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The State of Our Economy: The National and State Perspective



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

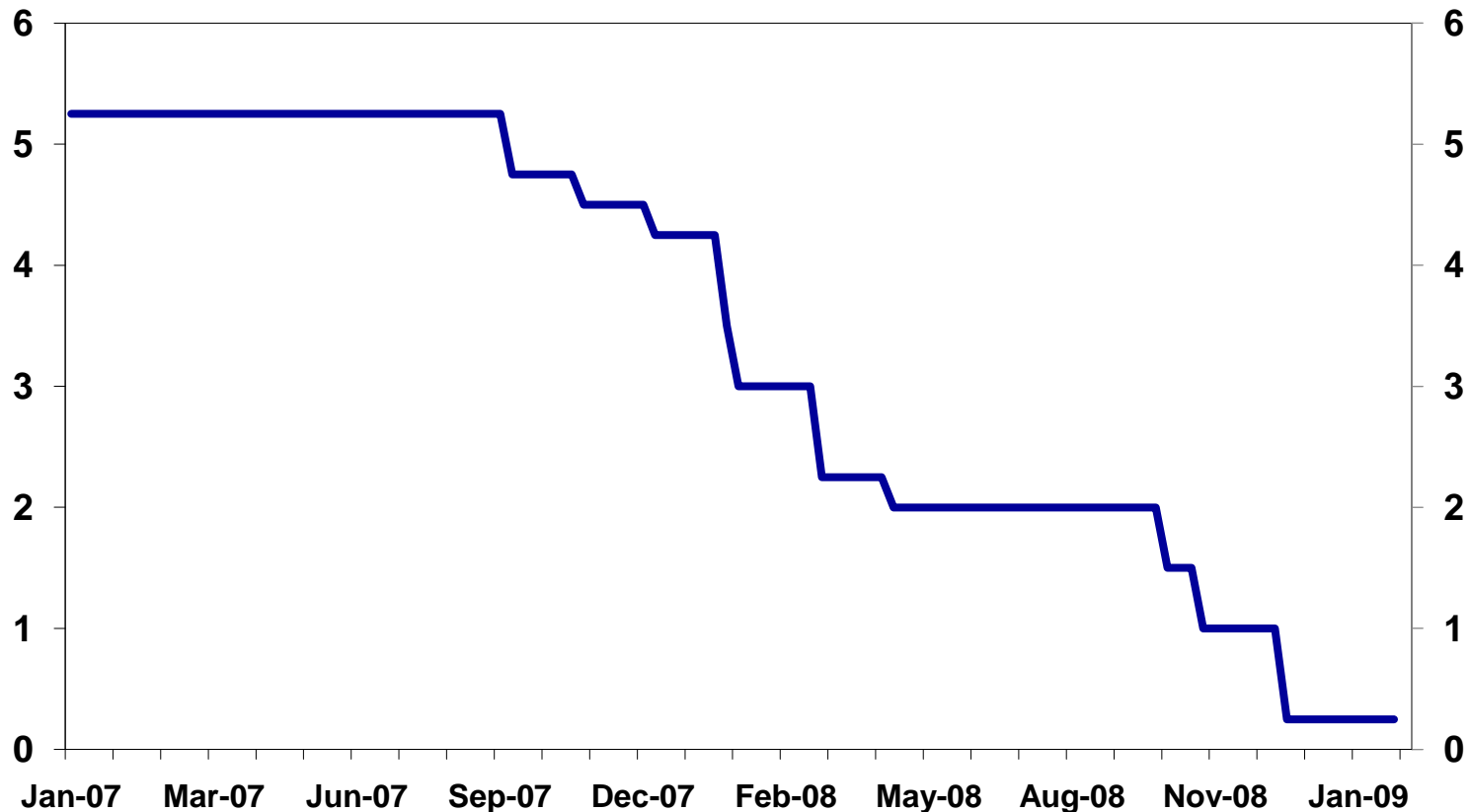
- **Monetary Policy 101**
- **The Financial Crisis Intensifies**
- **The Recession Deepens**
- **What is the Impact on Agriculture?**



What happens to monetary policy at the zero bound?

