The Economy and Banking

The views expressed are those of the author and do not necessarily reflect the opinions of the Federal Reserve Bank of Kansas City or the Federal Reserve System.
Today’s Roadmap

- The financial crisis has eased, but risks still exist
- Economic update
- What to make of concerns regarding future inflation, disinflation, and deflation
The financial market crisis has eased.

Source: Federal Reserve Board of Governors
While the financial crisis has eased, risks still exist in the economy.

- Probably the one risk most talked about today is commercial real estate (CRE)
- Most banks are exposed to CRE and/or have exposures to commercial mortgage backed securities (CMBS)
- Eventually, CRE will need to be refinanced...who will do this in today’s market?
U.S. commercial vacancy rates are rising.

U.S. Commercial Real Estate Vacancy Rates

Source: Torto-Wheaton Research
The share of CRE loans past due are rising.
While commercial banks’ profitability has fallen, capital levels have risen.
The U.S. is going through a de-leveraging process.

Domestic Debt Outstanding

Percent of GDP

Source: Federal Reserve Board of Governors
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Forecastsers expect we have hit bottom and should return to growth.

Real GDP Growth

Annualized percent change from previous quarter

Source: Bureau of Economic Analysis and Blue Chip Economic Indicators
Since 2008, retail sales have fallen. Recent boost from cash-for-clunkers, but is it sustainable?

U.S. Monthly Retail and Food Sales

Source: U.S. Census Bureau
The unemployment rate continues to rise.

U.S. Unemployment Rate

Source: Bureau of Economic Analysis
Improvements in the U.S. trade balance continue.

Real Net Exports of Goods and Services

Source: Bureau of Economic Analysis
Will emerging countries lead the recovery?

GDP Growth

Annual percent change, constant dollars

Source: International Monetary Fund, April 2009
The bulk of the stimulus package comes in 2010.

Estimated Budget Impact of American Recovery and Reinvestment Act (ARRA) of 2009

Billion Dollars

Source: Congressional Budget Office, February 13, 2009
The financial crisis has eased, but risks still exist

Economic update

What to make of concerns regarding future inflation, disinflation, and deflation
The U.S. is experiencing disinflation.

Consumer Price Inflation

Source: Bureau of Labor Statistics
With the Fed Funds Rate at the zero bound, the Fed has expanded its balance sheet.

Federal Reserve Balance Sheet: Assets

Billion Dollars

Jan-07 Jul-07 Jan-08 Jul-08 Jan-09 Jul-09

Source: Federal Reserve Board of Governors
Unlike the Great Depression, money stock (M2) has edged up with a surge in the monetary base.

Growth in Monetary Aggregates

Index (Jan 1930 = 100)

Source: Federal Reserve Bank of St. Louis, Friedman and Schwartz

Index (Jan 2007 = 100)

Source: Federal Reserve Board of Governors
The velocity of money has plummeted.
What is the future path of interest rates?

Fed Funds Rate

Source: Federal Reserve Board of Governors and CME Group
Conclusion

- The financial crisis and recession appear to be ending, but risks surround the recovery.
- The outlook hinges on consumer spending, both in the U.S. and globally.
- As the recovery strengthens, questions will switch from growth to inflation.
- When will consumers and investors start “chasing”? 
For More Information

Federal Reserve Bank of Kansas City – Omaha Branch

www.kansascityfed.org/omaha