolutely exciting things going on here."

She's not the only one to notice. There are others in the community like her, and the dynamics are changing, she says.

"We're really empowered to make Norfolk a better place."



BY BRYE STEEVES, SENIOR WRITER

FURTHER RESOURCES

"COMING HOME TO RURAL AMERICA: DEMOGRAPHIC SHIFTS IN THE TENTH DISTRICT"

By Jason Henderson and Maria Akers
KansasCityFed.org/TEN

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



Residential mortgages *and community banks*

Smaller insured financial institutions see less decline

Although the U.S. residential real estate market has deteriorated at an unprecedented level, with dramatic declines in both the number of homes sold and home prices, mortgage lending at First Westroads Bank in Omaha hasn't been affected quite like you'd guess.

Many financial institutions are experiencing steep reductions in lending, but Steve Robinson, the community bank's president and chief lending officer, says, "We have certainly seen an increase in the demand for permanent residential mortgage loans."

While the housing industry's descent has affected the banking industry as a whole, it seems that certain areas are faring better than others, says Jim Harvey, a policy economist at the Federal Reserve Bank of Kansas City. Harvey recently researched residential mortgages and their impact on community banks (small institutions, generally with assets less than \$1 billion). His analysis includes real

estate trends since 2005 and the likelihood they will continue.

The decline in the residential real estate industry has reduced demand for home mortgages. All lending, regardless of the type and size of lender, has dropped.

However, insured financial institutions—particularly smaller ones—have seen smaller declines in loan origination than other lenders, especially private mortgage banks. Loans purchased by nongovernment agencies have dropped dramatically, which has disproportionately affected private mortgage banks because they typically sell their loans in the secondary market. In contrast, insured financial institutions are more likely to hold loans rather than sell them in the private secondary market, although First Westroads Bank, for example, rarely holds loans on its books and has still fared better than larger institutions.

With the decline in the overall residential mortgage market during the last several years,

small banks' share of loan originations has doubled. This has occurred even as their overall volume of lending has declined slightly.

"There are reasons to believe this advantage may continue as the mortgage market begins to rebound during the next several years," Harvey says. "However, if this share is to be maintained, or grow, community banks likely will need to address challenges in their business practices."

Trends: mortgage lending, housing market

The U.S. residential real estate market has dramatically deteriorated during the last few years—declines in both the number of homes sold and home prices are unprecedented.

From 2005 through 2008:

- Sales: The total number of homes sold dropped by more than 35 percent. The market for new homes took a particularly hard hit—sales fell from 1.3 million to less than half a million.

- Prices: The median value of existing home prices declined 24 percent.

- Purchases: The number of home purchase loan originations fell 58 percent.

- Total loans: The number of total mortgage loan originations (including refinancing and home improvement) dropped 55 percent.

The decline in loan originations varied by the type and size of lending institution. From '05 to '08, insured depository institutions, including commercial banks, thrifts and credit unions, experienced a reduction of 45 percent, whereas private mortgage banks saw a drop of 72 percent.

"A major cause for the greater decline in loan activity at mortgage companies appears to have been their reliance on the private secondary market to fund the loans they originated," Harvey says.

Because mortgage companies don't have access to insured deposits to fund the loans they make, they typically sell the loans they originate in the secondary market. Their profits come from loan origination and other fees,

not from the interest earned on the loans. This means they're reliant on high volume and high fees.

By the second half of 2006, many secondary sources of funding, especially for higher risk loans, were nearly nonexistent. Mortgage banks didn't have sources of funding or capital to hold loans on their balance sheets, resulting in the dramatic drop in lending in '07 and '08.

"Reliance on private funding affected various types of lenders," Harvey says.

In '05, mortgage companies sold 72 percent of their loans in the private market, whereas depository institutions sold 24 percent of their loans in the private market. Both types of lenders saw similar declines in the private market, but because mortgage companies relied so heavily on the private market, they were hit harder than depository institutions, he says.

But perhaps most surprising is how well loan originations that were sold to government agencies fared, Harvey says. These loans fell just 13 percent from '05 to '08 and actually increased in '07 and '08. Mortgage companies had just a small share of this market and did not benefit from government agencies' continued growth during the recent turmoil.

While depository institutions fared better than mortgage companies, there are differences among banks depending on their size.

