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 recovery is expected to be moderate, as debt and uncertainty remain high

- Inflation is expected to remain tame in the near term, but longer-run risks exist
Broad measures of financial stress are nearing normal levels

Kansas City Financial Stress Index

Variables include:
- 3-mo LIBOR/TED spread
- 2-year swap spread
- Off/on 10-yr Trs spread
- Aaa/10-yr Trs spread
- Baa/Aaa spread
- Junk/Baa spread
- Cons ABS/5-yr Trs spread
- Corr of stock/bond returns
- Volatility of stocks (VIX)
- Volatility of bank stocks
- Dispersion of bank stocks

Source: KCFRB
First quarter GDP growth was solid but not robust

Growth in Components of GDP

Percent change from the previous period

Source: U.S. Bureau of Economic Analysis
U.S. employment is finally growing

National Payroll Employment

Change from previous month, thousands

Heading forward, Fed policymakers expect a moderate GDP recovery

Gross Domestic Product

Percent change, year-over-year

Source: U.S. Bureau of Economic Analysis, FOMC
With unemployment remaining high for some time
Consumer debt could constrain short-run growth and federal debt projections are a concern.

U.S. Debt as a Share of GDP

Sources: Federal Reserve, BEA, CBO
Both business and consumer loan demand remain 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 much later than the nation, and is recovering with only a slight delay

- Most sectors are growing, and conditions remain much better than in the nation

- But low natural gas prices are a risk
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
A fairly similar pattern appears to be playing out this time, though with bigger job losses.
The most up-to-date labor market indicators show further OK improvement in April.

Initial Claims for Unemployment Insurance

Index (Apr-05=100)

*Does not include last week of April

Source: Bureau of Labor Statistics
And monthly state jobs data are on an upward trend, only slightly delayed.
Oklahoma City held up better in 2009 than Tulsa, due largely to less manufacturing.
With our shorter recession, unemployment is lower than U.S. across the state.

Unemployment Rate
Seasonally Adjusted*

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<th>Location</th>
<th>Dec-07</th>
<th>Mar-10</th>
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<td>U.S.</td>
<td>5.0</td>
<td>9.7</td>
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<td>OKC metro</td>
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<tr>
<td>Tulsa metro</td>
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<td>Lawton metro</td>
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</tr>
<tr>
<td>Non-metro OK</td>
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Source: U.S. Bureau of Labor Statistics

* Estimated by FRBKC
Indeed, our entire region maintains relatively low unemployment rates.
Manufacturing surveys show solid output recovery in Oklahoma, slightly delayed

Manufacturing PMI Indexes
Seasonally adjusted, 3-month moving avg.

Source: ISM, FRBKC Manufacturing Survey
Oklahoma’s rig count has risen 75% since September, but leveled off recently.

Source: Baker Hughes
Home prices clearly held up better here, providing cushion to consumers and banks.
Mortgages are in much better position in Oklahoma than in the nation or even region.
Overall, banks in the state remain in much better shape than in the nation.
Commercial real estate is also in better condition than the nation, but is a risk

Office Vacancy Rates

Source: Torto Wheaton
But natural gas prices are the biggest risk relative to the nation.
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.