

Jason Henderson
Vice President and Branch Executive
Federal Reserve Bank of Kansas City – Omaha Branch
www.kansascityfed.org/omaha
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Economic Conditions



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

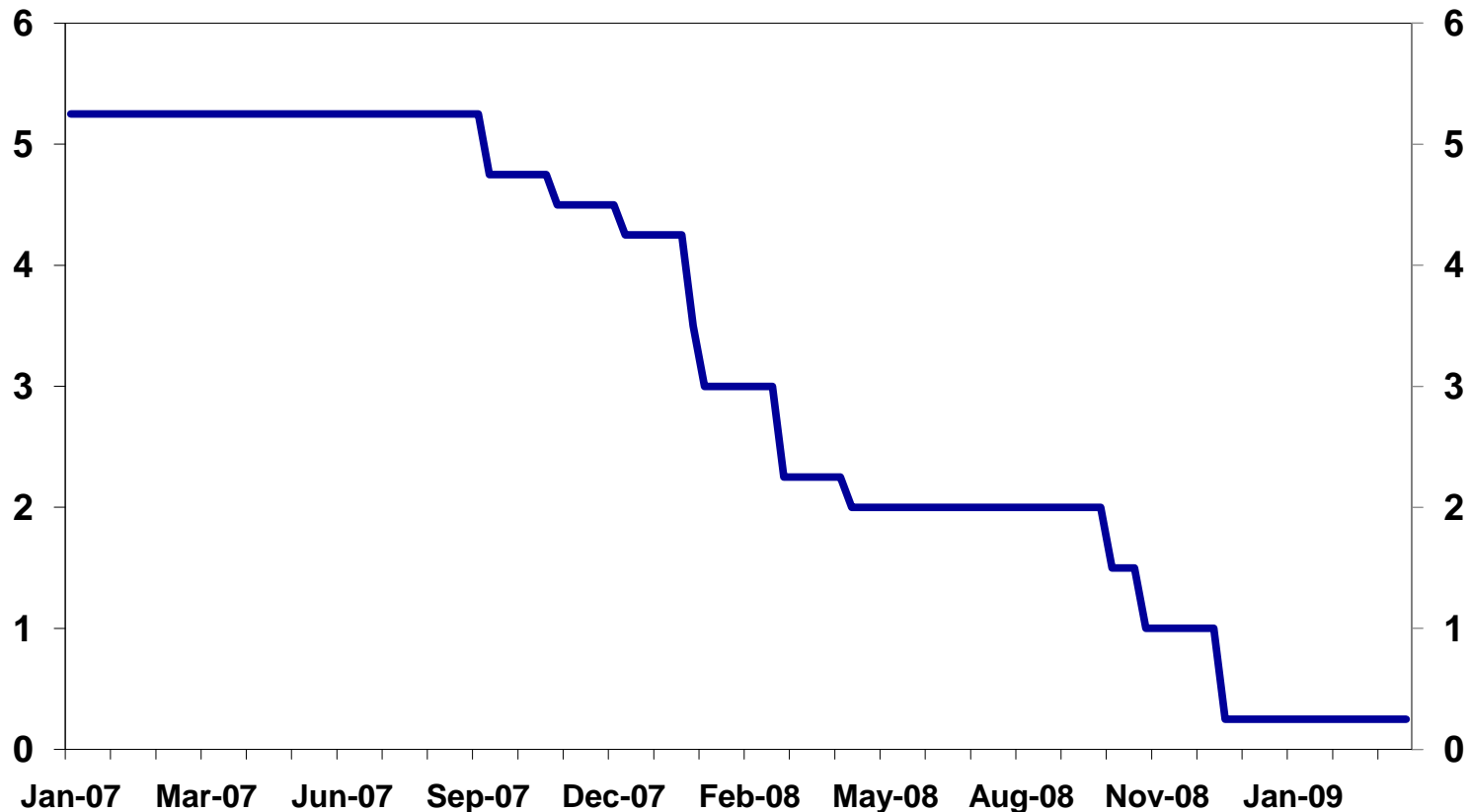
- **Monetary Policy 101**
- **“Glimmers of Hope”**
 - **The Financial Crisis Eases**
 - **A Softer Economic Contraction**
- **What is the Impact on Agriculture?**



What happens to monetary policy at the zero bound?

Fed Funds Rate

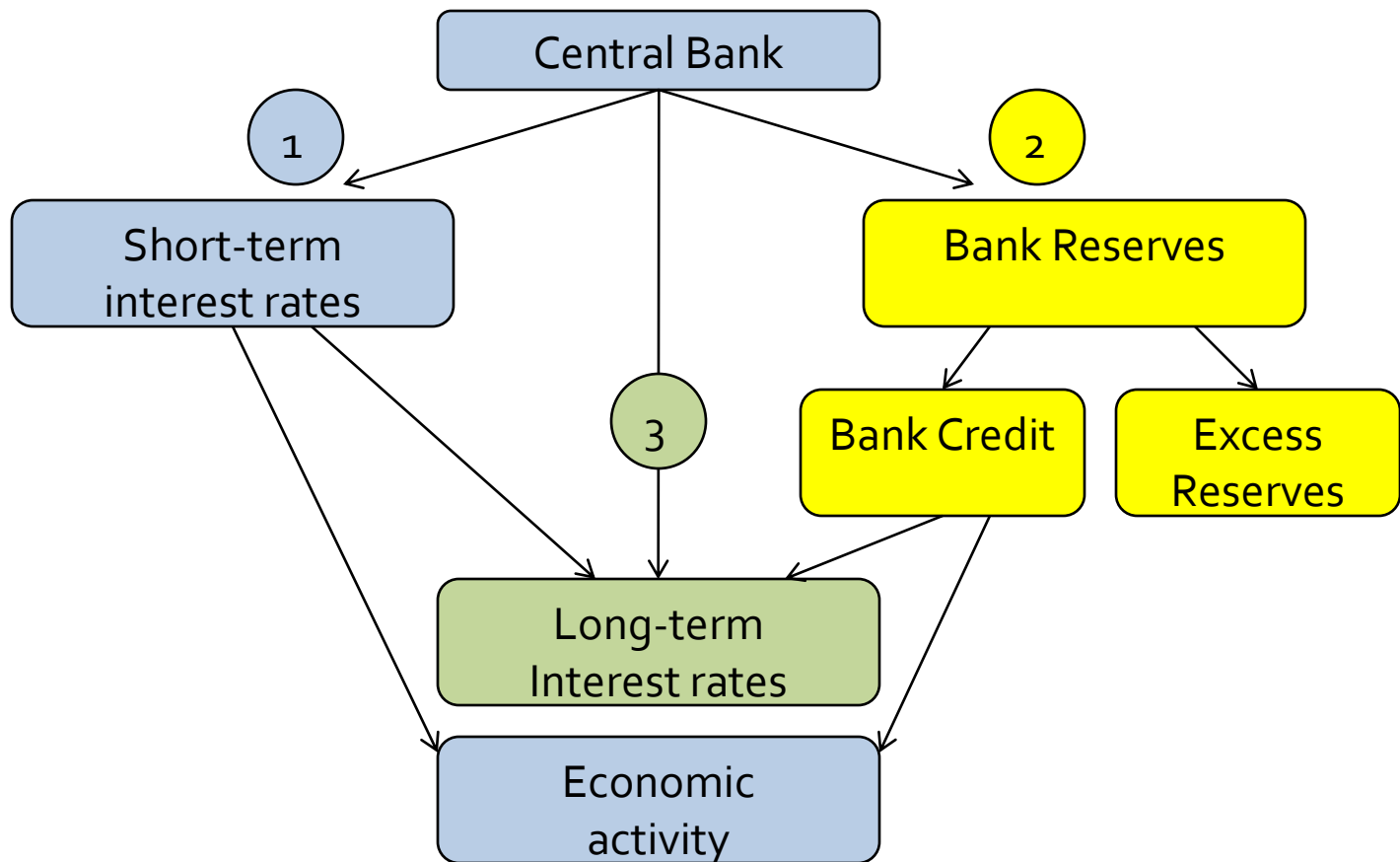
Percent



Source: Federal Reserve Board of Governors



Monetary Policy Transmission Mechanisms



Source: Gordon Sellon (2003) "Monetary Policy and the Zero Bound: Policy Options When Short-Term Rates Reach Zero"
Economic Review <http://www.kansascityfed.org/Publicat/ECONREV/PDF/4q03sell.pdf>