Fed Funds Rate

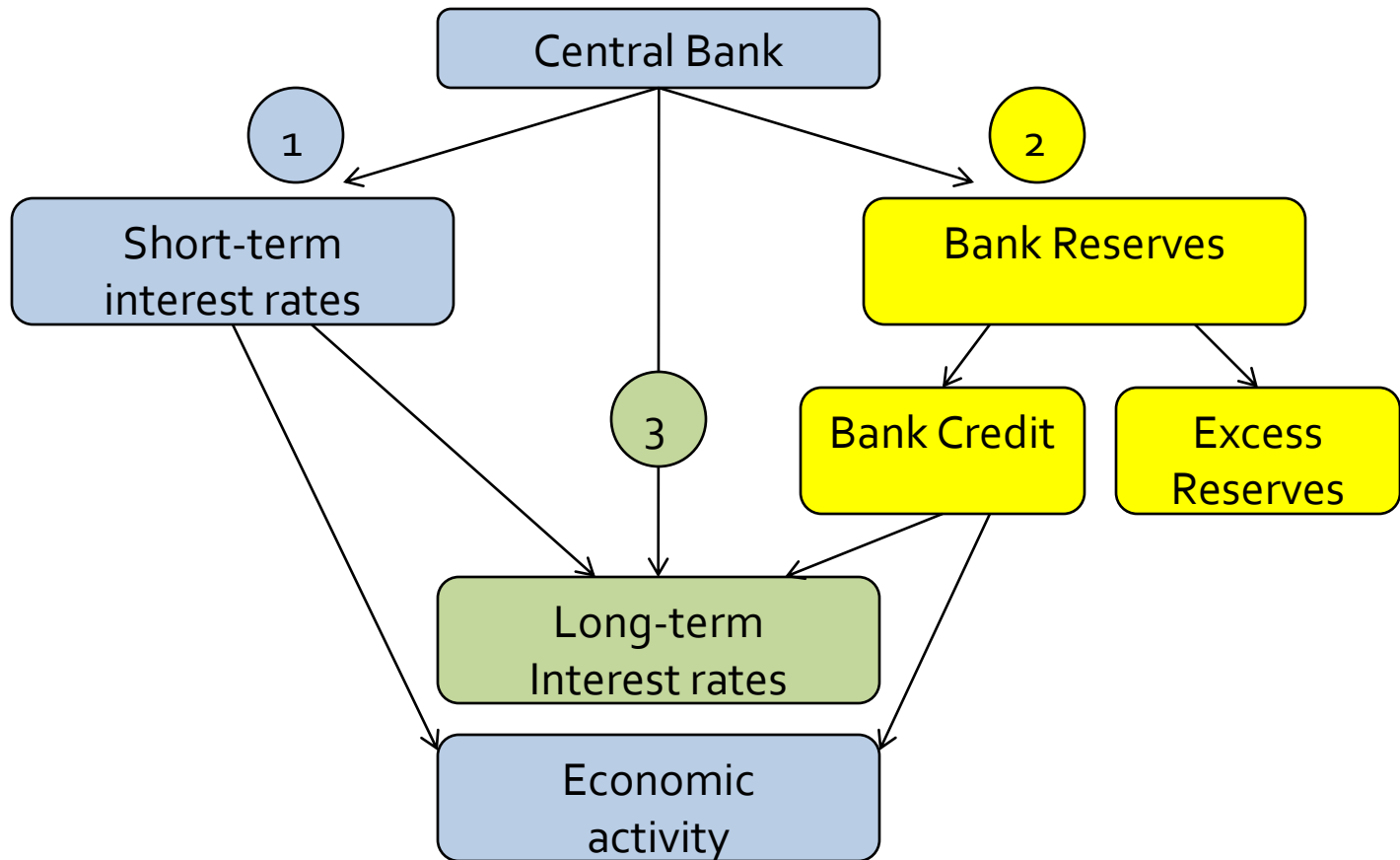
Percent



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**

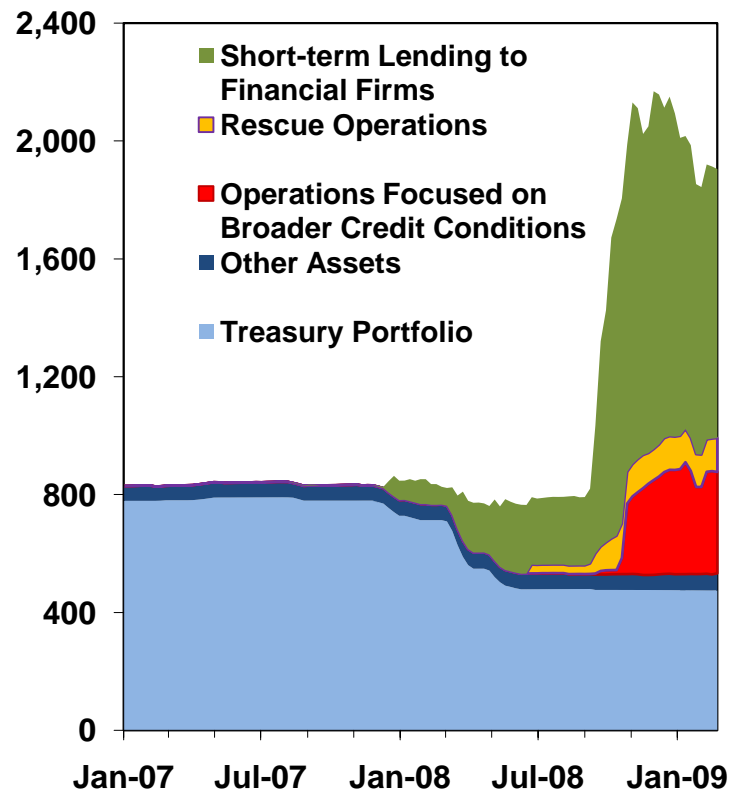
- Offset by lower treasury portfolio - **Blue**

- After September 2008, Fed unable to sterilize liquidity injections through the discount window and various lending facilities.

- The creation of the Term Asset-backed Securities Loan Facility (TALF) to acquire consumer loans could expand the balance sheet even further.

Federal Reserve Balance Sheet

Billions of Dollars



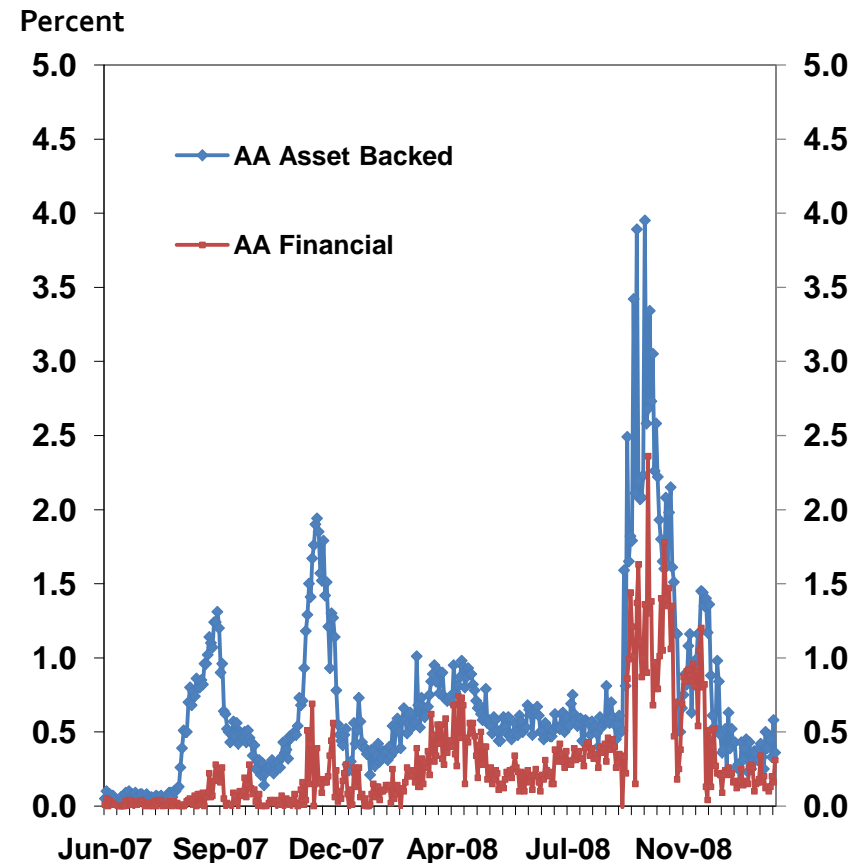
Source: Federal Reserve Board of Governors



Stress in the mortgage market spread to financial markets in the fall of 2008.

