The Fed and the Economy in the U.S. and Oklahoma

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Overview of the Federal Reserve System

• The “Fed” consists of three main entities:
  • Board of Governors: 7 members appointed by U.S. President
  • Federal Reserve Banks: 12 total; semi-independent by design
  • Federal Open Market Committee: 19 members; 12 voting

• As with most central banks, the Fed’s primary responsibilities fall within four general areas:
  • Lender of last resort – provide liquidity in times of crisis
  • Monetary policy – promote full employment and low inflation
  • Bank regulation – ensure safety and soundness of banks
  • Financial services – bank for banks, bank for federal govt.
Federal Reserve Districts and Office Locations
The Oklahoma City Branch of the Federal Reserve Bank of Kansas City

• Functions – 35 staff
  • Economic research and outreach for U.S. monetary policy purposes
  • Examinations and inspections of Oklahoma financial institutions
  • Economic and financial education outreach to teachers and citizens
  • Community development outreach to low and moderate income areas

• 2012 board of directors
  • Jim Dunn (chair), Chairman, Mill Creek Lumber and Supply, Tulsa
  • Linda Capps, Vice Chairman, Citizen Potawatomi Nation, Shawnee
  • Pete Delaney, Chairman, CEO, & President, OGE Energy Corp., OKC
  • Jacque Fiegel, Senior EVP and COO, Coppermark Bank, OKC
  • Doug Tippens, President and CEO, Bank of Commerce, Yukon
  • K. Vasudevan, Chairman, Service and Technology Corp., Bartlesville
  • Rose Washington, Exec. Director, Tulsa Economic Development Corp.
U.S. Economy and Monetary Policy

• U.S. economic growth has slowed in recent months, as uncertainties have risen again

• The FOMC expects continued improvement in unemployment, and for inflation to stay low

• The range of views among FOMC members about monetary policy are relatively wide
U.S. economic growth has slowed, with jobs and survey numbers the lowest since 2009

U.S. Private Payroll Employment and Business Indexes

Change from previous month, thousands

Index

Private Employment (left axis)
ISM Manufacturing Index (right axis)
ISM Non-Manufacturing Index (right axis)

Readings on the ISM factory index below 50 have not always meant recession
Factories have less than 10% of U.S. and District jobs, but they’ve spurred growth lately.

Manufacturing's Share of Total Job Growth, Last 6 Months  
(Nov-2011 to May-2012)

Percent

Source: U.S. Bureau of Labor Statistics

<table>
<thead>
<tr>
<th>District</th>
<th>Percent</th>
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<tbody>
<tr>
<td>US</td>
<td>17%</td>
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<tr>
<td>Tenth District</td>
<td>20%</td>
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<td>NM</td>
<td>56%</td>
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<tr>
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<td>34%</td>
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District manufacturers say the European impact has been moderate and more indirect.
The European Trilemma

• **Sovereign debt crisis** – Poor fiscal management and rising bond yields in some countries threaten fiscal sustainability.

• **Banking crisis** – A property bust in some markets and a decline in sovereign debt values have impaired the balance sheets of some Eurozone banks.

• **Slow growth and recession** – Tighter fiscal policy and financial conditions, plus the uncertain climate, is weighing on European growth.
The impact on the U.S. of an intensification of the European crisis

- Long-term rates would fall and support U.S. economic activity

- Credit standards would likely tighten, so fewer households and businesses would have access to the lower rates

- Appreciation of the U.S. dollar would weigh on exporters

- Commodity prices would likely decline

- Sharp fall in confidence and heightened uncertainty
Looking ahead, purchasing managers in the region were mostly optimistic in June.

Tenth District Manufacturing Expectations
Six-Months Ahead, Seasonally Adjusted

Source: KC, Dallas FRB Manufacturing Surveys
But Tenth District factory exports to Europe are declining, and China’s boost has lessened.
Exports are a relatively small part of the Tenth District economy, and even the nation’s

Exports as Share of GDP, 2010

Percent

Rest of World
China
Europe

U.S. 10J NE KS MO CO WY OK NM
3.4 2.1 2.3 2.8 2.1 2.2 1.3 1.5 1.7
0.7 0.6 1.2 0.8 0.8 0.4 0.1 0.3 0.2
8.3 5.6 8.6 8.6 5.8 4.3 4.8 4.3 3.6

Sources: U.S. Bureau of Economic Analysis, USDA, WISERTRADE
Financial stress in Europe remains higher than a few years ago, but is stable in U.S.

**Eurozone and U.S. Financial Stress**

- **European Financial Stress Index**
- **U.S. Financial Stress Index**

Source: FRBKC
The “fiscal cliff” and political uncertainty are also weighing on the U.S. economy.

**Estimated Impact on 2013 GDP**

**Worst Case**

Percentage points

- End payroll tax holiday
- End extended unemployment benefits
- AMT fix expires
- 2001 and 2003 tax cuts lapse
- Sequestration (automatic discretionary cuts)

Sources: Goldman Sachs
At its June meeting, the FOMC expected unemployment to gradually fall further.
And for inflation to remain at or below its long-term target

PCE Inflation Index

Percent change, year-over-year

June FOMC Forecast Ranges in Yellow

Long Term

Source: U.S. Bureau of Economic Analysis, FOMC
The majority of FOMC members expect interest rates to stay low through 2014.

Federal Funds Rate
Year-end target

Note – Number of participants who project the initial increase will occur in the specified year in parenthesis.

Source: U.S. Bureau of Economic Analysis, FOMC
The Fed’s balance sheet is at historically high levels

Federal Reserve Balance Sheet

Assets
- Treasury securities
- MBS & agency debt
- Short term lending
- Targeted lending programs
- Rescue operations

Liabilities
- Reserves
- Other
- Currency

Source: Federal Reserve Board
The Oklahoma Economy

• Oklahoma economic growth remains stronger than the nation, but has slowed

• The relative strength reflects solid energy, manufacturing, and real estate sectors

• Europe is less of a direct risk to the state, but lower energy prices are a concern
There remains considerable variation in economic strength in the nation and region.

Employment Growth, Year-over-Year (percent)
May 2012

Scale
- 1.54 - 6.75
- 1.06 - 1.54
- 0.47 - 1.06
- -0.86 - 0.47

Source: U.S. Bureau of Labor Statistics
Except for Tulsa, employment in Oklahoma is back to or above pre-recession levels.
Unemployment is very low in northwest and southern Oklahoma—and Washington Co.!

County Unemployment Rates
May 2012

Source: OK Employment Security Commission
But Oklahoma job growth has slowed since winter, across a number of industries.

Annualized Job Growth by Industry
Past Six Months of Data

Winter 2011-12 (Dec-Feb)
Spring 2012 (Mar-May)

Source: Bureau of Labor Statistics
Home prices continue to hold up much better in Oklahoma than in the nation.
And banks remain in much better shape than in the nation as a whole.
But Oklahoma energy activity has been flat for the past year (albeit at a high level)
Conclusions

- Growth in the U.S. economy has slowed moderately, as concerns about Europe and politics have risen.
- Inflation has remained low, and monetary policymakers disagree about future paths.
- Oklahoma economic growth remains better than in the nation and region, but job growth has slowed recently.
For more information about the Oklahoma economy, subscribe to the quarterly **Oklahoma Economist** at: [www.kansascityfed.org/publications/research/oke](http://www.kansascityfed.org/publications/research/oke)