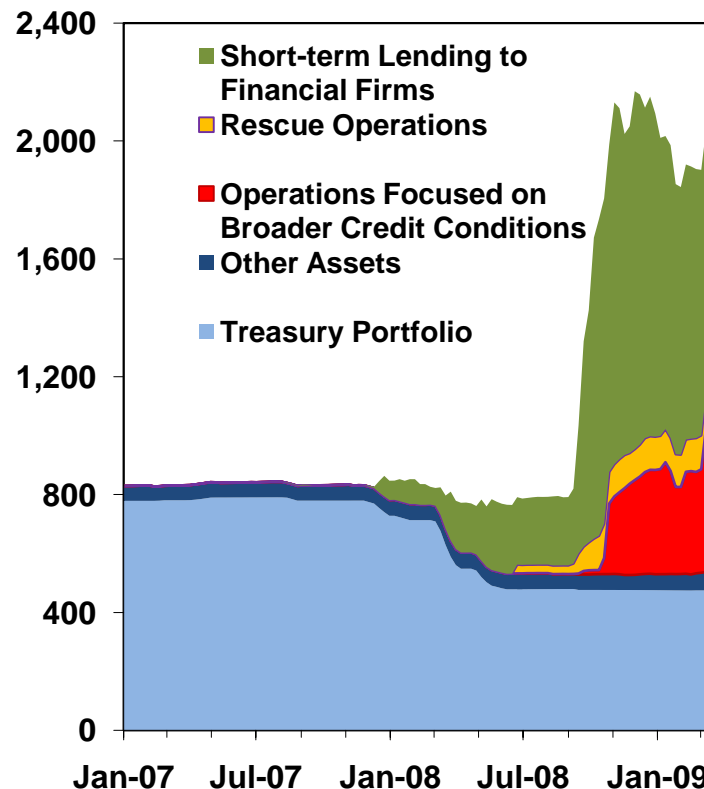


The Fed has expanded its balance sheet to extend credit to banks.

- Prior to September 2008, the Fed was sterilizing liquidity injections to capital markets.
 - Expansion of short-term lending through Term Auction Facility (TAF) - **Green**
 - Offset by lower treasury portfolio - **Blue**
- After September 2008, Fed unable to sterilize liquidity injections.
 - Creation of Commercial Paper Funding Facility and holdings of agency MBS - **Red**
- Further expansions in 2009,
 - The Term Asset-backed Securities Loan Facility (TALF) acquires consumer loans – **Red**
 - Purchase of long-term treasuries - **Green**

Federal Reserve Balance Sheet

Billions of Dollars



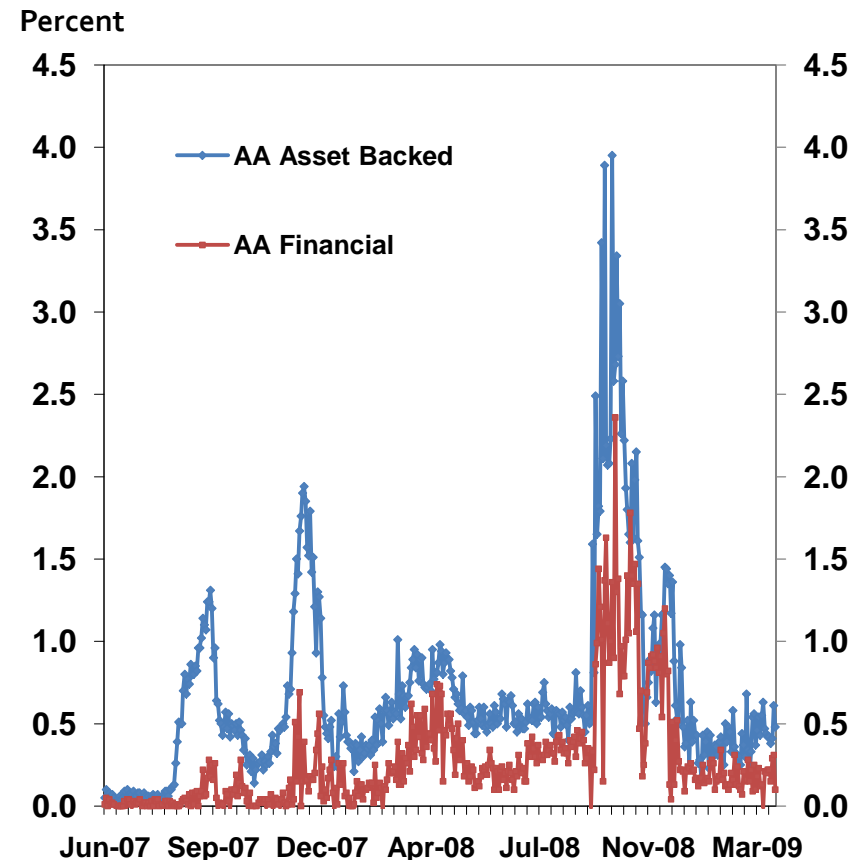
Source: Federal Reserve Board of Governors



Financial market stress has eased, but markets remain fragile.

- Interest rate spreads indicate market risk.
 - Higher risk = Higher rates
- In 2007, spreads on asset-based (mortgage) rates rose sharply.
- In Sept. 2008, risks and interest rate spreads rose sharply in financial markets

Commercial Paper Rates Spreads
(Difference from Nonfinancial Commercial Paper)



Source: Federal Reserve Board of Governors

The FOMC is Battling Deflation

- Deflation: *A decline in general price levels,*
 - *often caused by a reduction in the supply of money or credit.*
 - *brought about by direct contractions in spending, either in the form of a reduction in government spending, personal spending or investment spending.*
- “In light of increasing economic slack here and abroad, the Committee expects that **inflation will remain subdued**. Moreover, the Committee sees some risk that **inflation could persist for a time below rates that best foster economic growth and price stability in the longer term.**”

*FOMC Statement
March 18, 2009*



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Consumers



Business Investment



Net Exports



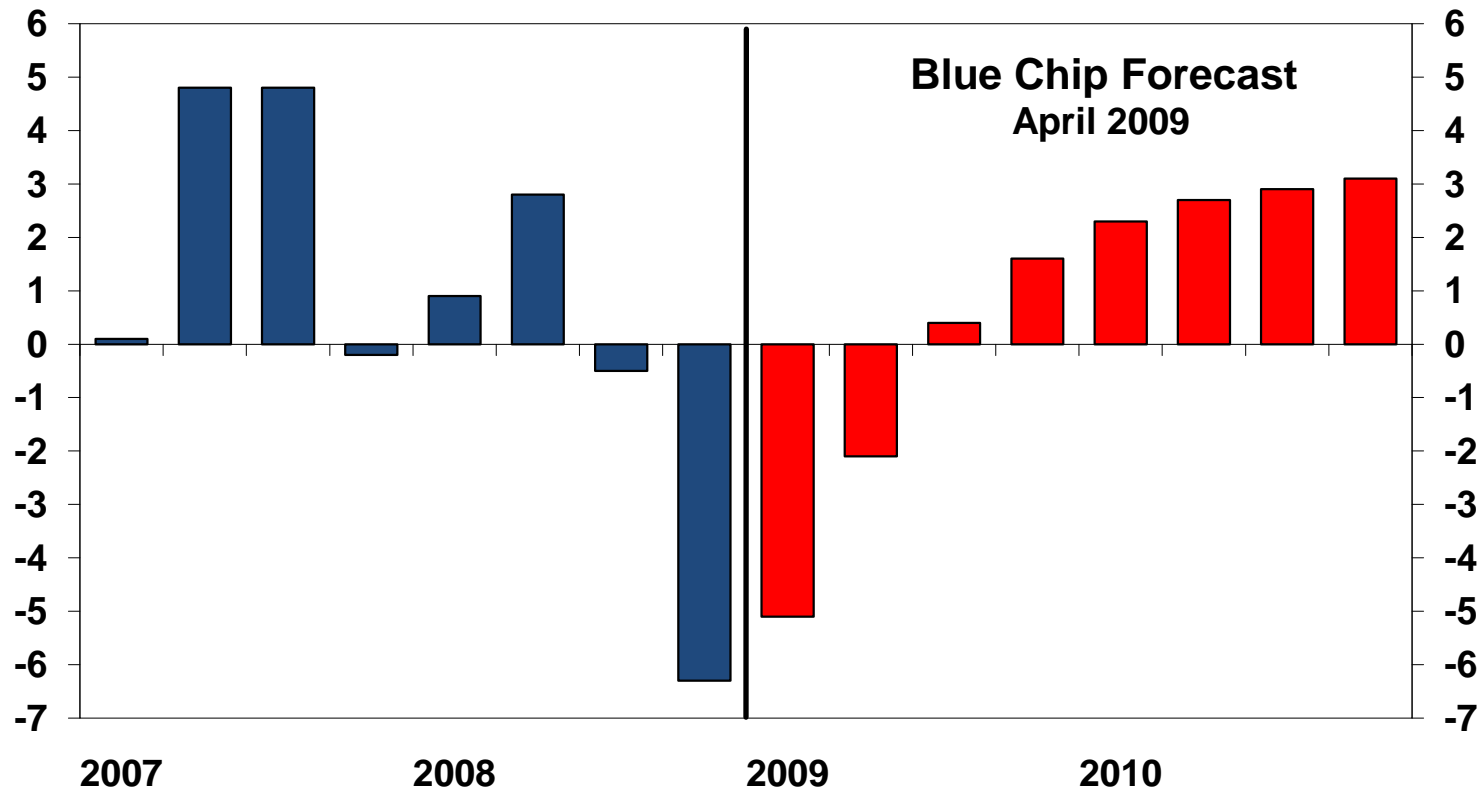
Government



The U.S. economy is in recession.