- 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



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

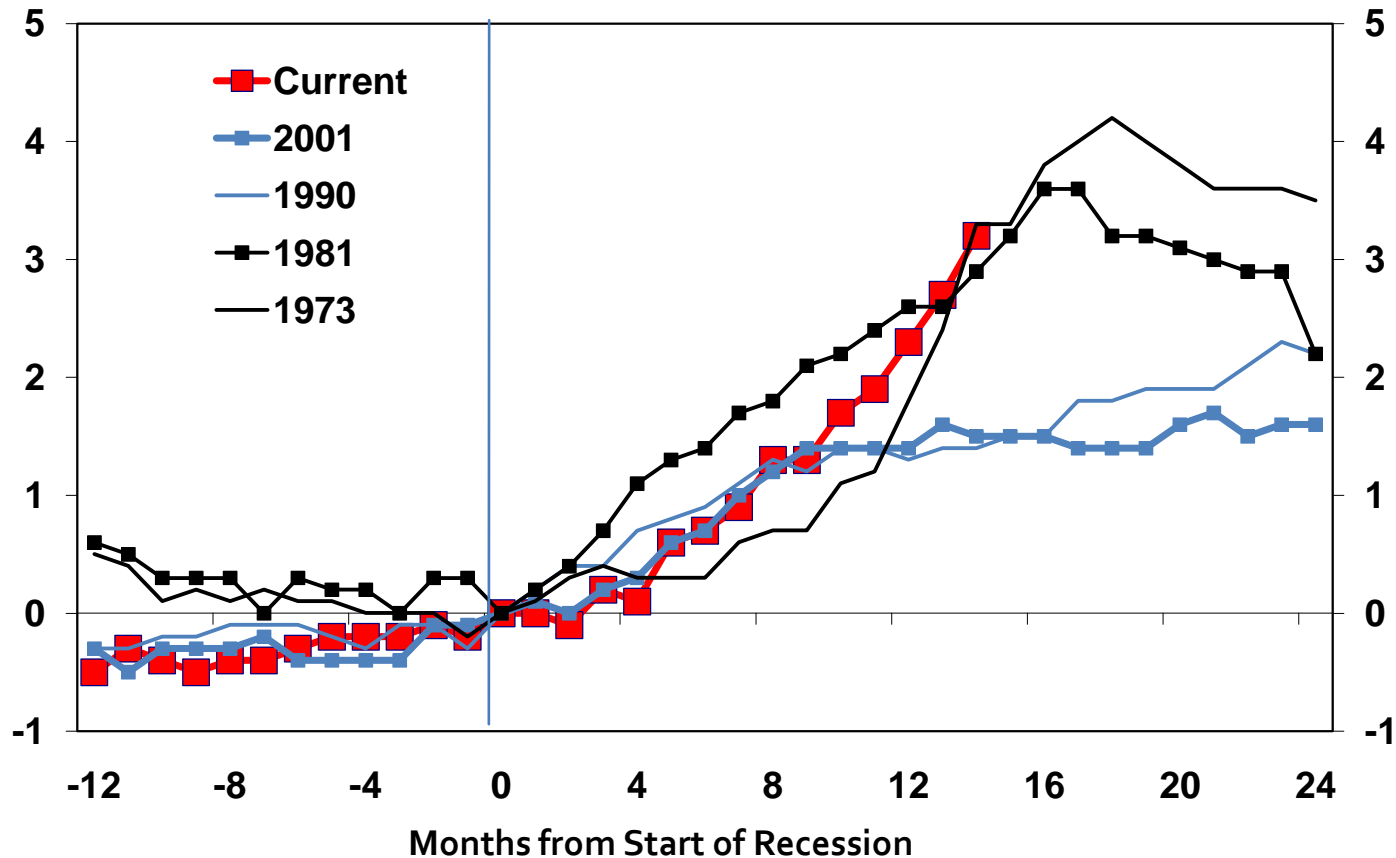
Source: NBER



Job loss are tracking the 1981 and 1973 recessions.

Unemployment Rate Around Business Cycle Peak

Change in unemployment rate



Federal Reserve Economic Projections

(January 28, 2009)

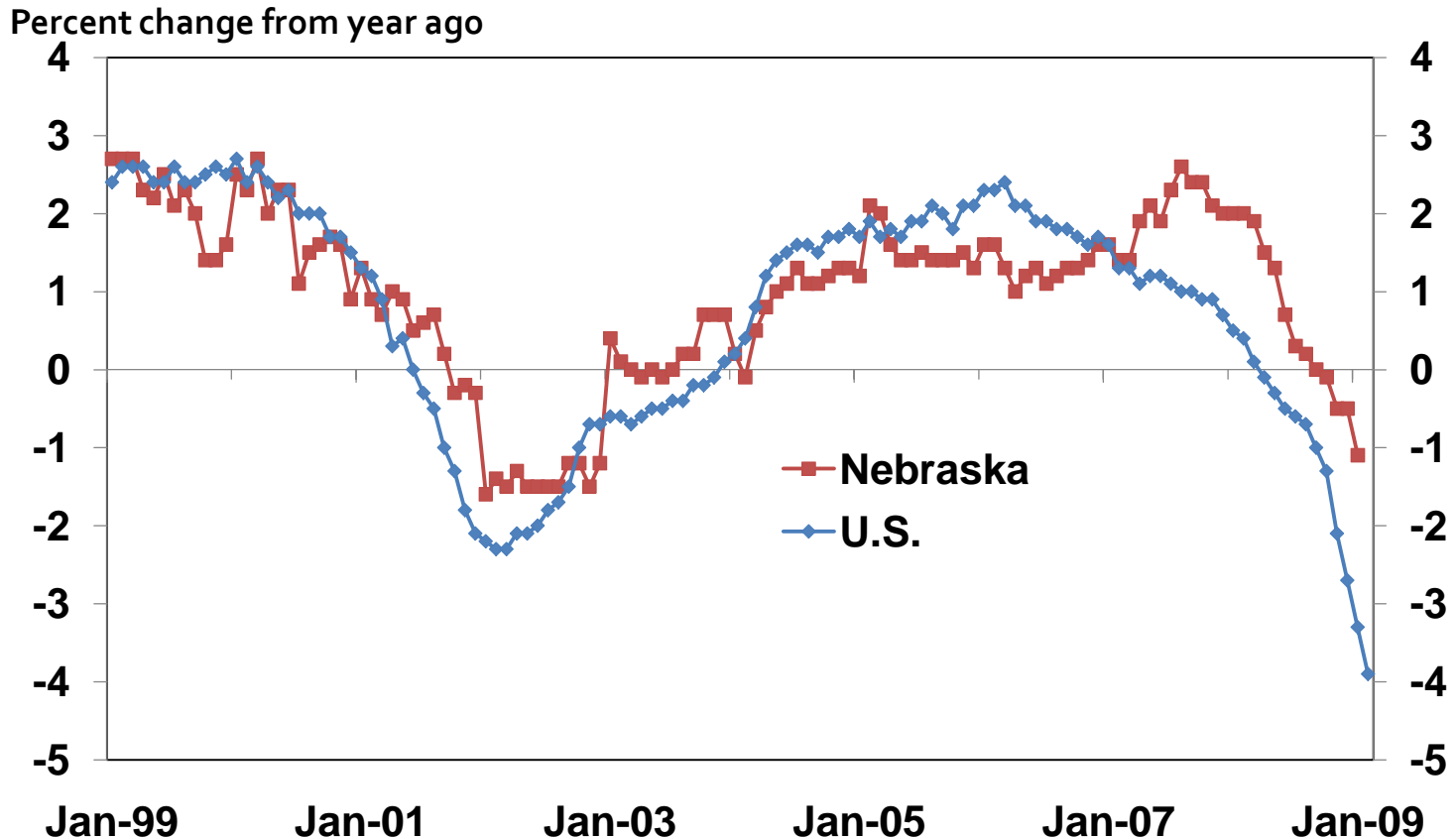
	2009	2010	2011	Longer Run
Real GDP Growth	-1.3 to -0.5	2.5 to 3.3	3.8 to 5.0	2.5 to 2.7
October '08 projection	-.2 to 1.1	2.3 to 3.2	2.8 to 3.6	
Unemployment Rate	8.5 to 8.8	8.0 to 8.3	6.7 to 7.5	4.8 to 5.0
October '08 projection	7.1 to 7.6	6.5 to 7.3	5.5 to 6.6	
PCE Inflation	0.3 to 1.0	1.0 to 1.5	0.9 to 1.7	1.7 to 2.0
October '08 projection	1.3 to 2.0	1.4 to 1.8	1.4 to 1.7	

Source: Summary of Economic Projections, Minutes of the Federal Open Market Committee, January 27-28, 2009.
Available at www.federalreserve.gov



Nebraska's economy is performing better than the rest of the nation.

