

The Economy and Manufacturing in the U.S. and Colorado



Chad Wilkerson

Oklahoma City Branch Executive
Federal Reserve Bank of Kansas City

Purposes and Structure of the Federal Reserve System

- **Overall purposes of the Fed are to promote:**
 - Low and stable inflation
 - Maximum sustainable employment
 - National financial stability (in conjunction with others)
- **The primary functional areas of the Fed are:**
 - Monetary policy – typically the most well-known role to the public
 - Bank regulation – of bank holding companies, state Fed member banks
 - Payments systems – cash; electronic; bank for federal government
- **The Federal Reserve System consists of:**
 - Board of Governors: 7 members who are appointed by the U.S. President and confirmed by the Senate to serve 14-year terms.
 - Federal Reserve Banks: 12 Banks, each serving a unique district.
 - Federal Open Market Committee (FOMC): Consists of 12 voting members and 19 total members; sets national monetary policy

Federal Reserve Districts and Office Locations

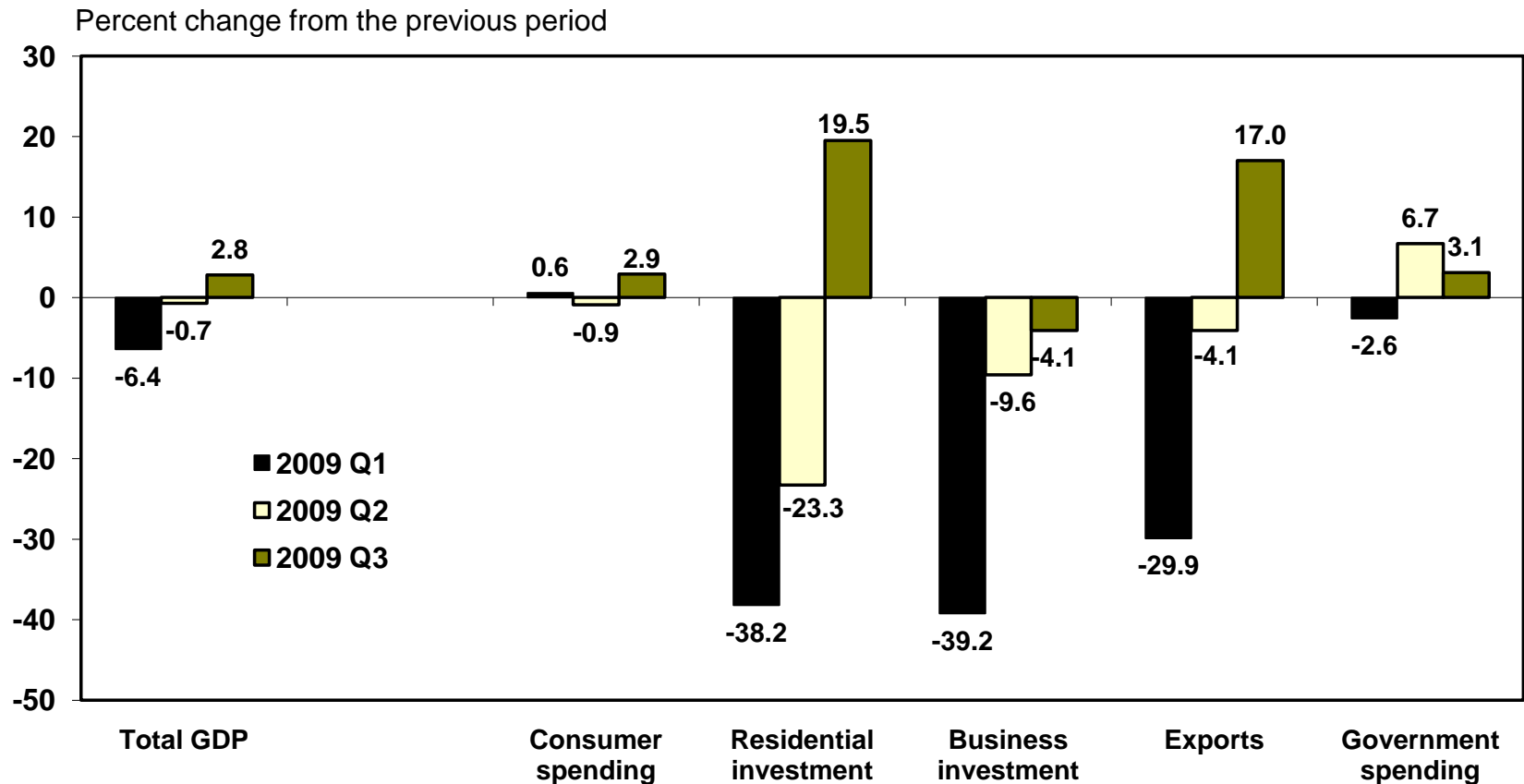


The U.S. Economy

- The U.S. economy is growing again, with help from monetary and fiscal stimulus
- But the strength of recovery is likely to be modest, due to a number of factors
- With modest growth, inflation is expected to remain tame in the near term

