The National and Midwestern Economic Outlook

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The views expressed are those of the presenter and do not necessarily reflect the positions of the Federal Reserve Bank of Kansas City or the Federal Reserve System.
Overview

- The U.S. economy has contracted sharply since the recession began.
  - Housing markets and construction activity have been very weak.
  - Financial markets and credit conditions have tightened.
  - Manufacturing activity declined dramatically as export markets weakened and consumers cut back.
  - Labor market conditions have worsened.

- The economy is beginning to show signs of recovery as policies implemented by the Federal Reserve, Treasury, Congress and President start to take hold.
Real GDP has fallen 3.7% since the recession started in December 2007.

Source: Bureau of Economic Analysis; FOMC  
Latest release: 07/31/2009
Housing and Construction Activity
Home sales have fallen sharply since late 2005, but have increased slightly over the past 3 months.
The months supply of homes has decreased lately, but remains elevated.
Home prices are well below year-ago levels.
Home price appreciation has varied widely across the nation.

Home Price Appreciation, 2009 Q1
Year-over-year percent change

Legend
- 0% and higher
- -2% to 0%
- -4% to -2%
- -6% to -4%
- -8% to -6%
- Lower than -8%

Source: Federal Housing Finance Agency
Foreclosure rates are up across the nation, but regional variation persists.

Source: Mortgage Bankers Association
Residential and commercial construction activity has slowed.

Source: U.S. Census Bureau and F.W. Dodge

Latest release: 07/27/2009
Financial Markets
Credit conditions are improving.

Corporation Bond Spreads over 10-Year Treasury

Source: Federal Reserve Board
Latest release: 07/27/2009
Banks have tightened lending standards.

Net Percentage of Banks Reporting Tighter Lending Standards

<table>
<thead>
<tr>
<th></th>
<th>Large and Medium C&amp;I Loans</th>
<th>Prime Residential Loans</th>
<th>Subprime Residential Loans</th>
</tr>
</thead>
<tbody>
<tr>
<td>Q2 2005</td>
<td>0</td>
<td>0</td>
<td>-25</td>
</tr>
<tr>
<td>Q2 2006</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Q2 2007</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Q2 2008</td>
<td>50</td>
<td>75</td>
<td>0</td>
</tr>
<tr>
<td>Q2 2009</td>
<td>90</td>
<td>100</td>
<td>-25</td>
</tr>
</tbody>
</table>

Source: Federal Reserve Board

Latest release: 05/04/2009
Stock prices have fallen substantially but have rebounded over the past few months.

Source: Dow Jones and Nasdaq
Consumers
Consumer confidence has plummeted since the recession began.
Consumers are spending less...
And saving more.

[Graph showing personal savings rate from Jun-95 to Jun-09 with data points and source information: BEA Latest release: 08/04/2009]
Manufacturing
Recent surveys indicate that manufacturing activity is stabilizing.

Source: ISM and KC Fed Manufacturing Survey

Latest release: 08/03/2009
Labor Market
Employment has fallen sharply over the past year.

Nonfarm Employment Growth
Jun-09 over Jun-08

Source: Bureau of Labor Statistics
Latest release: 07/02/2009
Unemployment rates continue to increase sharply.

Source: Bureau of Labor Statistics
Latest release: 07/02/2009
There are large regional variations in unemployment.
The education and health industries are the only industries experiencing job growth.

Private Job Growth by Industry
Jun-09 over Jun-08

Source: Bureau of Labor Statistics
Latest release: 07/02/2009
Initial unemployment claims remain elevated.

Source: Department of Labor
Latest release: 07/23/2009
Forecasts indicate that employment will continue to fall in 2010 but at a slower pace.
Policy Responses
The U.S. Policy Response

- **Federal Reserve**
  - Lowered the Fed Funds rate
  - Purchased long-term securities
  - Implemented numerous liquidity facilities

- **U.S. Treasury and Congress**
  - TARP
  - Fiscal stimulus
  - Foreclosure prevention policies
Programs implemented by the Federal Reserve have expanded its balance sheet.

Federal Reserve Balance Sheet

<table>
<thead>
<tr>
<th></th>
<th>Jan-07</th>
<th>May-07</th>
<th>Sep-07</th>
<th>Jan-08</th>
<th>May-08</th>
<th>Sep-08</th>
<th>Jan-09</th>
<th>Jun-09</th>
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</thead>
<tbody>
<tr>
<td>Longer-Term Securities</td>
<td>2,000,000</td>
<td>2,500,000</td>
<td>2,000,000</td>
<td>1,000,000</td>
<td>500,000</td>
<td>0</td>
<td>0</td>
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<tr>
<td>Liquidity to Key Credit Markets</td>
<td>1,000,000</td>
<td>1,500,000</td>
<td>0</td>
<td>500,000</td>
<td>0</td>
<td>0</td>
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<tr>
<td>Lending to Financial Institutions</td>
<td>1,000,000</td>
<td>1,500,000</td>
<td>0</td>
<td>500,000</td>
<td>0</td>
<td>0</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Traditional Security Holdings</td>
<td>1,000,000</td>
<td>1,500,000</td>
<td>0</td>
<td>500,000</td>
<td>0</td>
<td>0</td>
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</tr>
</tbody>
</table>

Source: Federal Reserve Board
Latest release: 06/03/2009
Despite expansionary monetary policy, inflation remains contained.

PCE and Core PCE Inflation
Seasonally adjusted

Source: Bureau of Economic Analysis
Latest release: 06/26/2009
Programs enacted by the federal government have increased the budget deficit.
Any Signs Of A Recovery?
Signs of recovery

- **Housing**: New and existing home sales have increased the past 3 months. Residential construction activity seems to have leveled off, and the pace of home price deterioration has slowed.

- **Financial markets**: Credit conditions have improved, and stock prices have increased sharply over the past few months.

- **Consumers**: Consumer confidence is well above its recent lows.

- **Manufacturing**: Surveys indicate that the manufacturing industry is stabilizing.

- **Labor markets**: Initial unemployment insurance claims (4-week average) have decreased since peaking in early April.
Conclusions

- The U.S. economy is in a severe recession.
  - Housing and construction activity remains extremely slow.
  - Credit conditions have improved, but financial markets are still stressed.
  - Consumer confidence remains at low levels.
  - Labor market conditions continue to deteriorate.

- The economy is showing signs of recovery.

- However, the return to potential growth is likely to be slow.
Questions?