U.S. and Nebraska Private Employment Growth



Source: Bureau of Labor Statistics



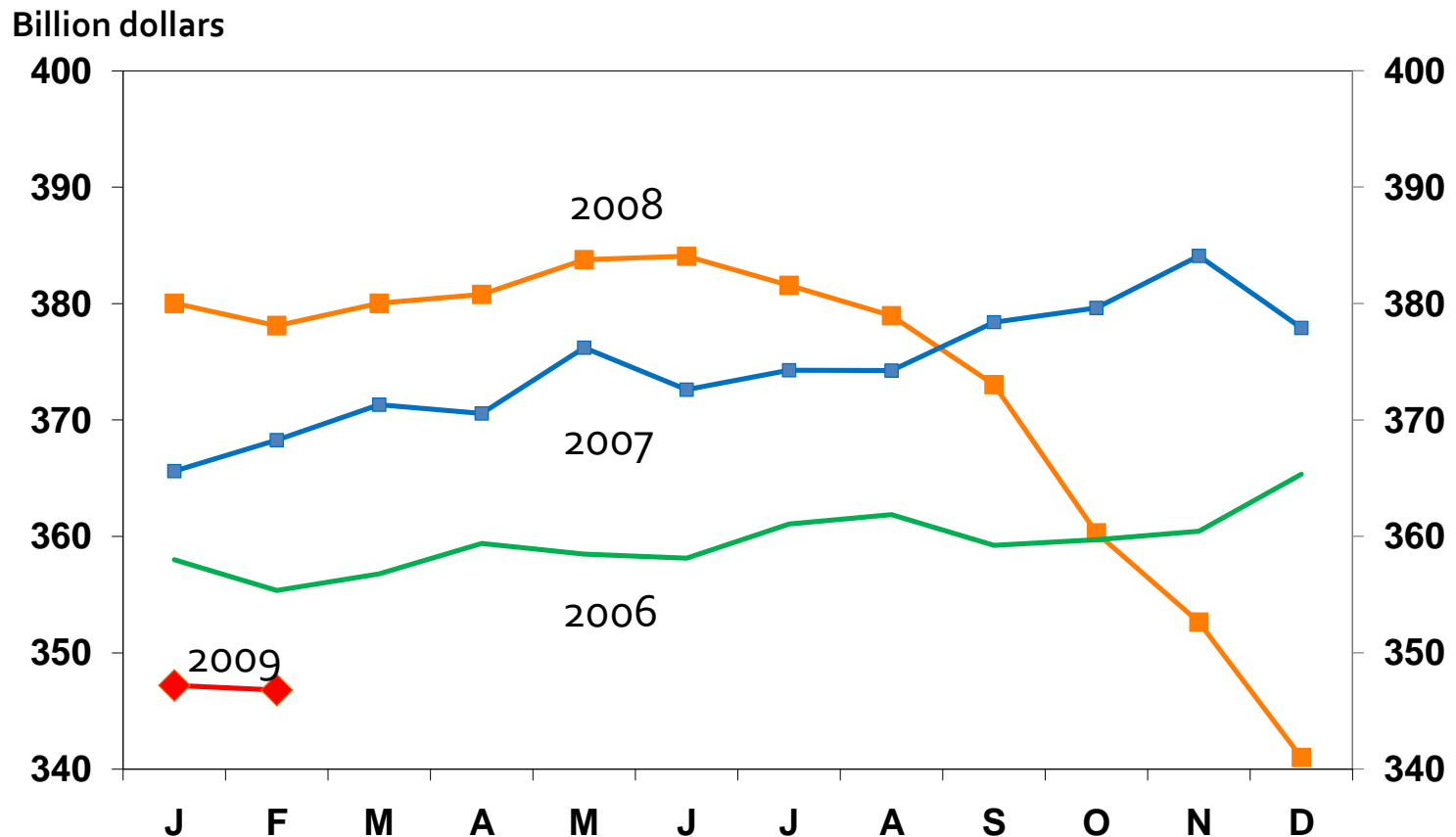
The Recession Intensifies

- Consumer spending drops sharply.



Consumer spending drops sharply.

U.S. Monthly Retail and Food Sales

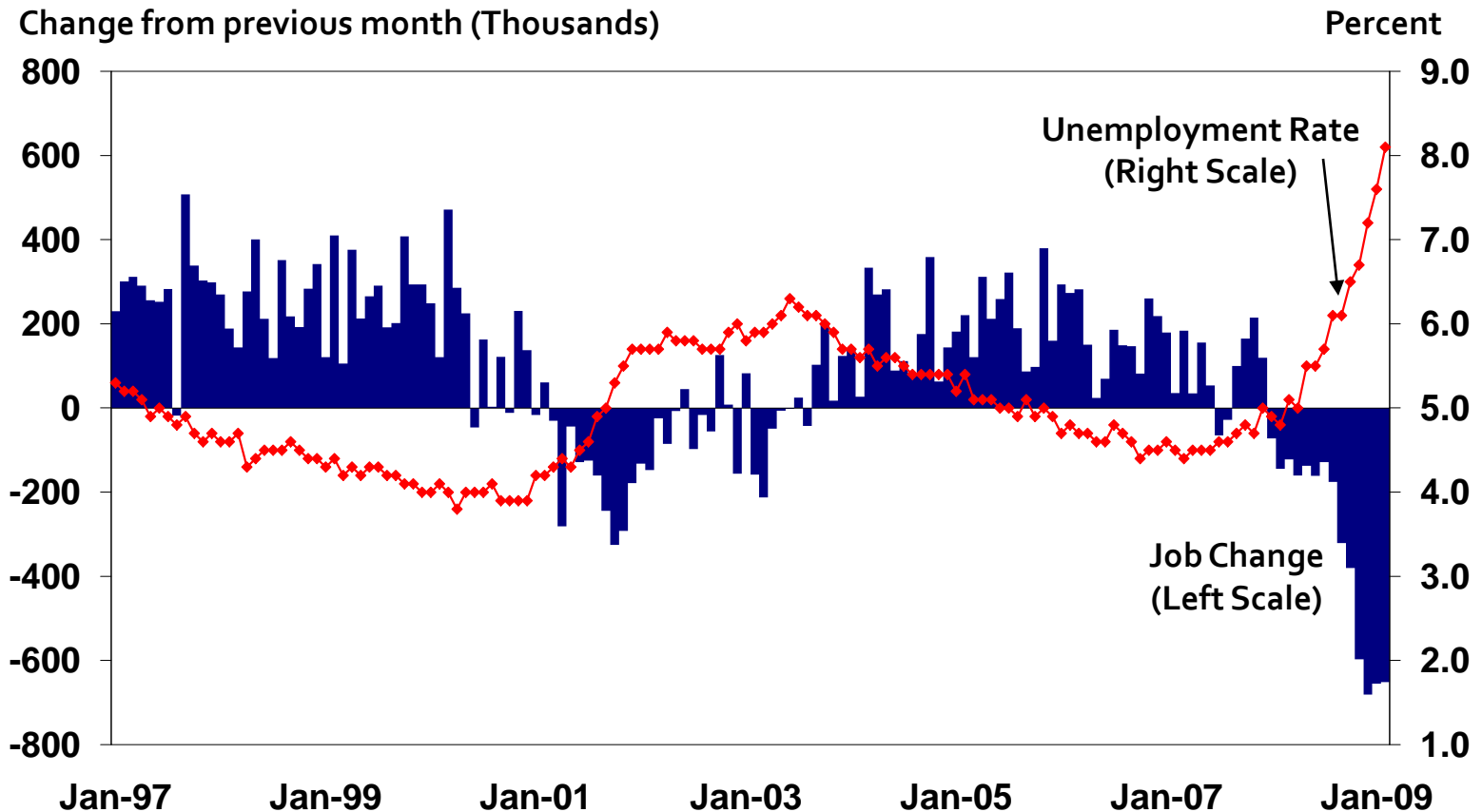


Source: U.S. Census Bureau



Job losses mount.