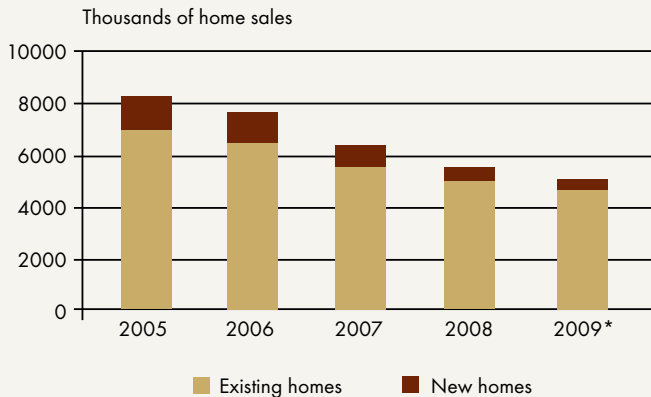


PHOTO BY ISTOCK

Decline of home sales and home financing in recent years

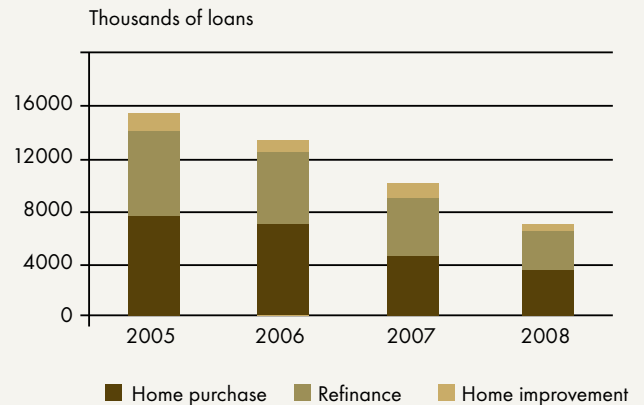
The U.S. housing market's dramatic decline in homes sold and home prices has affected the banking industry, greatly reducing the demand for home mortgages. Though all lending has dropped, smaller insured financial institutions have fared better than other lenders.

Number of new and existing homes sold



Source: National Association of Home Builders
* as of May 2009

Number of loans originated by loan purpose



Source: Home Mortgage Disclosure Reports, Federal Reserve System

- The largest banks (more than \$10 billion in assets) saw loan originations drop 51 percent;
- Medium-sized banks (\$1 billion-10 billion in assets) saw a drop of 31 percent; and
- Community banks (less than \$1 billion in assets) saw a drop of just 10 percent.

The difference, Harvey says, is that smaller banks generally are much less reliant on selling loans in the secondary market than other lenders, including larger banks. The share of loans originated at the smallest banks increased substantially, though this wasn't absolute growth but rather less of a reduction compared to the overall market. Community banks did increase their lending from 2006 onward—particularly noteworthy during what is likely the worst residential real estate market on record, Harvey says.

In addition to business practices, Robinson, of First Westroads Bank, says there

may be a couple of reasons why smaller banks have seen smaller declines in mortgage lending the past couple of years.

"I would attribute that to the availability of attractive loan rates and terms, as well as the \$8,000 first-time homebuyer tax credit (offered by the government) this past 12 months," he says. "Also, with the fallout from the subprime mortgage loan debacle, there has been a decrease in the number of residential mortgage loan originators resulting in more loan requests to those lenders still standing—including our community bank."

Relationship banking may be a factor as well.

"Another reason is the safety and soundness of the community bank and the trusting relationship the bank has established with its customers and the community," Robinson says. "Borrowers like the familiarity of their

community bank when it comes to handling the most important financial transaction of their lives.”

What does this mean for community banks?

After community banks doubled their share of loan originations since 2005, they still have just 7 percent of the residential real estate market. Maintaining or increasing this share seems feasible, Harvey says.

Residential real estate loans make up about 14 percent of community banks’ assets, or about \$178 billion total for all community banks. Assuming better than normal growth, this could reach \$400 billion during the next five to seven years, he says.

This magnitude of growth, Harvey adds, has implications for various areas of community banks’ financial performance, including:

Capital: A large increase in one type of asset such as residential real estate would mean each dollar of capital would be supporting a larger amount of assets. Some community banks may have the capacity to grow without needing additional capital, but they could also substitute residential real estate loans for other assets or raise capital, if necessary.

Asset quality: Community banks have experienced significant declines in their asset quality during the last two years. Residential real estate has been low-risk lending historically, but future expansion will require proper underwriting and pricing.

Earnings: Residential real estate loans don’t usually generate high interest rates compared to other types of lending. Therefore, increased residential real estate lending may not improve banks’ interest margins. However, it’s possible that rising residential real estate loans may improve earnings in other ways. Banks could see an increase in noninterest income if they maintain servicing rights on loans they originate and subsequently sell.

Liquidity / interest rate risk: The most difficult challenge community banks may face

in expanding residential real estate lending is managing liquidity and interest rate risk. They will need additional funding unless lending is reduced in other areas, and they already face long-term challenges to find stable funding sources. They could also face maturity mismatches if they use short-term funding sources, such as deposits, to fund longer-term mortgages. This would leave them vulnerable to rising interest rates.

