Macroeconomic Update

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

- Financial Crisis
- Economic Recession and Recovery
- Inflation and Federal Reserve exit strategy
The financial market crisis has eased.

Commercial Paper Rates

Percent

Jun-07 Aug-07 Nov-07 Jan-08 Apr-08 Jul-08 Sep-08 Dec-08 Feb-09 May-09 Jul-09

Source: Federal Reserve Board of Governors
The financial markets still remain fragile.
Is commercial real estate a risk?

Commercial Mortgage Debt Outstanding by Type of Institution

- Commercial Banks
- Savings Institutions
- Life Insurance Companies
- ABS Issuers

Source: Federal Reserve Board of Governors
Commercial vacancy rates are on the rise.

U.S. Commercial Real Estate Vacancy Rates

Source: Torto-Wheaton Research
Agricultural bank returns are still strong.

Average Return on Assets (First Quarter)

Source: Board of Governors of the Federal Reserve and FDIC
Agricultural banks are banks with agricultural loans accounting for 14% or more of their loan portfolio.
Small commercial banks are banks with less than $500 million in assets.
Collateral requirements have tightened and loan maturities have fallen.

Collateral Requirements and Loan Maturity on Non-Real Estate Loans

Diffusion Index

Average Maturity of Non-Real Estate Loans – U.S. (Right Axis)

Collateral Required Tenth Federal Reserve District (Left Axis)

Source: Federal Reserve Bank of Kansas City and Agricultural Finance Databook
Loan delinquency rates and charge-offs edge up.

Charge-off and Delinquency Rates on Agricultural Loans

Source: Federal Reserve Board of Governors
If margins narrow, what is the future path of farmland values?

Nonirrigated Farmland Values
(Tenth Federal Reserve District)

Dollars per acre

Source: Federal Reserve Bank of Kansas City
Today’s Roadmap

- Financial Crisis
- Economic Recession and Recovery
  - The recession appears to be ending.
  - When will demand strengthen?
If forecasts hold, the bottom is near.

Real GDP Growth

Annualized percent change from previous quarter

Source: Bureau of Economic Analysis and Blue Chip Economic Indicators
Consumer spending is beginning to stabilize.

U.S. Monthly Retail and Food Sales

Billion dollars

Source: U.S. Census Bureau
A bottom in the housing market?

U.S. Residential Construction

Thousands

Billion Dollars

Single-Family Housing Starts (left axis)

Value of Private Residential Construction Put-in –Place (right axis)

Source: U.S. Census Bureau
Job losses will limit domestic spending.

U.S. Non-farm Job Growth and Unemployment Rate

Source: Bureau of Labor Statistics
Lower wealth levels will limit spending.

Assets Held by Households and Nonprofit Organization

- Financial Assets (left axis)
- Real Estate Assets (right axis)

Trillion dollars

Source: Federal Reserve Board of Governors
In the short-run, increased savings limits spending. In the long-run, best prescription to reduce debt.

Personal Savings as a Percent of Disposable Income

Source: Bureau of Economic Analysis
Food sales decline, especially at restaurants.

U.S. Food Sales

Percent change from previous year

<table>
<thead>
<tr>
<th>Year</th>
<th>Away-from-home sales</th>
<th>At-home sales</th>
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<tr>
<td>2006</td>
<td>8</td>
<td>6</td>
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<tr>
<td>2007</td>
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<tr>
<td>2008</td>
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<td>4</td>
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<tr>
<td>2009</td>
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Source: USDA
2009 data are year-to-date through June
Contractions in business activity have slowed.

U.S. Manufacturing Activity Indices

Source: Institute of Supply Management
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
Will emerging countries lead the recovery?

GDP Growth

Annual Percent Change, constant dollars

Source: International Monetary Fund, April 2009
Improvements in the U.S. trade balance continue.

Real Net Exports of Goods and Services

Source: Bureau of Economic Analysis
What is the future path of the dollar?

Value of the Dollar

Index

80 85 90 95 100 105 110 115 120

Jan-90 Jan-93 Jan-96 Jan-99 Jan-02 Jan-05 Jan-08

Broad Dollar Index

Source: Federal Reserve Board of Governors
Will foreign growth drive commodity prices?

Crude Oil and Corn Prices

Dollars per barrel

Dollars per bushel

Source: Commodity Research Bureau
Today’s Roadmap

- Financial Crisis
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- Inflation and Federal Reserve exit strategy
Monetary Policy Transmission Mechanisms

1. Short-term interest rates
2. Bank Reserves
3. Bank Credit
   Excess Reserves

Long-term Interest rates
Economic activity

Economic Review http://www.kansascityfed.org/Publicat/ECONREV/PDF/4q03sell.pdf
The Fed has expanded its balance sheet.

Federal Reserve Balance Sheet: Assets

Billion Dollars

- Short-term Lending to Financial Firms
- Rescue Operations
- Operations Focused on Broader Credit Conditions
- Other Assets
- Treasury Portfolio

Source: Federal Reserve Board of Governors
What is the future path of interest rates?

Fed Funds Rate

Source: Federal Reserve Board of Governors and CME Group
Conclusion

- The recession appears to be ending, but ...
- When will consumers spend again?
- Where will growth come from?
  - Domestic or foreign growth?
- The exit strategy depends on the “letter” of recovery.
  - L, U, V or W?
For More Information

Federal Reserve Bank of Kansas City – Omaha Branch

www.kansascityfed.org/omaha