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



Source: Bureau of Labor Statistics



The Recession Intensifies

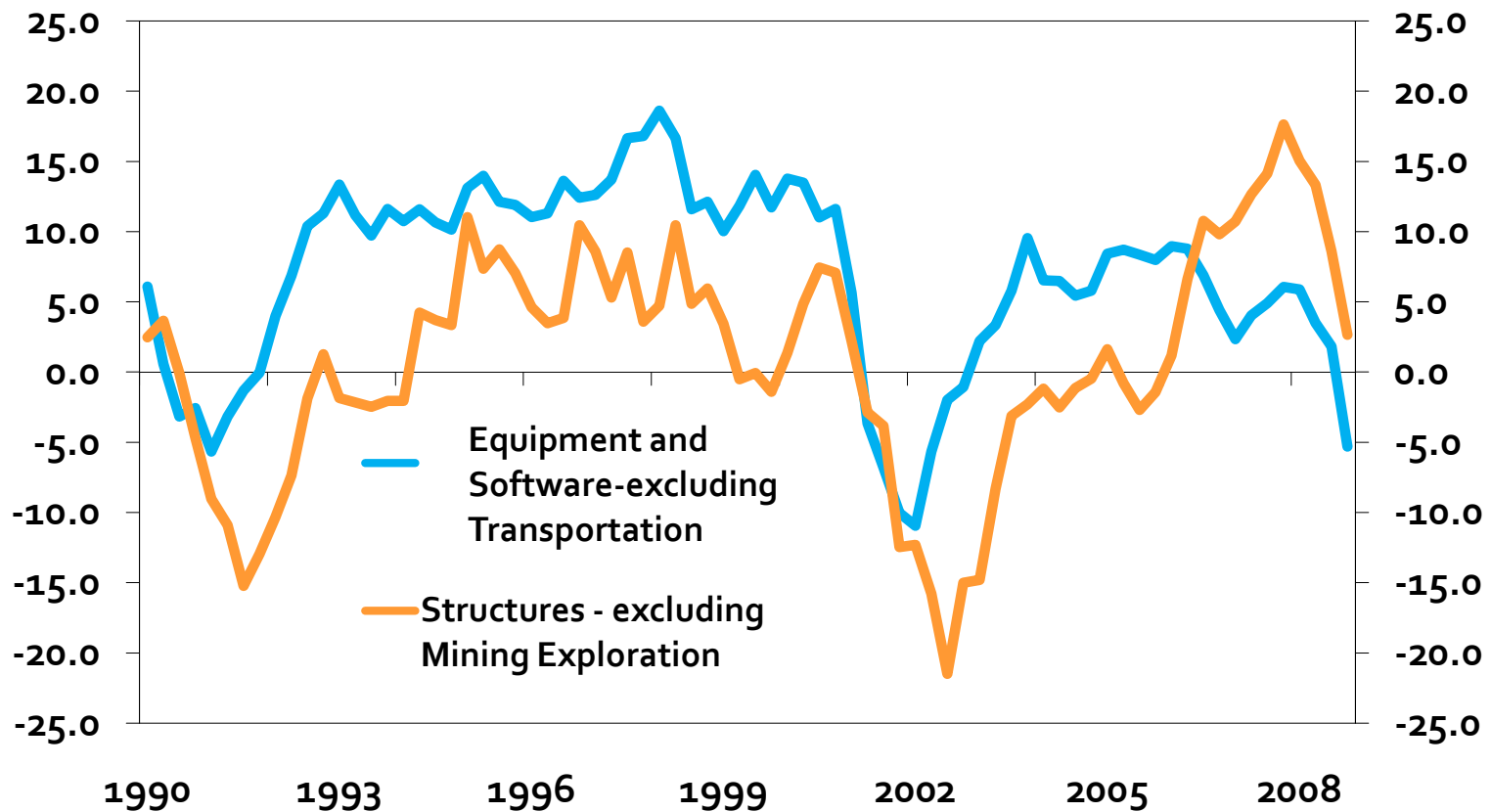
- **Consumer spending drops sharply.**
- **Business activity plummets.**



Business investment has plummeted.