For banks primarily originating and selling residential mortgage loans, Robinson says that qualified lenders, convenient locations, competitive loan products, technologically advanced tools, strong marketing and more are necessary.

“All of these elements require a capital commitment on the part of the bank,” Robinson says, “and the more the community bank wishes to grow this lending area, the more capital it will need.”

Harvey says recognizing how an increase in a specific asset, such as residential mortgages, would affect their financial performance is key.

“There are reasons to believe that this share of increases may stick as the residential real estate market begins to recover,” Harvey says. “That said, community banks will need to devise strategies to increase funding and manage interest rate risk to successfully grow their residential mortgage loan portfolios.”



BY BRYE STEEVES, SENIOR WRITER

FURTHER RESOURCES

“TRENDS IN RESIDENTIAL MORTGAGE LOAN ORIGINATIONS AND THEIR IMPACT ON COMMUNITY BANKS”

By Jim Harvey
KansasCityFed.org/TEN

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

About... The Money Museum

See millions of dollars inside the region's largest cash vault. Design your own currency. Learn about the Federal Reserve's role in the economy.

The Kansas City Fed's interactive Money Museum is open to the public to learn about currency, the economy, bank operations, the Fed's purpose and functions, and much more.

Tours are free, available weekdays during regular business hours, and can be guided or self-guided.

Exhibits appeal to visitors of all ages, but some—such as student groups—may want to take advantage of additional resources. Fed staff wrote lesson plans for educators to use in conjunction with a Money Museum tour as well as take-home activities for families.

The 3,000-square-foot museum is a part of the Kansas City Fed's headquarters at 1 Memorial Drive in Kansas City, Mo.

Many exhibits have touch screens with video and text. Visitors can watch two short films on the Kansas City Fed and its history.

Additionally, the museum's coin machine is stocked with the latest issues of state quarters and presidential dollars, and The Vault gift shop sells Fed merchandise, including T-shirts, books and one-of-a-kind items. All visitors receive a bag of shredded currency and can choose from a variety of free publications.



The Truman Coin Collection:

More than 450 coins from every presidential administration, on loan from the Harry S. Truman Library.



Money of the Olympiads

During the 2010 Vancouver Winter Olympics, come see coins from ancient Olympic games. Dating back to 776 B.C., the coins enhanced the prestige of the competition and also served as legal tender. This exhibit from the American Numismatic Association is on display Feb. 8 - 26.



Interactive exhibits: Allow guests to step into the role of a bank examiner, try to spot a counterfeit note and learn more about the Fed.

Cash operations: Through glass, a portion of the vault and the automated vehicles that move the money can be seen.



“The Fed and You”: A short introduction film displayed on a 12-foot-long video wall.

The Legacy Exhibit: Includes artifacts dating back to the Kansas City Fed’s opening day in 1914, such as this Tommy Gun used by guards.

Exhibits for young children: Include displays about the role of currency in the economy; creating their own money at the rubbing station; and lifting a gold bar.



Come visit. It's free.

For more information on The Money Museum, directions, parking, group-specific tours and making reservations, visit KansasCityFed.org or call (800) 333-1010 ext. 12683.



Resolutions help kids start new year with financial awareness

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.

We traditionally kick off a new year with positive attitudes and life-improving declarations. Why not help kids start off 2010 with some financial resolutions of their own? During my years in the classroom, I managed our school's on-site bank for students. I asked my young depositors to develop goals for their savings accounts, such as making a certain number of deposits and setting a yearly deposit total. I would review these goals periodically during the school year to see their progress and to keep them on track. The same idea can be easily implemented at home. Parents can help their children develop goals by using the "Go-Getter Goal Setter" planner on Page 30. Each of the five planner areas below—saving, earning, spending, donating and learning—contains a saying to illustrate the goal and help kids remember its importance. These resolutions will benefit children of all levels of financial knowledge and can be tailored to the appropriate age groups.

2010 Saving Goal: "Don't save what is left after spending, spend what is left after saving."

Ask your child to list one or more saving goals to accomplish during the upcoming year. Listing items or events will help him plan long-term and budget accordingly. Examples could be a bike or video game, spending money for vacation, or holiday gifts. After listing his goals on the Goal Setter sheet, have him decide what portion of his income he needs to save. As he earns his income, that amount should be de-

posited in a bank account to earn interest. Older children can develop a budget sheet listing goal items, income to purchase items and amount left to save monthly.

