The Economic Outlook for the U.S. and Oklahoma

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History and Structure of the Federal Reserve System

- Founded by Congress in 1913 as the nation’s third central bank, the Fed consists of 3 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 (FOMC)**: 19 members; 12 voting

- As with most central banks around the world, the Fed’s responsibilities fall within four general areas:
  - **Monetary policy** – control money supply to affect growth and inflation
  - **Lender of last resort** – provide liquidity in times of financial crisis
  - **Bank regulation** – ensure safety and soundness, consumer rights
  - **Financial services** – bank for banks, bank for federal government
Federal Reserve Districts and Office Locations
The Oklahoma City Branch Office of the Federal Reserve Bank of Kansas City

- **Branch staff and functions**
  - 35 staff involved in economic research, examining banks, and public outreach

- **2010 branch board of directors**
  - **Steve Agee** *(chairman)*, President, Agee Energy, and Professor, OCU, OKC
  - **Bill Anoatubby**, Governor, Chickasaw Nation, Ada
  - **Jim Dunn**, Chairman, Mill Creek Lumber and Supply Company, Tulsa
  - **Jacque Fiegel**, Senior EVP and COO, Coppermark Bank, OKC
  - **Rose Washington Rentie**, Executive Director, TEDC Creative Capital, Tulsa
  - **Doug Tippens**, President and CEO, Bank of Commerce, Yukon
  - **K. Vasudevan**, Chairman, Service and Technology Corp., Bartlesville
The U.S. Economy

- Credit market conditions have improved, and the U.S. economy is growing again, but the recovery is expected to be moderate.

- Inflation is expected to remain tame in the near term, but will require diligent actions to stay in check over the longer run.
Interbank lending markets have largely returned to normal in recent months.

Source: Bloomberg
And broader measures of financial stress are also nearing normal levels.

**Kansas City Financial Stress Index**

<table>
<thead>
<tr>
<th>Variables include:</th>
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<tbody>
<tr>
<td>3-mo LIBOR/TED spread</td>
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<tr>
<td>2-year swap spread</td>
</tr>
<tr>
<td>Off/on 10-yr Trs spread</td>
</tr>
<tr>
<td>Aaa/10-yr Trs spread</td>
</tr>
<tr>
<td>Baa/Aaa spread</td>
</tr>
<tr>
<td>Junk/Baa spread</td>
</tr>
<tr>
<td>Cons ABS/5-yr Trs spread</td>
</tr>
<tr>
<td>Corr of stock/bond returns</td>
</tr>
<tr>
<td>Volatility of stocks (VIX)</td>
</tr>
<tr>
<td>Volatility of bank stocks</td>
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<tr>
<td>Dispersion of bank stocks</td>
</tr>
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Source: KCFRB
Early 2010 data show continued improvement in the U.S. economy

National Business Indexes and Payroll Employment

Change from previous month, thousands

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

Heading forward, Fed policymakers generally expect a moderate recovery.
With unemployment remaining high for some time...

Unemployment Rate
Seasonally Adjusted

Source: U.S. Bureau of Labor Statistics, FOMC
One reason is credit standards are much tighter than a few years ago.

Source: FRB Senior Loan Officer Survey
But another is that loan demand remains very sluggish

Net Percentage of Banks Reporting Increased Loan Demand

Source: FRB Senior Loan Officer Survey
Inflation is expected to remain tame in the near term, but will require careful oversight.

PCE Inflation Index

Source: U.S. Bureau of Economic Analysis, FOMC
The Fed’s balance sheet is still large, with extra assets now largely MBS.
The Oklahoma Economy

- As usual in recessions, Oklahoma entered this recession later than the nation—not joining until energy prices fell in late 2008.

- After steep declines for much of 2009, the state is showing recent signs of recovery—and conditions remain better than the nation.
Oklahoma usually enters recessions late but leaves around the same time as the nation.

Average Recession Path, 1956-2006
Employment level 4 quarters before and 8 quarters after U.S. jobs peak

Indexed to U.S. jobs peak

Source: U.S. Bureau of Labor Statistics
Oklahoma entered this recession 3 quarters late and appears to be leaving one quarter late.

*Only one week of March

Source: Bureau of Labor Statistics
Manufacturing surveys show solid output recovery in Oklahoma, slightly delayed

Source: ISM, FRBKC Manufacturing Survey
Revised state jobs data show a similar story of very late entry, slightly late exit.

Nonfarm Payroll Employment Growth

Year-over-year percent change

Source: U.S. Bureau of Labor Statistics
Oklahoma City held up better in 2009 than Tulsa, due largely to less manufacturing
Unemployment remains well below the national average throughout the state

Unemployment Rate
Seasonally Adjusted*

Percent

<table>
<thead>
<tr>
<th></th>
<th>Jan-08</th>
<th>Jan-10</th>
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<tbody>
<tr>
<td>U.S.</td>
<td>4.9</td>
<td>9.7</td>
</tr>
<tr>
<td>Oklahoma</td>
<td>3.5</td>
<td>6.7</td>
</tr>
<tr>
<td>OKC metro</td>
<td>3.5</td>
<td>6.1</td>
</tr>
<tr>
<td>Tulsa metro</td>
<td>3.5</td>
<td>7.5</td>
</tr>
<tr>
<td>Lawton metro</td>
<td>3.6</td>
<td>5.4</td>
</tr>
<tr>
<td>Non-metro OK</td>
<td>3.5</td>
<td>6.7</td>
</tr>
</tbody>
</table>

Source: U.S. Bureau of Labor Statistics

* Estimated by FRBKC
Indeed, our entire region maintains relatively low unemployment rates.
Home prices clearly held up better here, providing cushion to consumers and banks.

Quality-Adjusted Home Price Growth
Purchase-Only

Percent change year-over-year

Source: FHFA
Mortgages are in much better position in Oklahoma than in the nation or even region.
Banks in the state also remain in much better shape than in the nation.

Noncurrent Loans as a Share of Total Loans
Commercial Banks

Source: FDIC
OKC and Tulsa home prices have caught up with some other regional cities.
But weakening natural gas prices provide a risk relative to the nation

Energy Prices

Source: Bloomberg
The U.S. economy is growing again, but recovery speed is expected to be modest.

Near-term inflation risks remain low, but long-term risks will require diligent action.

Oklahoma’s economy is showing signs of recovery, and from a better level, but recent natural gas price trends are a risk.