U.S. Non-residential Investment

Percent change from year ago



Source: Census Bureau



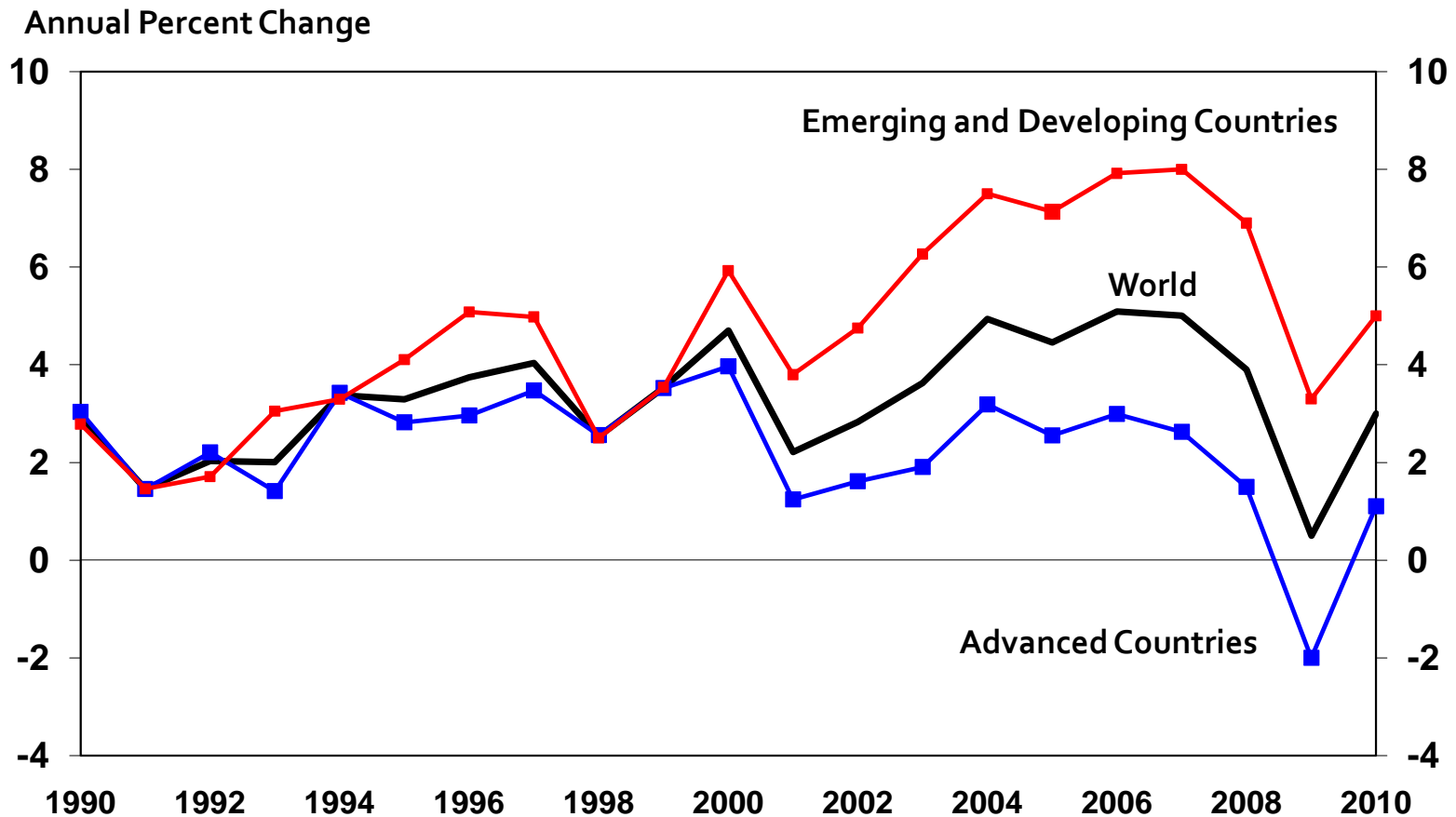
The Recession Intensifies

- **Consumer spending drops sharply.**
- **Business activity plummets.**
- **Export activity wanes with a global recession and a stronger dollar.**



The recession has spread globally.

World GDP Growth

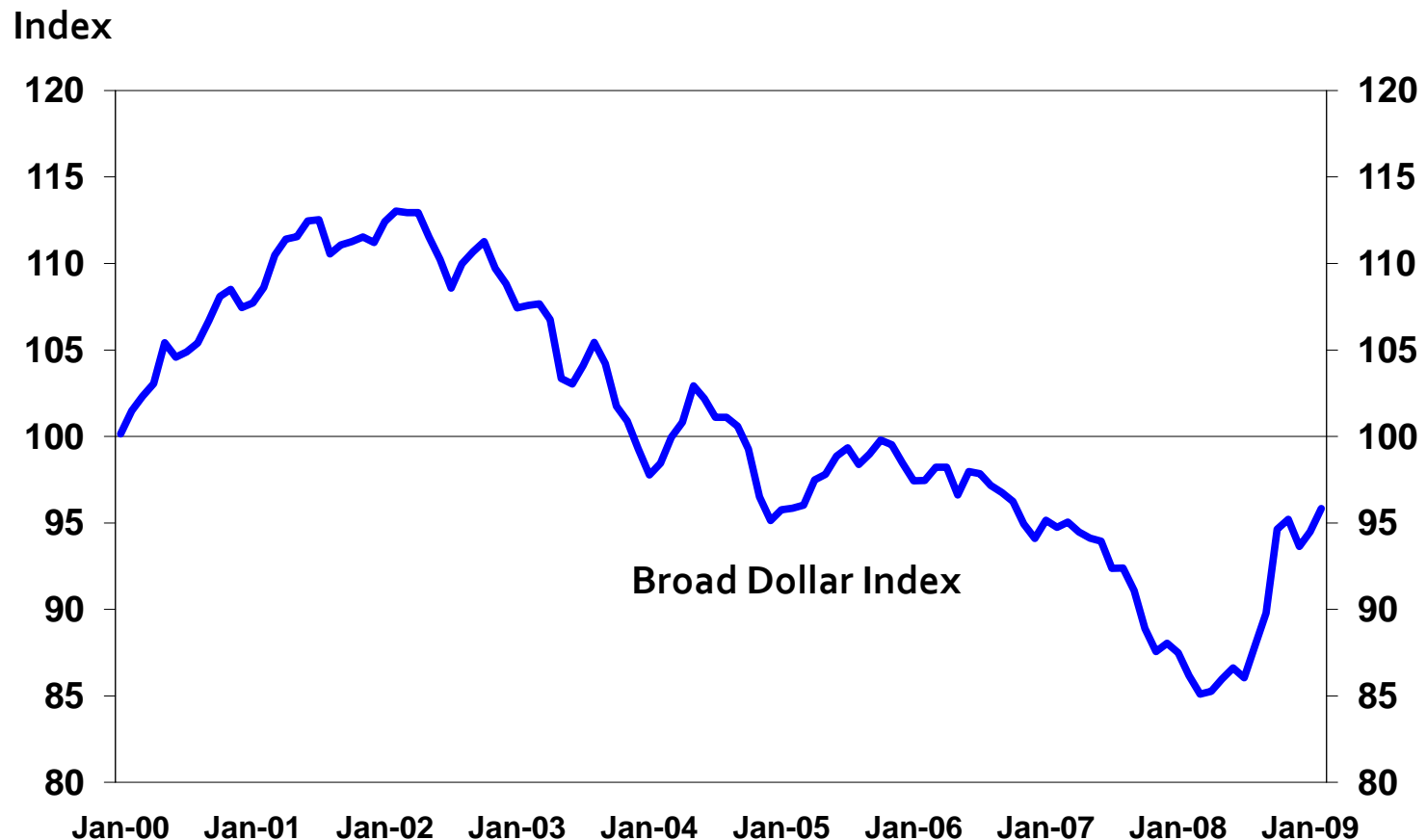


Source: International Monetary Fund, January 2009



The value of the dollar has strengthened as the world searches for safe investments.