2010 Earning Goal: "Never depend on a single income source."

Once your child's savings goals are in place, discuss how he will meet them by earning income. Ask him to list current sources, including allowance, cash gifts and any odd jobs he regularly gets paid for doing. Now brainstorm potential new income sources, such as garage sales, lemonade stands, dog walking or pet-sitting, and outdoor jobs, such as raking leaves or shoveling snow. Teens could include babysitting and running errands for family members and neighbors, as well as part-time employment. Ask your child to pursue two or three of these potential income sources during the year to develop new streams of income. Make sure additional income is earned and not just given to them. Earned income is usually valued—and spent more carefully—than money received without any work on their part.

2010 Spending Wisely Goal: "A fool and his money are soon parted."

When it's time for kids to spend hard-earned dollars, discuss tips to help them make wise purchases. Ideas include looking at store ads and online sales to find the best prices; making a list to comparison shop; buying quality goods instead of a quantity of goods; and evaluating purchases. Introduce the term "buyer's remorse" to older children and ask them for examples of times they've regretted their choices.

2010 Donating Goal: "It is better to give than receive."

Many families believe in donating a portion of their earnings to charitable organizations.

Whether it's giving to their church, synagogue or a nonprofit, it is satisfying for kids to know they've helped others. Think of several causes your family believes in and ask your child to make a choice for his own donations. Decide on an appropriate amount to give and how often to donate. For teens, discuss the word "philanthropy" as an active effort to promote goodwill toward others. Ask them to research nonprofits online and decide on a favorite.

2010 Learning Goal: "An investment in knowledge always pays the best interest."
Help kids increase their financial knowledge

this year. They can develop their "money sense" through exploring the books and online materials suggested in the resource section. In addition, parents can teach the personal finance concept words on Page 31, reinforcing the words with the activities suggested. Ask kids to set the number of resources they will read and words they will master on their planner. Focusing on these personal finance resources should help kids move toward their goals successfully and aid them in becoming more financially literate. And, they will be able to apply their new knowledge to next year's financial resolutions.



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.

Online at KansasCityFed.org/TEN:

Fifty Nifty Econ Cards help educators teach economic and personal finance words and their meanings. A resource guide with activities and games accompanies the cards. The cards and guide can be downloaded, or educators can order them for free from the Kansas City Fed. For ages 5-12.

Piggy Bank Primer introduces children to saving, spending and budgeting through a story format. For ages 6-9.

FederalReserveEducation.org is the Fed's website for economic and personal finance education. It includes free curriculum and publications for all ages, as well as information on monetary policy, banking supervision and financial services. For all ages.

Econ Explorers Journal helps children discover economics and personal finance in their home, neighborhood and school through five individual projects. For ages 8-11.

Fiction Books:

Max Malone Makes a Million

by Charlotte Herman
Max and friend Gordy try several money-making schemes with limited success. Younger neighbor Austin shows them his business know-how by considering location and market to make big profits. For ages 6-9.

Rock, Brock and the Savings Shock

by Sheila Bair
Twins Rock and Brock have different ideas about saving money earned from grandpa. Introduces

compound interest in an understandable way and highlights "six savings tricks" for kids. For ages 7-10.

Non-Fiction Books:

The Kids Money Book: Earning* Saving* Spending* Investing* Donating*

by Jamie McGillian

Offers an introduction to setting financial goals with quizzes and guides to help ensure success. For ages 8-12.

Raising Money Smart Kids:

What They Need to Know

by Janet Bodnar

Touches on mastering six money skills; setting allowance systems; and helping kids learn the virtues of working for pay. For adults.



2010 Financial Resolutions and Planner



Savings Goal:

I will save my money for _____

I will save _____ of my income weekly/monthly to reach my goal by _____



Earning Goal:

My current income is earned through _____

I might earn new income through _____



Spending Wisely Goal:

Tips I will use to make wise spending decisions: _____



Donating Goal:

I will donate a part of my income to _____

I will donate \$ _____ weekly/monthly/quarterly to this organization.



Financial Knowledge Goal:

I will learn more about using money wisely by reading _____ books or online resources.

I will learn and add _____ finance words to my vocabulary this year.



Goal Evaluation:

I will discuss my progress on these financial goals monthly/quarterly.

Signed, _____

Learn the financial fundamentals

Challenge kids to learn these finance words and their meanings listed on the back of the cards. Use the activities to help kids remember the money concepts.

Activity suggestion:

Finance Pictionary (Ages 5-10) Ask your child to choose a card to illustrate on paper, drawing and labeling a picture of the word in use. (For example, income could be drawn as money being paid to a worker.) Discuss the word, meaning and finished picture. Continue this activity periodically until pictures are drawn for all 10 words. Have your child alphabetize the words and drawings to create a pictionary of finance words to keep.