Real GDP Growth

Annualized percent change from previous quarter



Source: Bureau of Economic Analysis and Blue Chip Economic Indicators



Length of U.S. Recessions

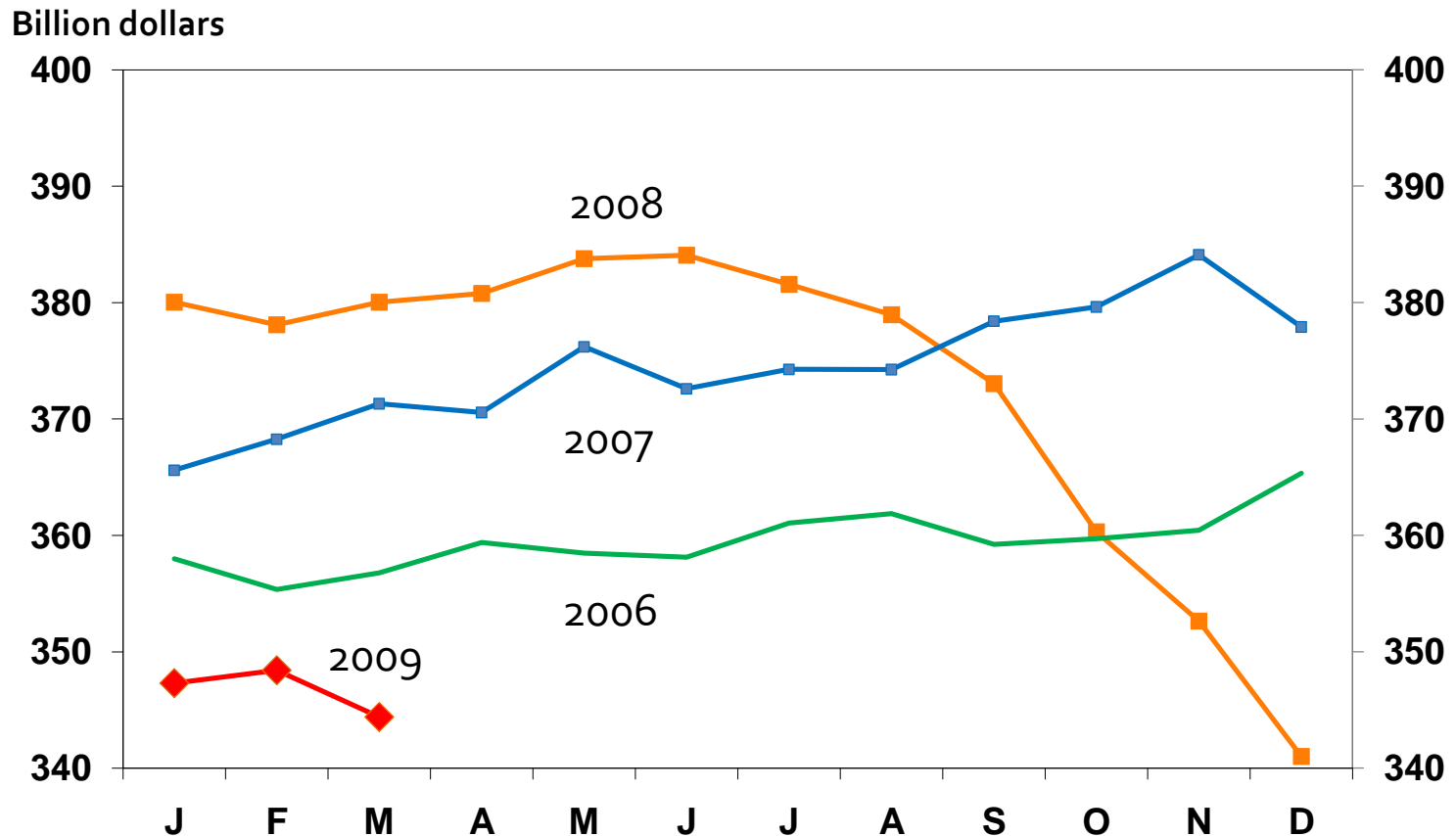
Start	End	Length (Months)
Nov. 1973	Mar. 1975	16
Jan. 1980	Jul. 1980	6
Jul. 1981	Nov. 1982	16
Jul. 1990	Mar. 1991	8
Mar. 2001	Nov. 2001	8
Dec. 2007	???	
Average since World War II		10

Source: NBER



Consumer spending slowed in March, but was revised up in January and February.

U.S. Monthly Retail and Food Sales

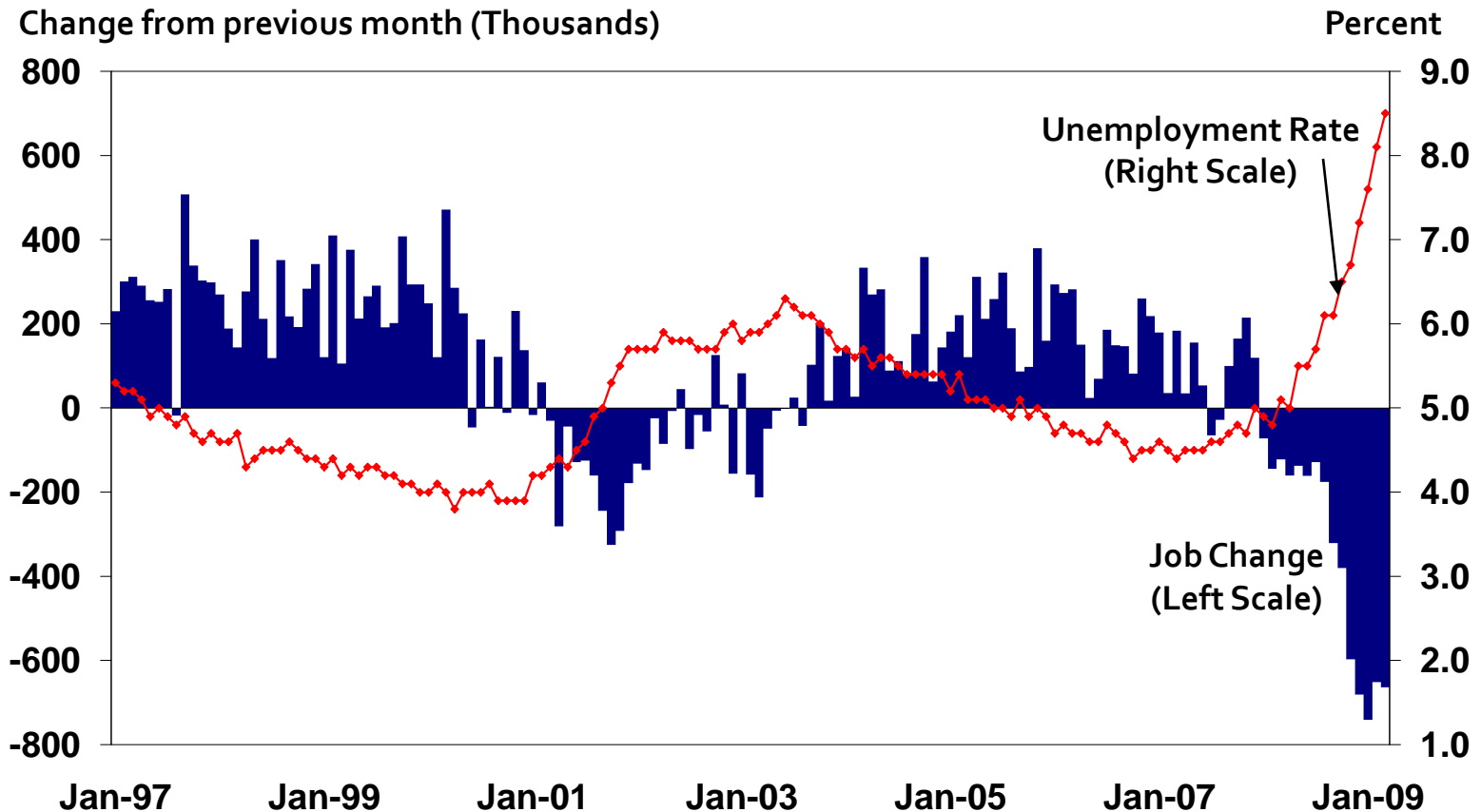


Source: U.S. Census Bureau



While unemployment rates rise, job losses do not accelerate further.