Value of the Dollar

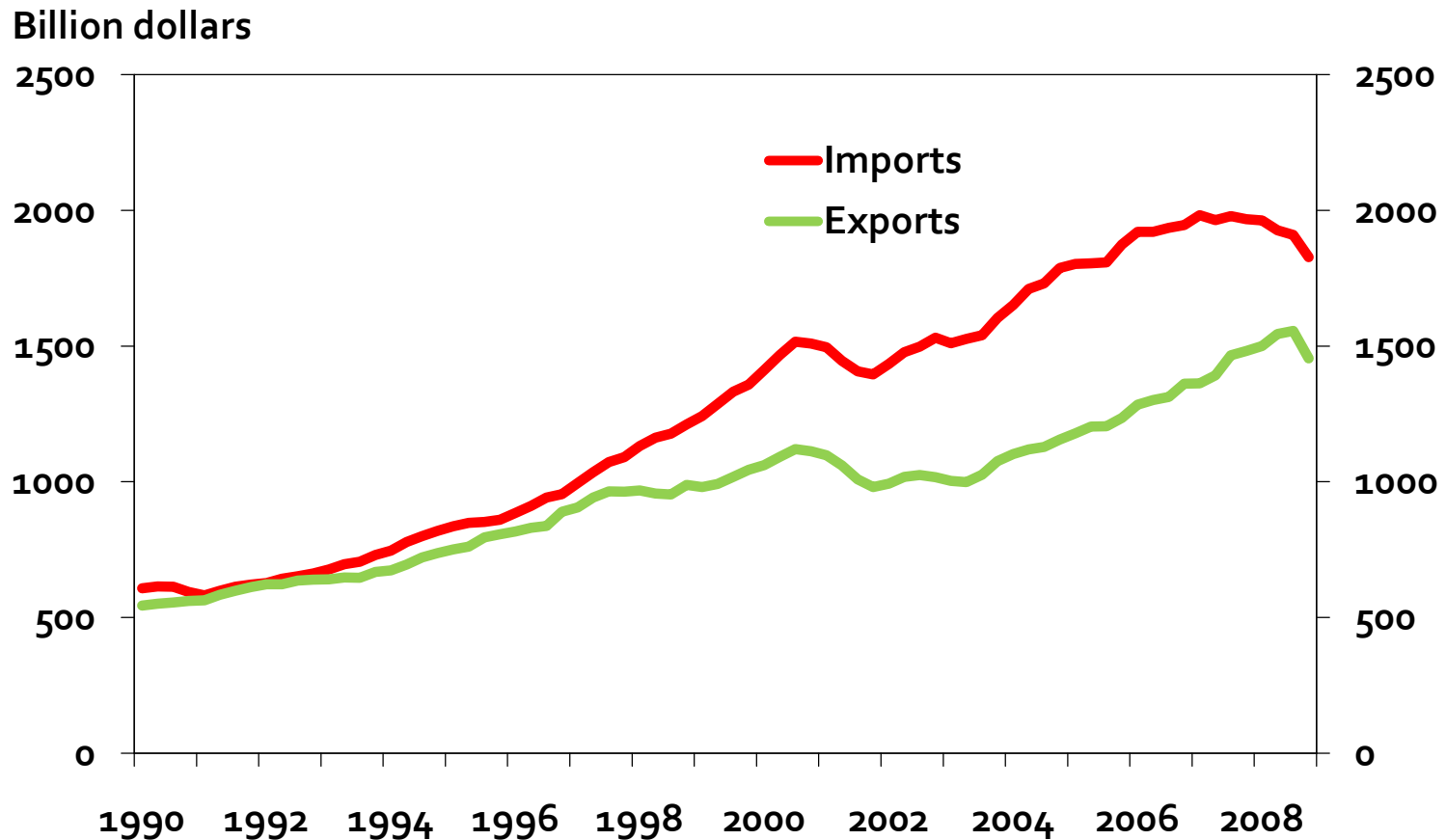


Source: Federal Reserve Board of Governors



Export activity has slowed.

U.S. Exports and Imports



Source: Bureau of Economic Analysis and Blue Chip Forecast, February 2009



The Recession Intensifies

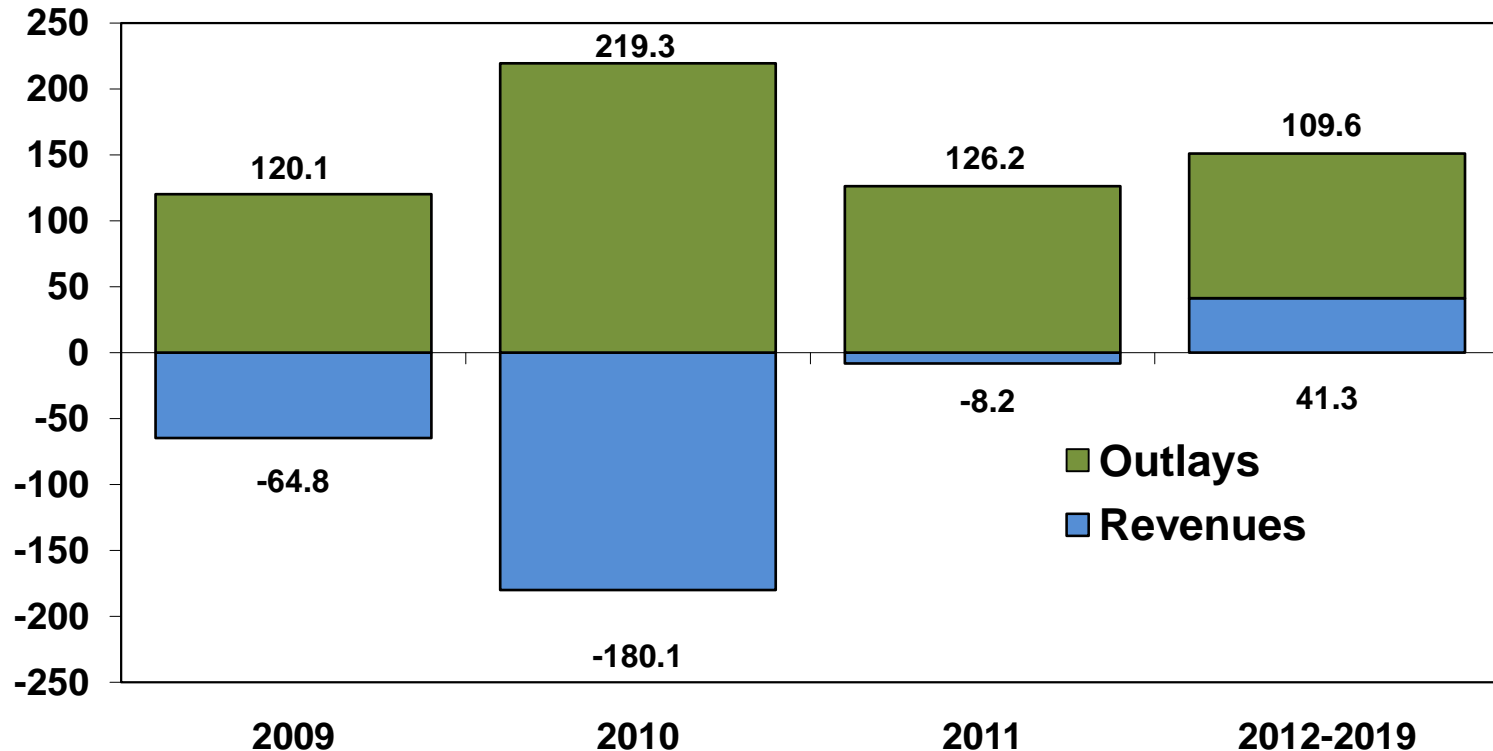
- **Consumer spending drops sharply.**
- **Business activity plummets.**
- **The recession spreads globally.**
- **Will fiscal stimulus jump start the economy?**