Earn

Save

Bank

Spend

Interest

Account

Budget

Income

Finance

Consumer

Learn the financial fundamentals

Activity suggestion:

World of Finance (Ages 10+) Ask older children to read the business section of the newspaper, or go online, to find these words and any other finance-related terms they see. Have them keep track of the number of words found and try to beat their score by periodically repeating this activity with new reading material. This is a good review of concepts learned, a way to introduce new ideas and show real-world application of this knowledge.

Save

To keep money to spend later

Spend

To use money to buy goods and services

Account

A record of money deposited or withdrawn from a bank

Income

Amount of money you earn or receive from different sources

Consumer

Someone who buys or uses goods and services to satisfy wants

Earn

To receive money for doing work

Bank

A business that provides money services

Interest

Payments made for the use of money

Budget

A plan showing how income is to be spent

Finance

The management of money

Ask an Economist...

Is the Kansas City Fed's Ag Credit Survey reliable?

Each quarter, the Federal Reserve Bank of Kansas City asks agricultural bankers in the region their perceptions on farm lending and farm land values. Their answers help the Kansas City Fed gauge regional agricultural financial conditions as well as offer insight into broader ag trends.

Brian Briggeman, an economist at the Kansas City Fed's Omaha Branch who specializes in ag and rural research, along with a research associate, recently examined the 30-year-old survey to determine how closely the District survey results correlate with national data and trends. Their findings will be published in a forthcoming edition of the Kansas City Fed's *Economic Review*.

Who receives the survey?

Briggeman: The Ag Credit Survey is sent to 350 ag banks (those with at least a 14 percent concentration in ag loans) in the Tenth Federal Reserve District. The District includes western Missouri, Nebraska, Kansas, Oklahoma, Wyoming, Colorado and northern New Mexico. Typically about 75 percent of the banks respond.

What does the survey include?

Briggeman: Survey results summarize several indicators of farm financial and lending conditions, including farm loan repayment rates, farm income, farmland values, collateral required to secure a loan, farm loan interest rates, credit supply and demand, as well as bankers' perceptions about future financial and lending trends.

What happens to the survey responses?

Briggeman: Both a summary and data are compiled by economists at the Omaha Branch and a report is distributed nationally. Because it is conducted more frequently than many other national measures, the survey also receives media attention.

How did you measure survey data and what did that comparison show?

Briggeman: We wanted to ensure we are surveying a sample that's representative of the District, so we looked at respondents county by county. This showed us the survey is broad reaching. Secondly, we compared survey responses about loan repayment rates against national data (loan delinquency rates reported by banks to regulators). We found that these two did indeed correlate. Moreover, responses are an excellent barometer of future agricultural lending conditions.

Do you have plans for further research?

Briggeman: Yes. I am collaborating with researchers at Oklahoma State University to validate farmland values collected in the survey against national sales price data.

Is the Ag Credit Survey valid?

Briggeman: Yes. Our research shows we've tested our data against national data, and the two sources track closely. By looking deeper into our own processes and tools, we're able to show how our efforts provide insight into ag research as well as the larger economy.

Why is the Ag Credit Survey important?

Briggeman: The survey is more than a window into this region's agricultural economy. Our research verifies we can use survey results to provide insight into national trends. This reinforces that the Kansas City Fed's District is important to the country as a whole: Our ag economy is a good microcosm for the national economy.

BY BRYE STEEVES, SENIOR WRITER

FURTHER RESOURCES

"CAN THE AG CREDIT SURVEY PREDICT NATIONAL CREDIT CONDITIONS?"

By Brian Briggeman and Christopher Zakrzewicz

The Ag Credit Survey

KansasCityFed.org/TEN

Barkema named director of research at Kansas City Fed

Alan Barkema is the Federal Reserve Bank of Kansas City's new director of research. He retains the title of senior vice president and continues to serve on the management committee, which guides the organization.



BARKEMA

In his new role, Barkema is responsible for coordinating all research-related work at the Kansas City Fed, including research on monetary policy, regional and agricultural economics, banking studies, and the payments system. The Bank's research informs its policy decisions in its three mission areas of monetary policy, bank supervision and payments. The Bank's research publications also are helpful to the public and policymakers.

He replaces Gordon Sellon, who was the director of research since 2006 and retired at the end of 2009 after 30 years of service.

Barkema most recently served the Kansas City Fed as its senior vice president of the Regional, Public and Community Affairs Division since 2005. He came to the Kansas City Fed in 1986 as a research economist. Barkema also has held several management positions through the years.



SELLON

He was promoted to assistant vice president in 1994. Barkema later served a three-year term as a professor and head of the Agricultural Economics Department at Oklahoma State University before returning to the Kansas City Fed in 1999 as a vice president and economist, helping to launch the Center for the Study of Rural America.

Barkema holds a master's degree from Cornell University and a Ph.D. in economics from Iowa State University.