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

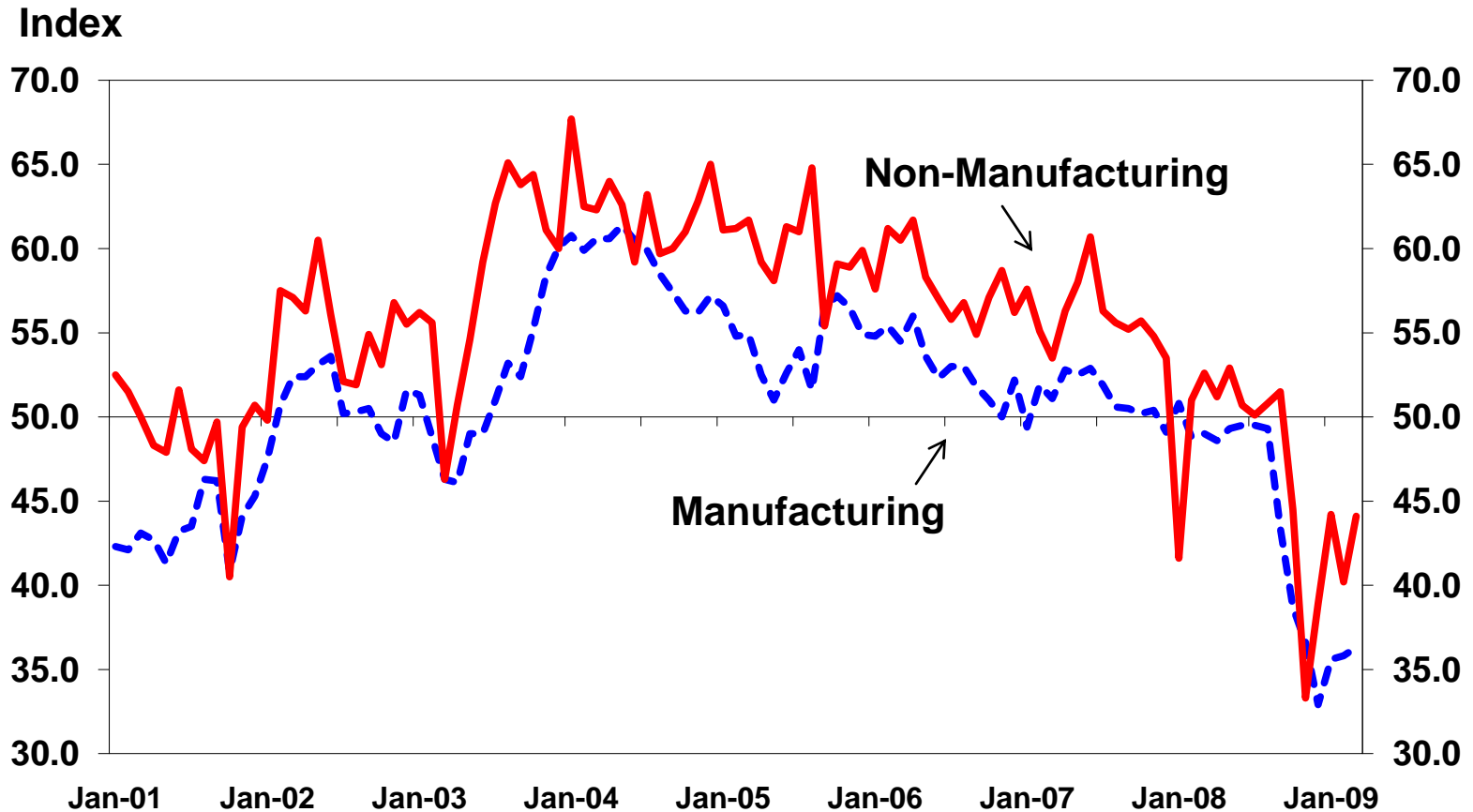


Source: Bureau of Labor Statistics



Contractions in business activity have slowed.

U.S. Manufacturing Activity Indices



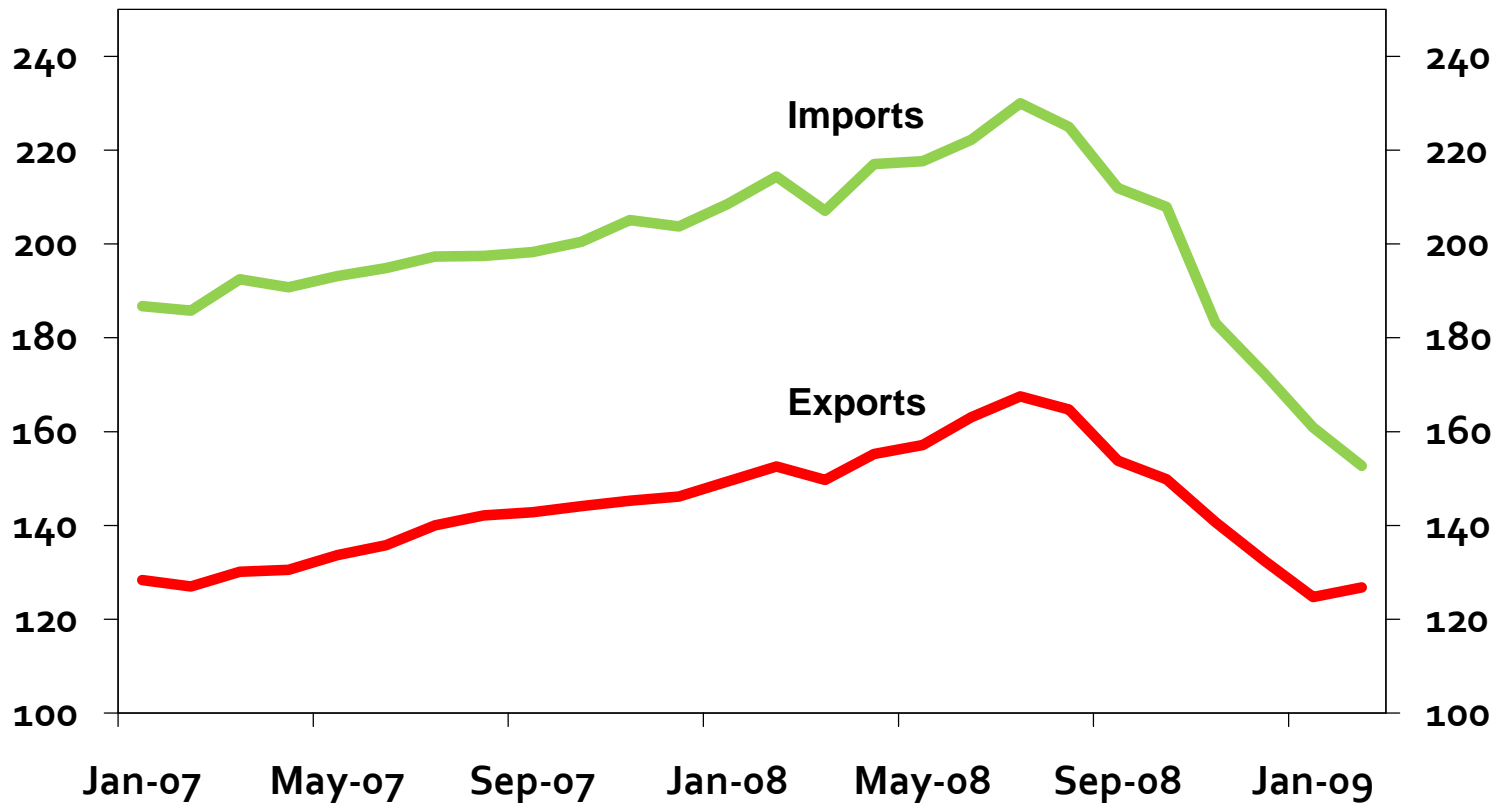
Source: Institute of Supply Management



Export activity edged up in February.