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



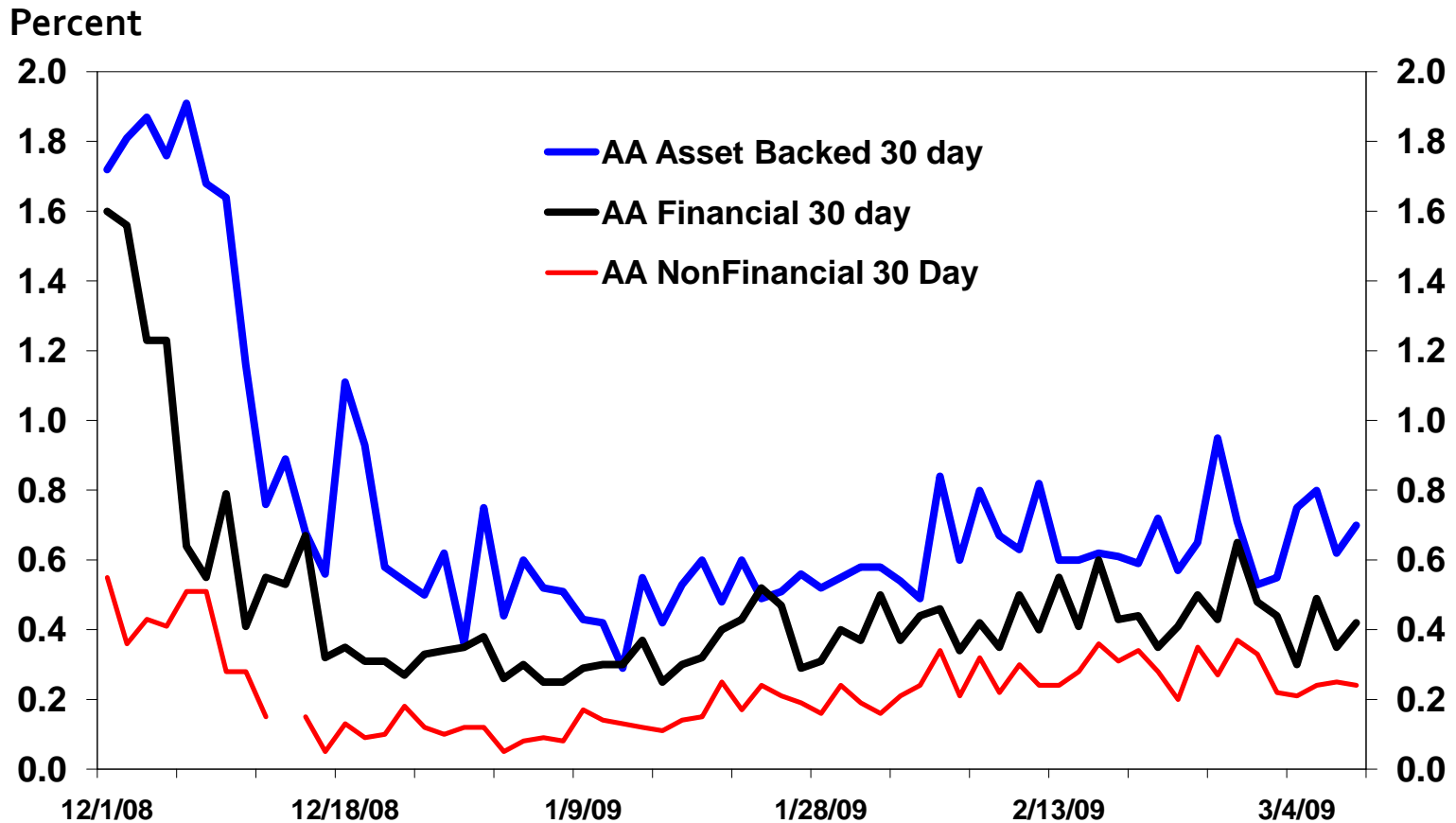
Today's Roadmap

- **The Recession Intensifies**
- **Will Recent Financial Market Improvements Persist?**



Commercial paper rates have crept up.

Commercial Paper Rates



Source: Federal Reserve Board of Governors



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Falling Demand for Farm Products.

- **Rising at-home consumption of food.¹**
 - Grocery store sales rose 0.4 % annually by December 2008
 - Restaurant sales slid 1.7 % annually by December 2008
- **Shift in meat demand to lower-priced poultry²**
 - Beef demand fell 4% in 2008.
 - Pork demand fell 5.6% in 2008.
 - Poultry demand rose 0.7% in 2008.
- **Agricultural exports forecasted to fall 17.3 % in 2009.³**
- **Projections for 2008/09 ethanol corn use fell 2.7% in January.⁴**

¹ U.S. Census, *Advanced Monthly Retail Sales*

² Kansas State University and University of Missouri

³ USDA, *Outlook for Agricultural Trade*

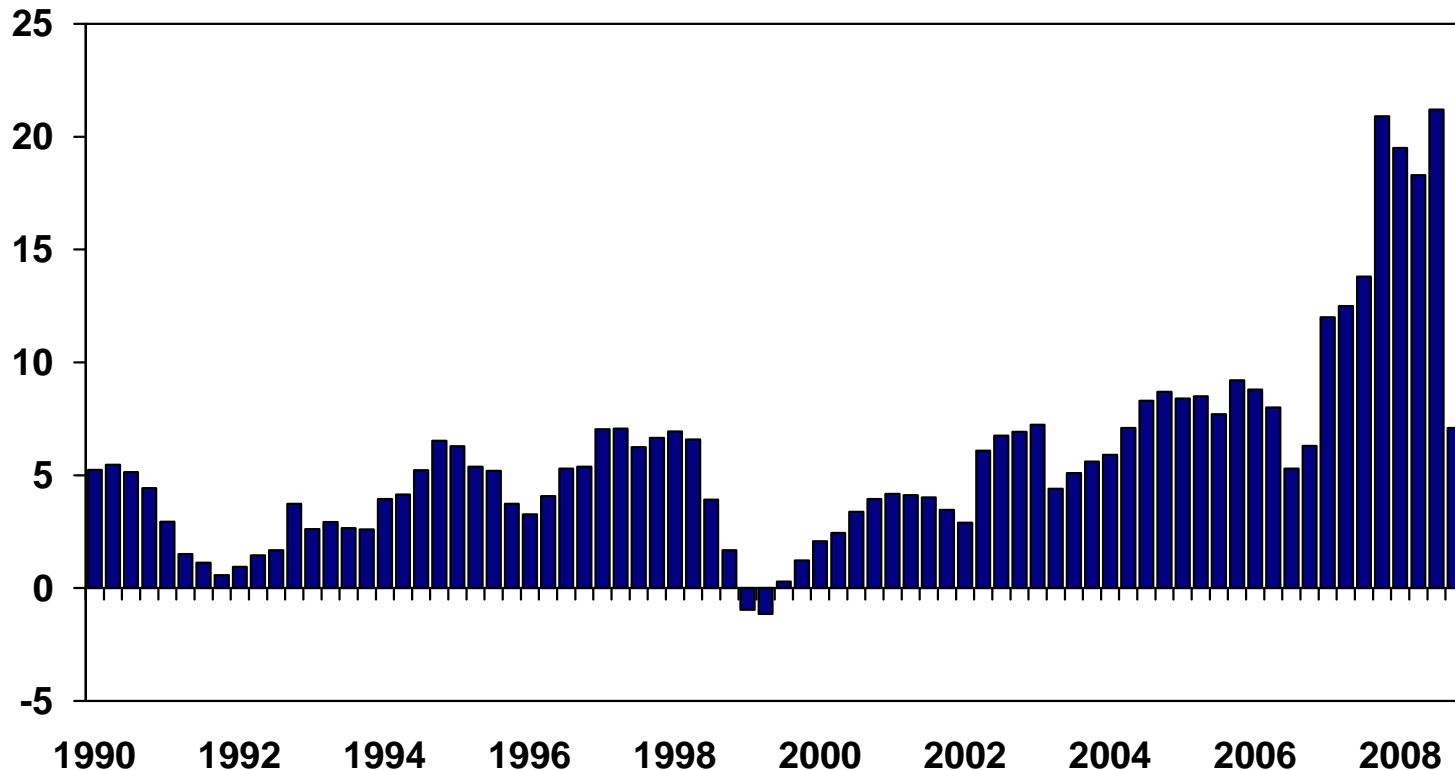
⁴ USDA, *World Agricultural Supply and Demand Estimates*



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.



Conclusions

- **The Longest and Deepest Recession Since World War II.**
 - A housing bust has spread to financial markets.
 - A financial and economic crisis leads to a deep recession.
 - Economic stabilization at the end of 2009 with modest growth in 2010.
- **The Recession Leeches into the Ag Economy.**
 - Agricultural demand collapses.
 - Farmland values fall amid weaker farm income.
 - Credit conditions tighten with increased risk.
- **When Will Fiscal and Monetary Stimulus Spark a Rebound?**