Connor leads Fed's Electronic Check Platform Project

Denise Connor has been named a senior vice president at the Federal Reserve Bank of Kansas City. She manages the Electronic Check Platform Project for the Federal Reserve System's Retail Products Office. Additionally, she now is a member of the Kansas City Fed's management committee, which strategically guides the Reserve Bank.



CONNOR

The national project is designed to implement a more efficient electronic check platform on behalf of the Federal Reserve's retail payments office. One of the Federal Reserve's three mission areas is monitoring the payments system, in addition to its work in monetary policy and financial industry supervision and regulation.

The multiple-year project began in early 2008. Connor oversees a core team in Kansas City as well as a large virtual team across the Federal Reserve System also dedicated to the project.

Connor joined the Kansas City Fed in 1987 and was promoted to assistant vice president in 1998 and vice president in 2000. Recently, she led the Federal Reserve System's efforts to analyze options to modernize Check 21, the electronic check processing platform.

She holds degrees in journalism, economics and finance from the University of Missouri-Columbia.

Raley heads Regional, Public and Community Affairs Division at Kansas City Fed; Young promoted to vice president



RALEY

Diane Raley now oversees the Kansas City Fed's Regional, Public and Community Affairs Division. Raley continues to serve as the public information officer, board of directors' secretary and member of the management committee, which guides the organization.

She has led the Public Affairs arm of the Division as its senior vice president since 2009; Raley takes on Regional and Community Affairs, which was led by Senior Vice President Alan Barkema until he became the director of research. Barkema now

heads the Economic Research Division.

The Regional, Public and Community Affairs Division was created to strengthen regional research efforts, heighten public understanding of the Federal Reserve's work and how people are affected, and support economic growth in communities, among other charges.

Raley came to the Kansas City Fed in 1998 from Memphis and Cincinnati, where she worked in public and media relations. She was promoted to assistant vice president and public information officer in 2001 and to vice president in 2004. She has a bachelor of arts degree in communication from the University of Cincinnati.



YOUNG

She also is the assistant secretary to the board of directors.

She came to the Kansas City Fed in 2001 as an analyst. Young has a bachelor of science degree in mass communication and broadcasting from Northwest Missouri State University and a master of business administration degree from Rockhurst University.

Also within the Division, Kristina Young has been promoted to vice president of the Public Affairs and Community Affairs departments. Young was an assistant vice president in Public Affairs since 2006.

Home loan guide for Native Americans

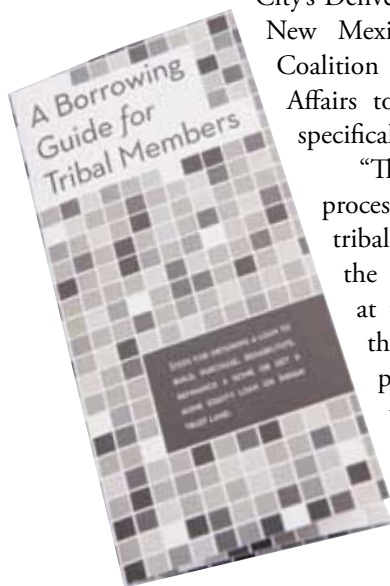
For Native Americans who want to build, purchase or rehab a house, or get a home equity loan on tribal land, help is available.

The Federal Reserve Bank of Kansas City's Denver Branch partnered with the New Mexico Tribal Homeownership Coalition and the Bureau of Indian Affairs to create a borrowing guide specifically for tribal members.

"The guide offers a seven-step process for applying for a loan on tribal land," says Ariel Cisneros, the Community Affairs adviser at the Denver office. "Because this type of loan application process is more in-depth than a typical home loan, it can deter applicants. Our goal is educate would-be borrowers and make the process less confusing."

Part of the Kansas City Fed's Community Affairs Department's mission is to promote economic growth in communities, including a focus on community development investments, neighborhood stabilization and consumer financial stability.

Thousands of guides have been distributed regionally, and the Bureau of Indian Affairs is working to make them available nationwide. To view the guide online, visit KansasCityFed.org/TEN.



Accounting roundtables held in Kansas City, Denver

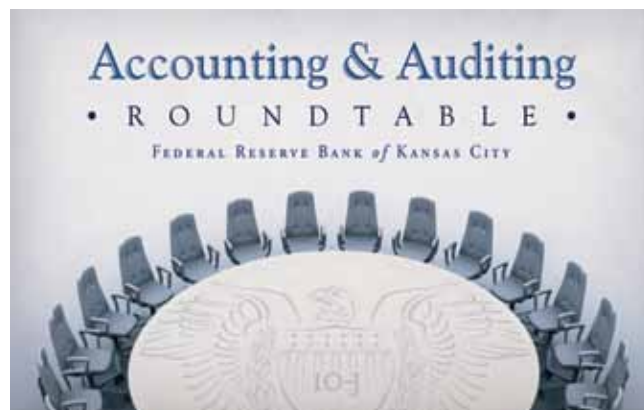
The Supervision and Risk Management Division of the Federal Reserve Bank of Kansas City hosted its annual Accounting & Auditing Roundtable in November.