U.S. Exports and Imports

Billion dollars



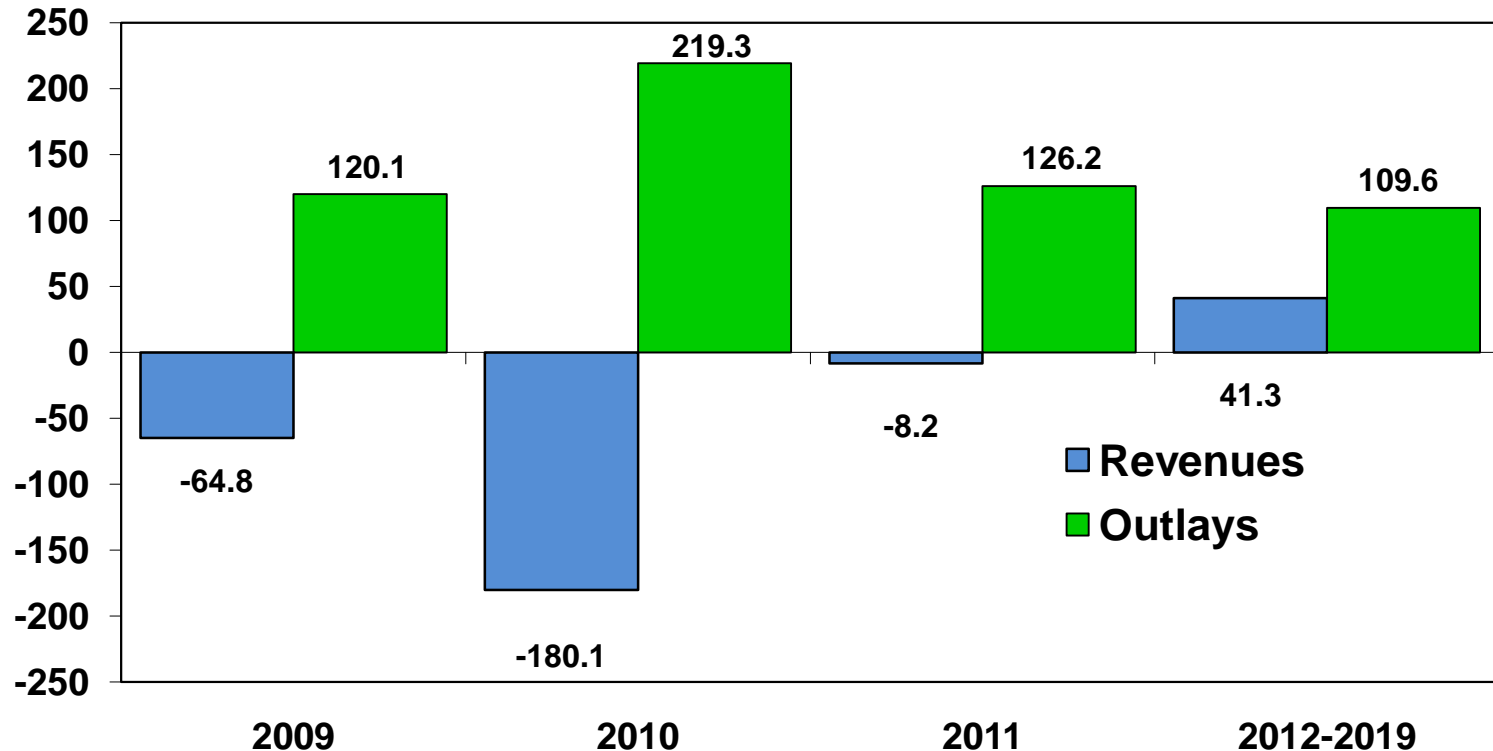
Source: Census Bureau



Will the stimulus package work?

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

Billion Dollars



Source: Congressional Budget Office, February 13, 2009



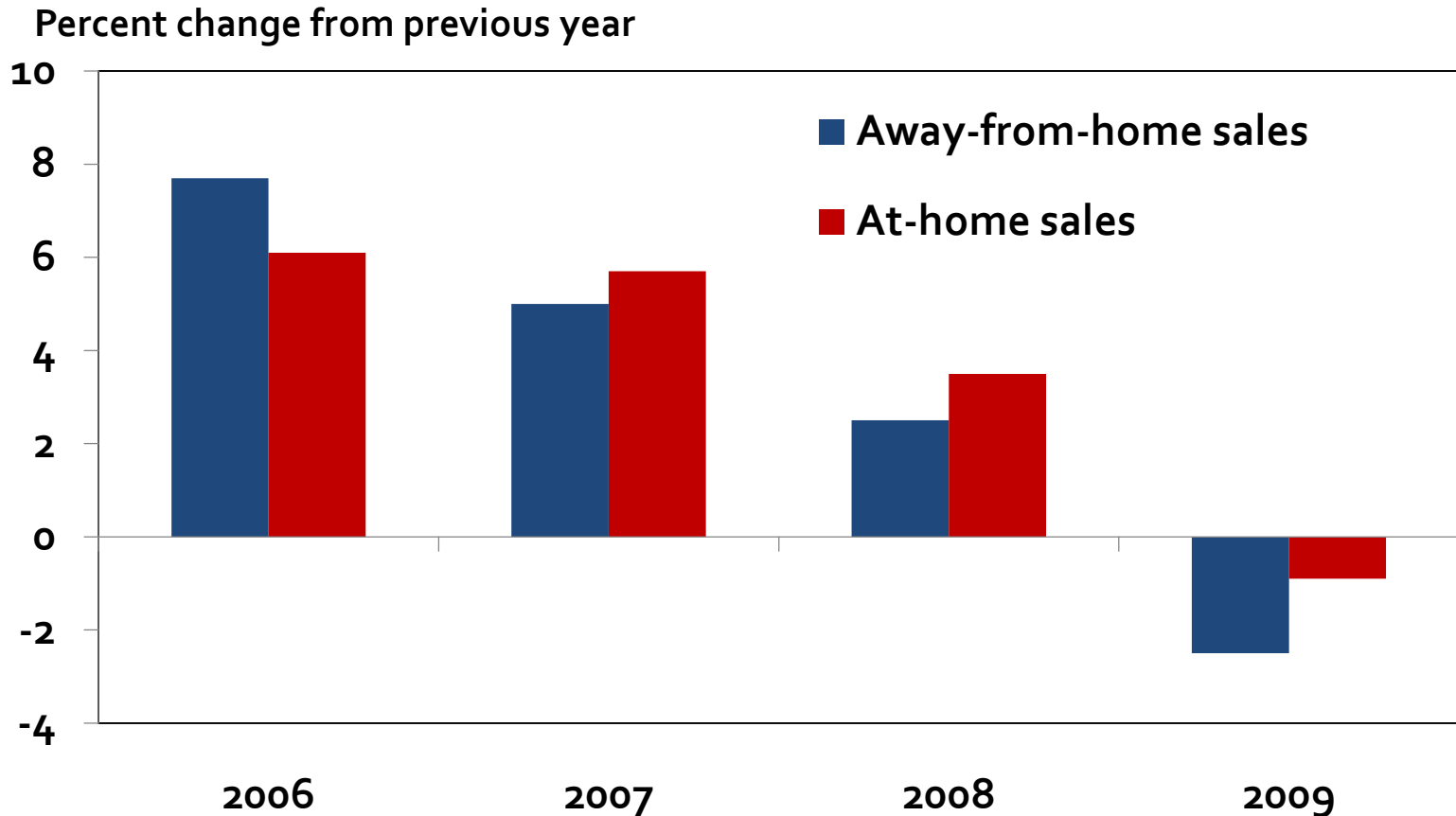
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 - Credit remains available, although credit standards tighten.



Food sales decline, especially at restaurants.