More than 100 bankers and accounting and auditing professionals with responsibility relative to financial reporting for banking organizations attended one of the two sessions in Denver or Kansas City.

The primary goal of the roundtables is to share knowledge about issues arising from accounting pronouncements, banking legislation and examination experiences, while enhancing communication with the Federal Reserve.

Discussion topics included troubled debt restructuring and loan modification, deferred tax assets, International Financial Reporting Standards (IFRS) and more.

Linda Ditchkus, a member of the Federal Reserve's Board of Governors, participated in the panel discussion, as did representatives from the Federal Reserve Banks of Kansas City and Chicago.





FEDERAL RESERVE GOV. KEVIN WARSH
addresses attendees.

Annual Regional Banking Organization Conference held in Kansas City

More than 100 staff from all 12 Federal Reserve Banks and the Federal Reserve Board of Governors gathered at the Federal Reserve Bank of Kansas City in early October to share information and best practices for bank oversight.

The annual Regional Banking Organization Conference served as a timely opportunity to discuss challenges posed by the financial crisis, including risk management and other issues banks may be facing, such as managing asset quality, access to capital and liquidity.

Speakers included Board of Governors member Kevin Warsh and Kansas City Fed President Tom Hoenig and First Vice President Esther George, as well as staff from other Reserve Banks, executives from large financial institutions, academics and financial analysts.

Foreclosure mitigation toolkit available

In an effort to prevent unnecessary foreclosures and ease the effects of those that do occur, the Federal Reserve developed an online toolkit of resources.

The toolkit includes data and maps on foreclosure trends and hotspots, information on foreclosure laws, and local resources and events for displaced homeowners.

The resources in the toolkit are presented as a four-step process:

- assess the foreclosure situation;
- reach troubled homeowners;
- establish post-foreclosure support systems;
- preserve neighborhoods.

“The Fed views the recent high rate of mortgage foreclosures as an urgent problem,” says Kelly Edmiston, Kansas City Fed senior economist who wrote much of the materials.

“The goal of this toolkit is to provide resources to address the current turmoil in the housing market and minimize the impact of foreclosures on neighborhoods.”

This toolkit is a part of the Kansas City Fed’s ongoing work to address foreclosures, including hosting events throughout the region; conducting research; and partnering with other regulators, community groups, policy organizations, financial institutions and public officials. Much of Edmiston’s research focuses on housing issues and the current foreclosure crisis.

To access the toolkit, visit KansasCityFed.org/TEN.

Student competition prompts creativity, teaches about the Fed

More than a hundred Kansas City metro-area students participated in the Federal Reserve Bank of Kansas City's second annual "Shred Challenge" competition in November.

The competition prompted high school students to create works of art that incorporated their personal views on saving. The medium: shredded money provided by the Kansas City Fed. As part of its on-site cash processing services, the Kansas City Fed shreds paper money that is unfit for circulation because it is too worn, torn or dirty. It is given to visitors for free.

Entries included pottery, paintings, drawings and more, many with an artist's statement explaining the importance of saving money.

Seven staff members from various areas of the Kansas City Fed served as judges.

Winners of the competition were Jack Wallace, Shawnee Mission North High School, first place; Quyen Hoang, Lincoln College Preparatory Academy, second place; Emily Anderson, Liberty High School, third place; Jamie Baum, Raymore-Peculiar High School, fourth place; and Amber Vasquez, Liberty High School, fifth place. Winners received U.S. savings bonds. Shawnee Mission North was the winning school and received a trophy.

Participants were invited to the Kansas City Fed to present their creations, tour The Money Museum, and learn more about the nation's central bank and the economy.

For more information on economic education events and free resources, visit KansasCityFed.org/TEN.



Economic Forums see high attendance in communities around region

The Federal Reserve Bank of Kansas City held its annual Economic Forums in several communities in Oklahoma and Colorado this fall, sharing its economic perspective

while gaining insight from local business communities.

Kansas City Fed staff, including President Tom Hoenig; Special Advisor on Economic Policy Craig Hakkio; and economists Todd Clark, Mark Snead and Chad Wilkerson, spoke to larger-than-anticipated crowds, totaling more than 1,500. Clark spoke about the national economic outlook while Snead and Wilkerson, who are the executive officers who oversee the Kansas City Fed's Denver and Oklahoma City

Branches, respectively, spoke about the regional economic outlook.

In Colorado, forums were held in Grand Junction, Durango, Pueblo, Greeley and Denver. In Oklahoma, forums were held in Ada, Bartlesville, Clinton and Oklahoma City. Economic education presentations or workshops for students and faculty at local

colleges were held in conjunction with many of the forums.

"This is an opportunity for the Kansas City Fed to share with local business leaders what the nation's central bank is seeing in the economy," Hoenig says. "In turn, we listen to—and learn from—these local communities."

The Kansas City Fed has held the forums for nearly 60 years, rotating the locations among the seven states included in its Federal Reserve District. Next year's events will be held in Kansas, Missouri, Nebraska, New Mexico and Wyoming.



CHAD WILKERSON, Oklahoma City Branch executive, discusses regional economics.

Bank Anniversaries

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 and March.

Colorado B&TC of La Junta	La Junta	Colo.	86
Lusk State Bank	Lusk	Wyo.	76
St. Marys State Bank	Saint Marys	Kan.	74
First Community Bank	Taos	N.M.	72
Community B&TC	Neosho	Mo.	68
Colorado Mountain Bank	Westcliffe	Colo.	31
Bank at Broadmoor	Colorado Springs	Colo.	30
First State Bank	Wheatland	Wyo.	29
First B&TC	Broken Bow	Okla.	10
Lamar B&TC	Lamar	Mo.	10
Town & Country Bank	Ravenna	Neb.	10
Peoples Exchange Bank	Belleville	Kan.	1
Gardner Bank	Gardner	Kan.	1
Bank VI	Salina	Kan.	1

International Payments Policy Conference

The changing retail payments landscape: What role for central banks?

Every day in the United States about \$225 billion noncash purchases are made—without a doubt, electronic payments like debit cards and PayPal are growing.

This has implications beyond consumers choosing to swipe a card in favor of writing a check, and the Federal Reserve Bank of Kansas City explored this evolution of the payments system and what it means for those involved

at its two-day conference in Kansas City, Mo., in November.

“The changing retail payments landscape: What role for central banks?” brought together more than 100 attendees from around the world from three principal groups: industry participants, policymakers and academics.

Representatives came from: central banks in Canada, Brazil, Japan, Mexico, Thailand, Australia, several European countries as well as the World Bank; large retailers, including Home Depot, IKEA and Walmart; and large commercial banks, credit card companies, universities, research firms and the Federal Reserve System.

In addition to its work in monetary policy and bank supervision and regulation, the Federal Reserve is charged with supporting an efficient, effective payments system, which includes cash, check, debit and credit.

It’s important for central banks to contemplate their role in the payments system, says Alan Barkema, the Kansas City Fed’s director of research and a senior vice president, and it’s important for facilitators and users to

gather for discussion.

“It’s one of our objectives here at the Kansas City Fed to facilitate that dialogue,” Barkema told attendees.

Participants stressed that integrity and efficiency in the payments system are public policy concerns, and that the role of the central bank is an important one. Around the world, central banks typically oversee the retail payments system, and some provide direct payment services as well.

During general discussion portions of the conference, speakers, panelists and audience members talked about bank and government regulation; payment surcharges and the effects on consumers; innovation in the payments system; and more.

Dan Hesse, CEO of Sprint Nextel Corporation, which is based in the Tenth Federal Reserve District in Overland Park, Kan., was the conference’s keynote introductory speaker.

“Americans and their mobile devices are becoming inseparable,” he said. “Mobile banking is a very natural part of the evolution of these devices.”

Kansas City Fed President Tom Hoenig also addressed attendees, as did others from the Federal Reserve System. Kansas City Fed Vice President and Director of Payments System Research Stu Weiner co-authored the paper “The role of central banks in retail payments: The central bank as operator” for discussion.

To read papers presented at “The changing retail payments landscape: What role for central banks?” the Kansas City Fed’s 2009 international payments policy conference, visit KansasCityFed.org/TEN.



DAN HESSE, CEO of Sprint Nextel, speaks at the conference.



BY BRYE STEEVES, SENIOR WRITER



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 western Missouri, Nebraska, Kansas, Oklahoma, Wyoming, Colorado and northern New Mexico. 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 check processing and other services to depository institutions.



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TEN also features articles on the Federal Reserve's history, structure and operations.

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“10J: The History of the Federal Reserve Bank of Kansas City”

Our Emmy-nominated documentary explores the origins of the nation’s central bank and the important role of the 12 Federal Reserve Banks in today’s economy. It includes interviews with Kansas City Fed President Tom Hoenig, historians and key players from around the region.

Visit The Money Museum in Kansas City and watch a portion of the documentary in our theater, or watch it in its entirety online. For more details, go to **KansasCityFed.org**.