U.S. Food Sales



Source: USDA

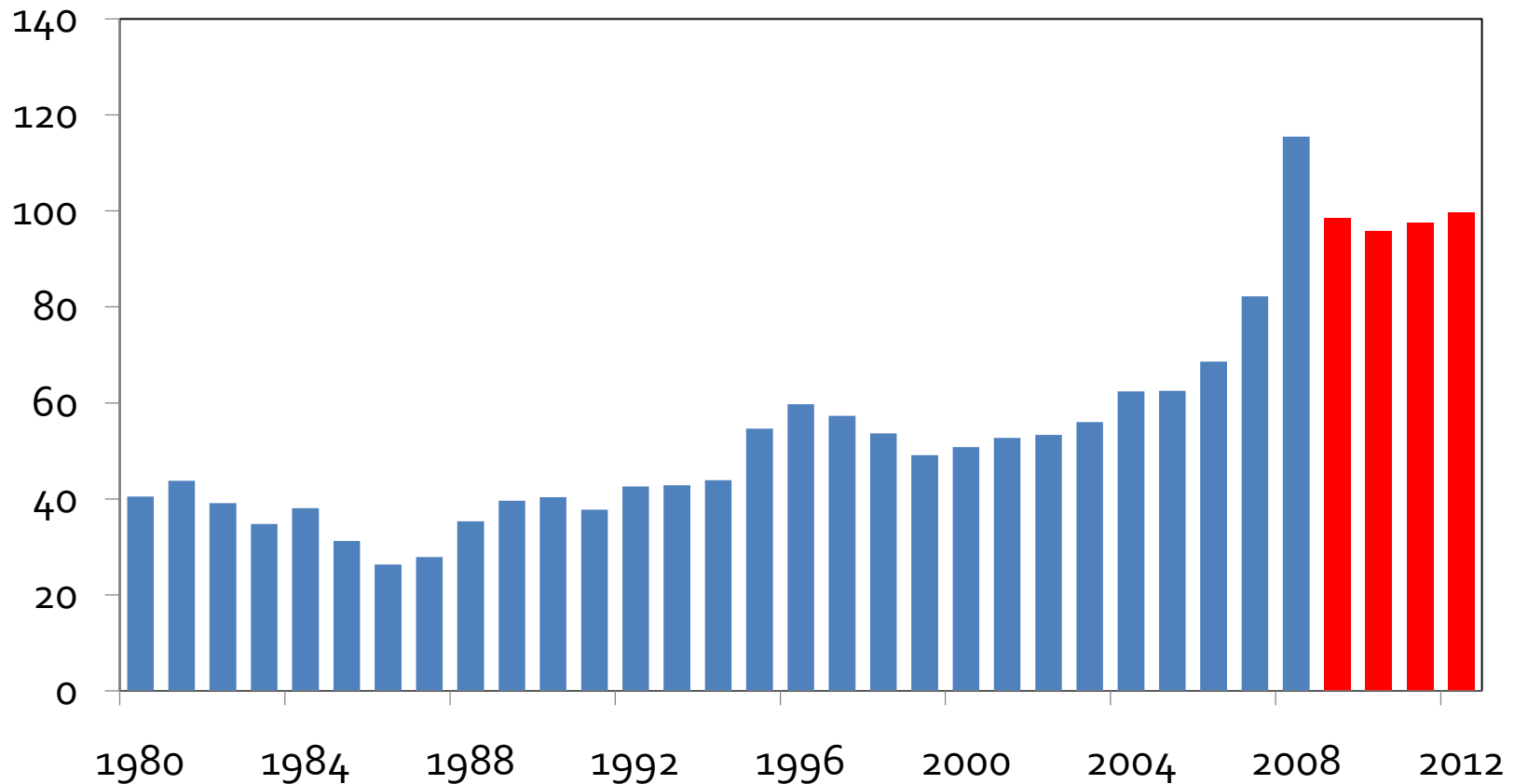
2009 data are year-to-date through February



Agricultural exports fall in 2009, but remain above historical levels.

U.S. Agricultural Exports

Billion dollars

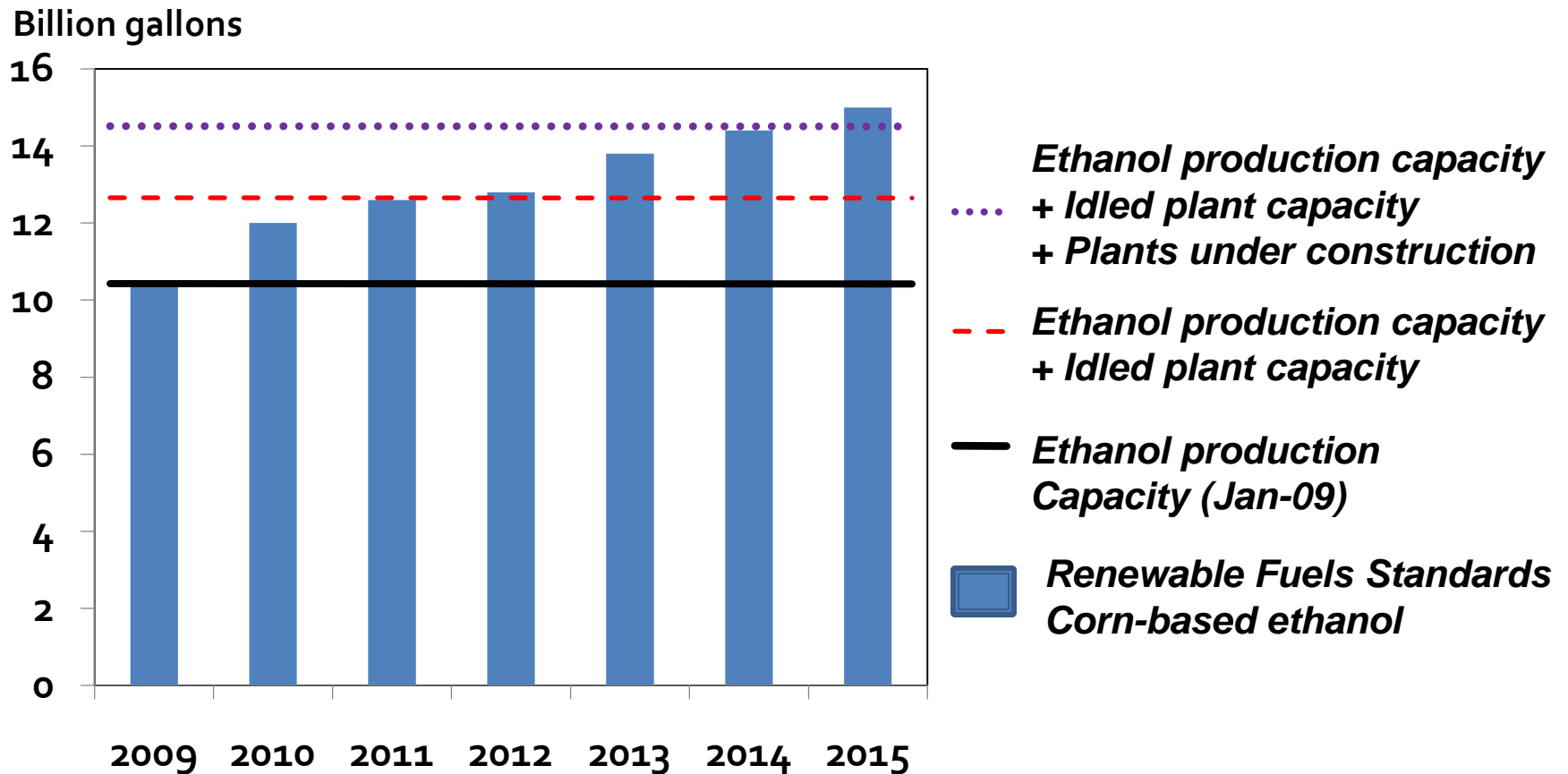


Source: USDA, fiscal years



Ethanol demand growth will slow.

Corn-based Ethanol Mandate in Renewable Fuels Standards

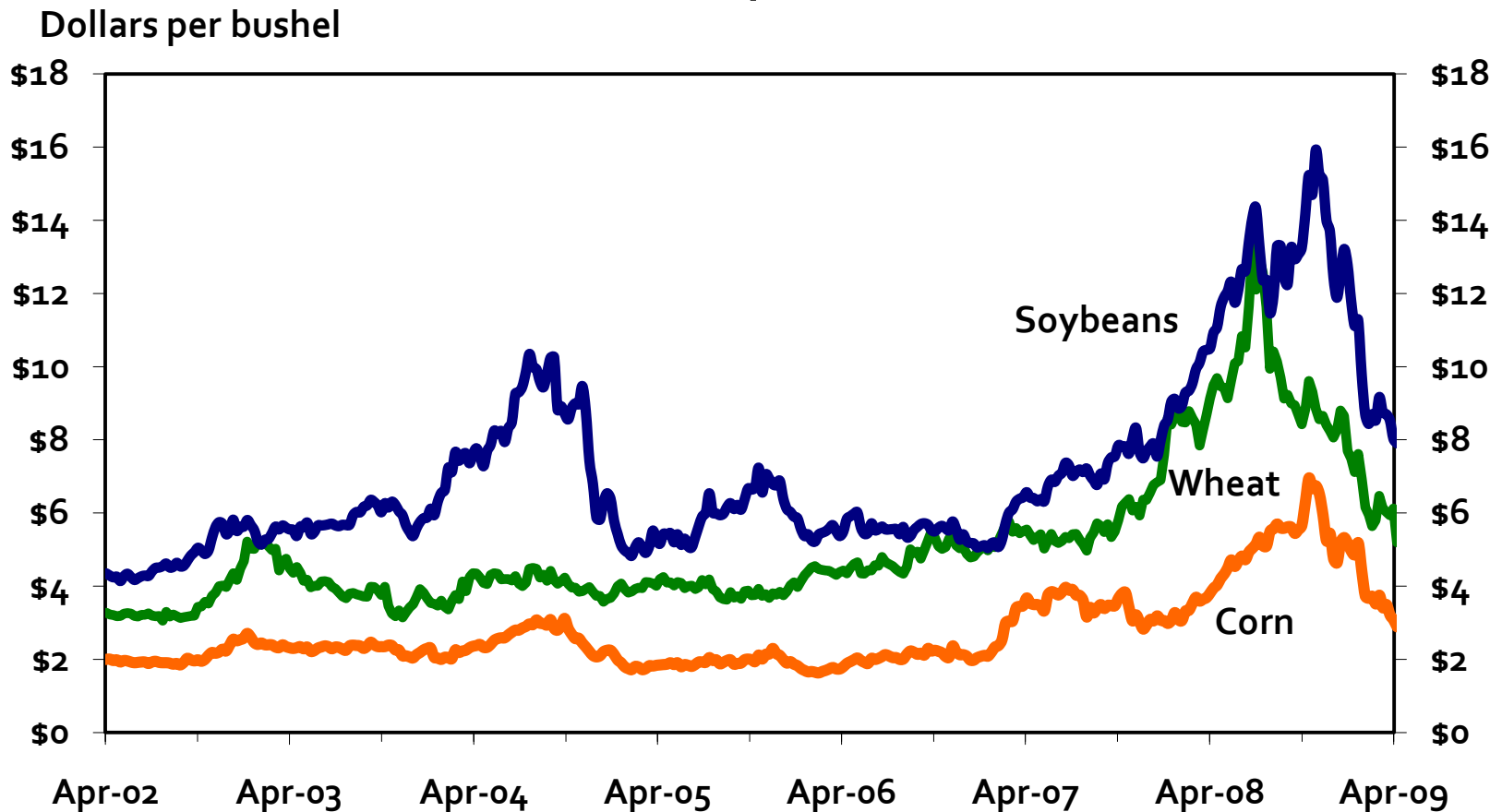


Source: Renewable Fuels Association and FAPRI



Crop prices fall with weaker demand, but remain above historical trends.

U.S. Crop Prices

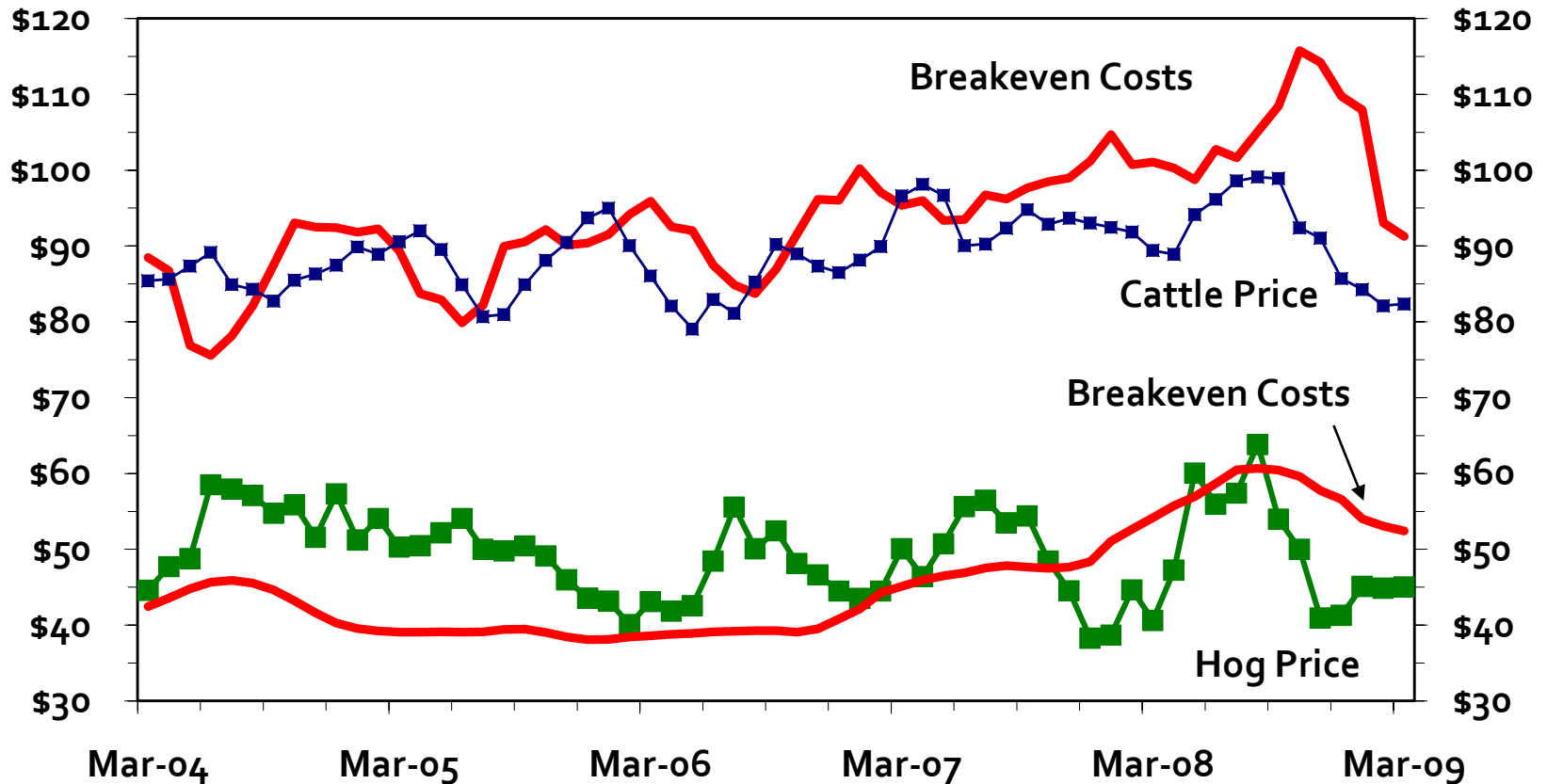


Source: Commodity Research Bureau

Profits remain elusive, despite lower production costs.

U.S. Livestock Prices and Breakeven Costs

Dollars per hundredweight

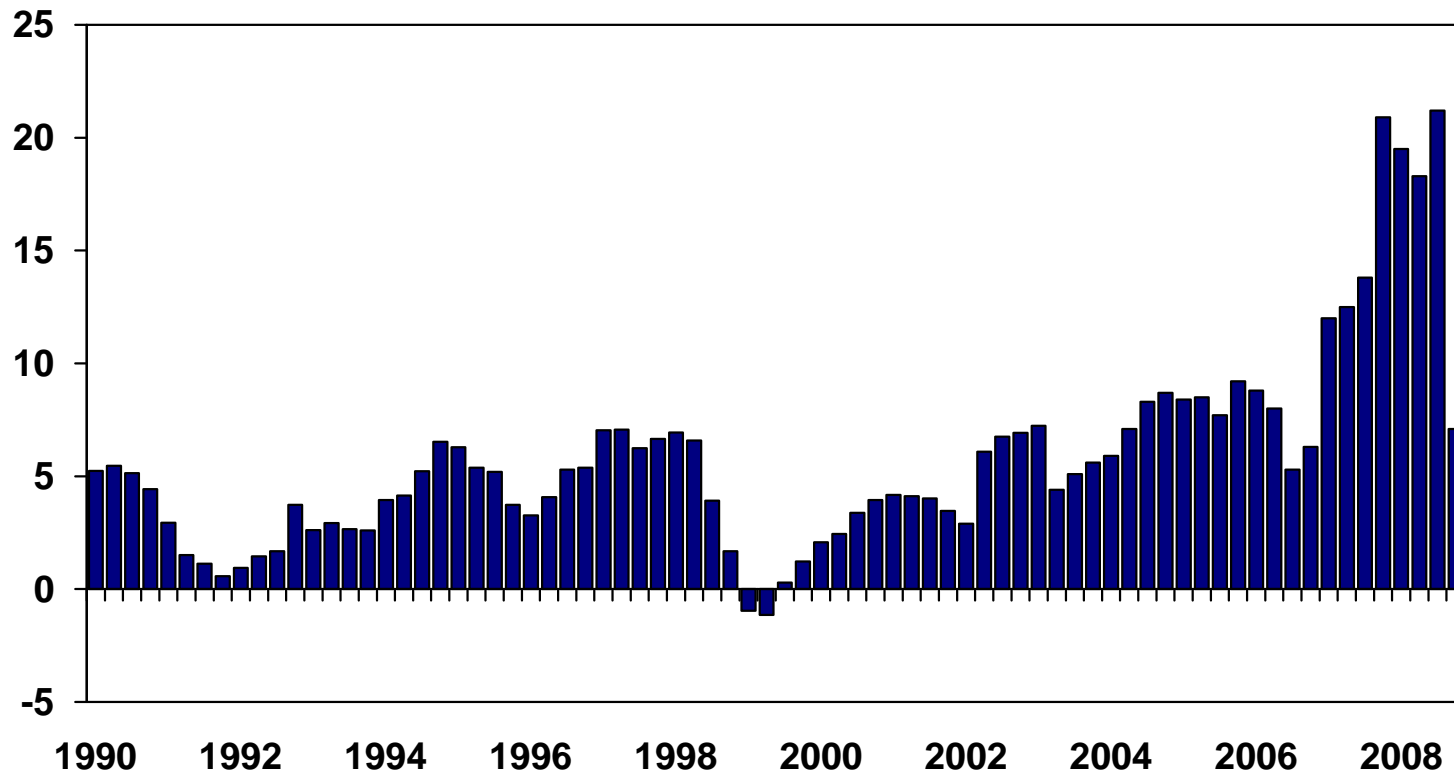


Source: USDA and Iowa State University

If farm incomes wane, what will happen to farmland values?

Nonirrigated Cropland Values (Tenth Federal Reserve District)

Sample percent change from a year ago*



Source: Federal Reserve Bank of Kansas City

*Percent changes are calculated using responses only from those banks reporting in both the past and the current quarter.

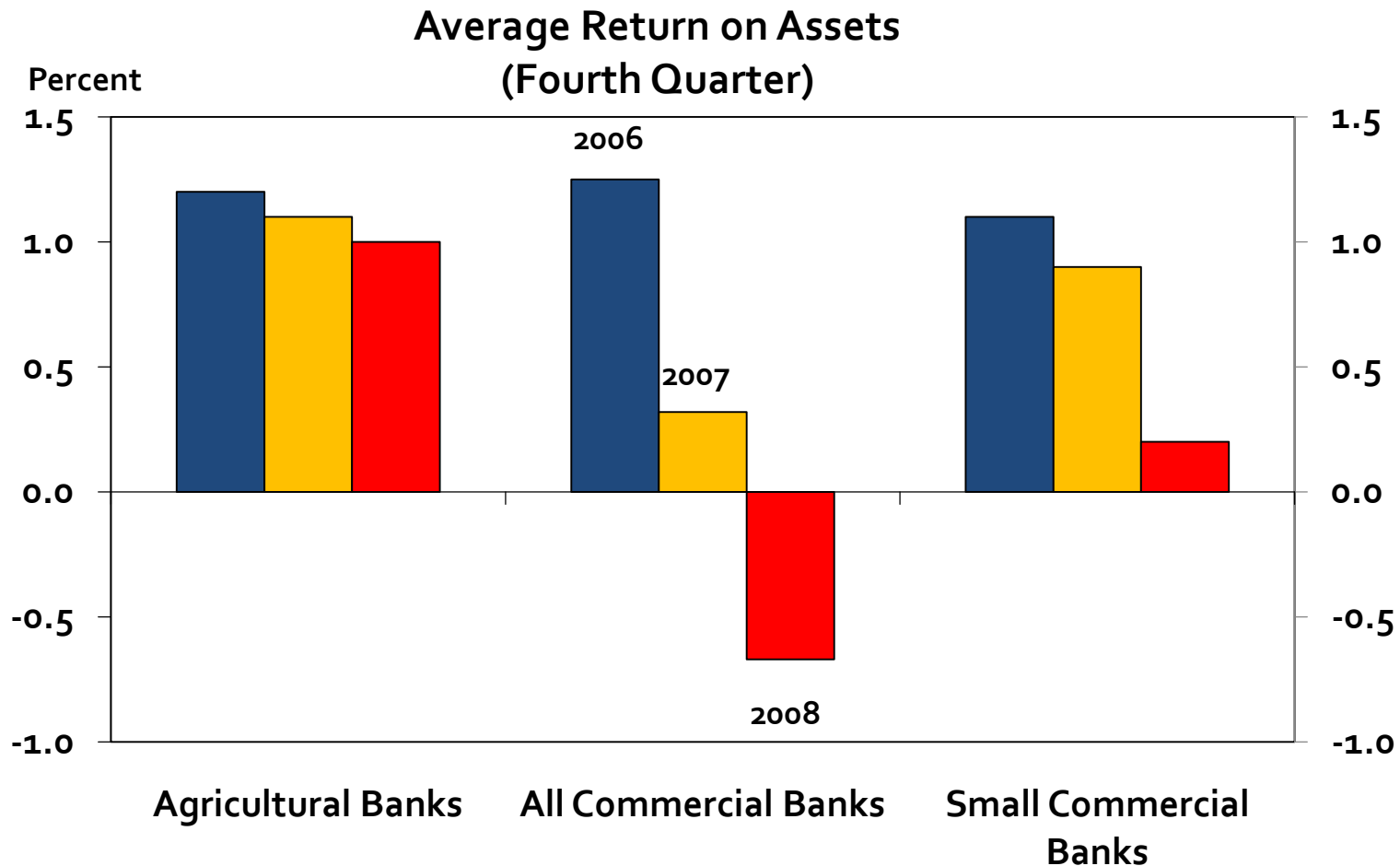


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Agricultural bank returns are still strong.



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.

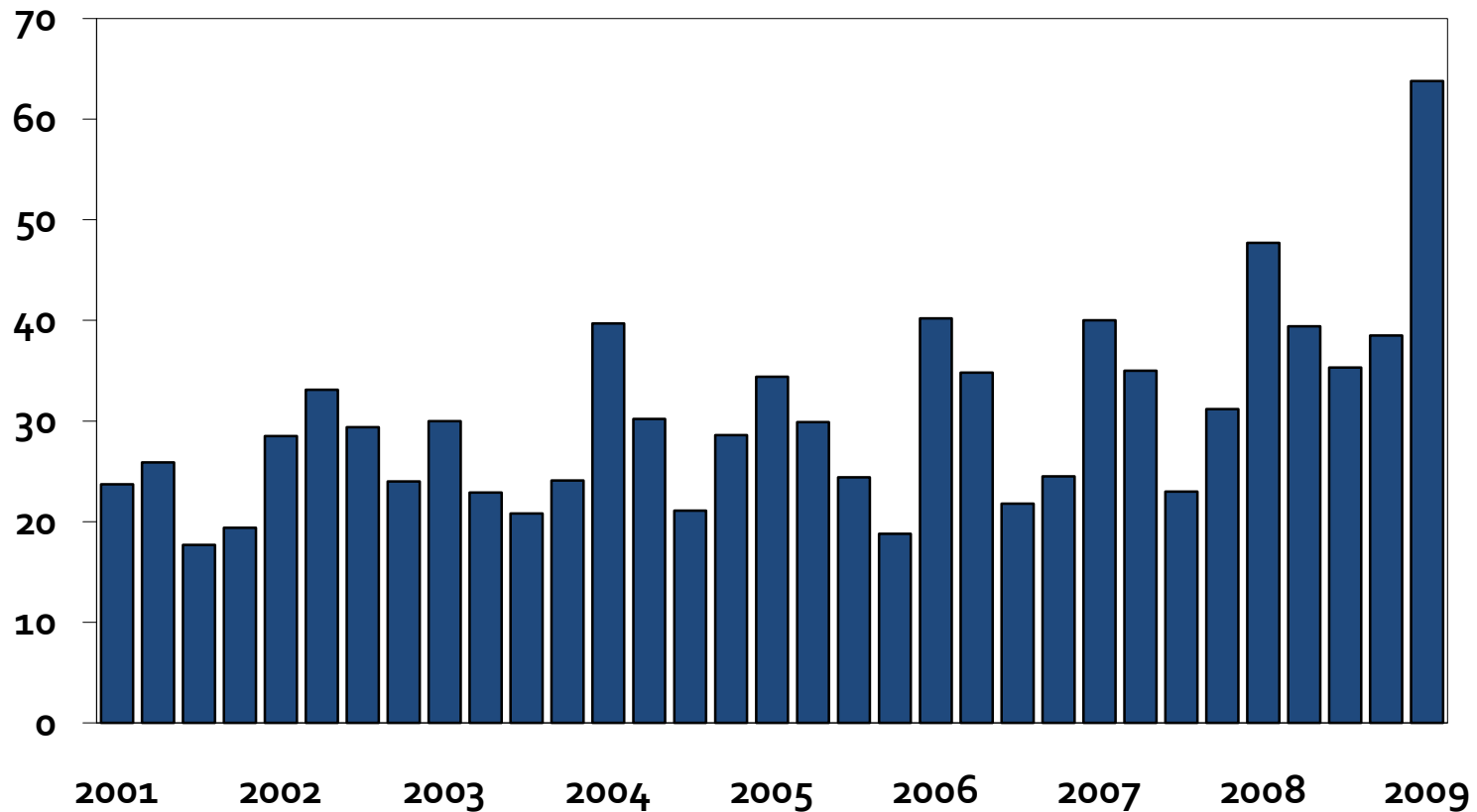
Small commercial banks are banks with less than \$500 million in assets



Commercial banks extend credit to farmers.

Volume of Non-Real Estate Bank Loans to Farmers (Current Operating Expenses)

Billions of dollars



Source: *Agricultural Finance Databook*



Conclusions

- **The U.S. is in the midst of a steep recession.**
- **“Glimmers of Hope” are emerging amid a fragile financial market and slower contractions in economic activity.**
- **The Recession Catches the Ag Economy.**
 - Agricultural demand collapses.
 - Lower commodity prices trim farm income.
 - Credit conditions tighten with increased risk.
- **When Will Fiscal and Monetary Stimulus Spark a Rebound?**