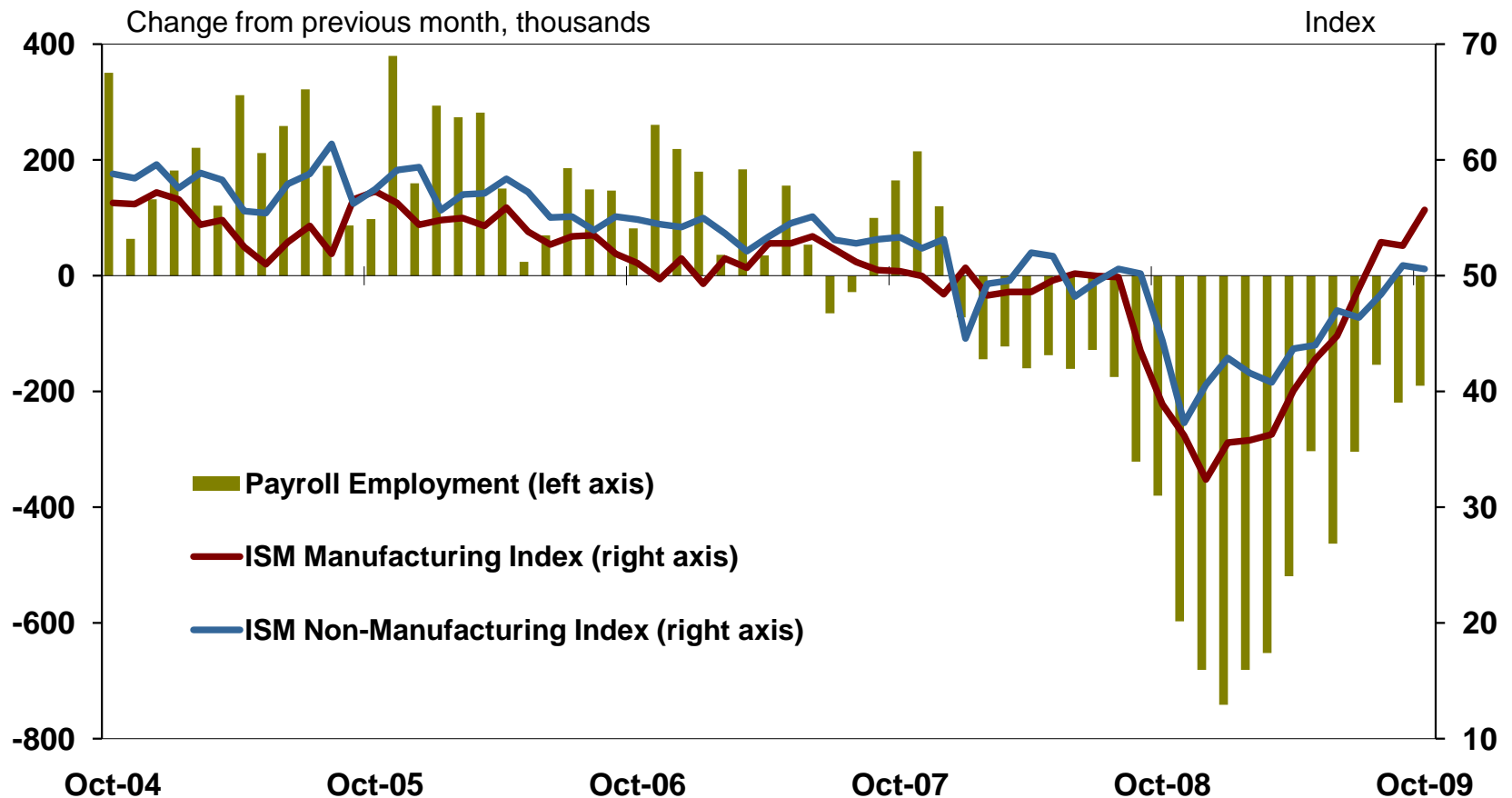
Third quarter GDP growth was quite positive, but was boosted by government stimulus

Growth in Components of GDP



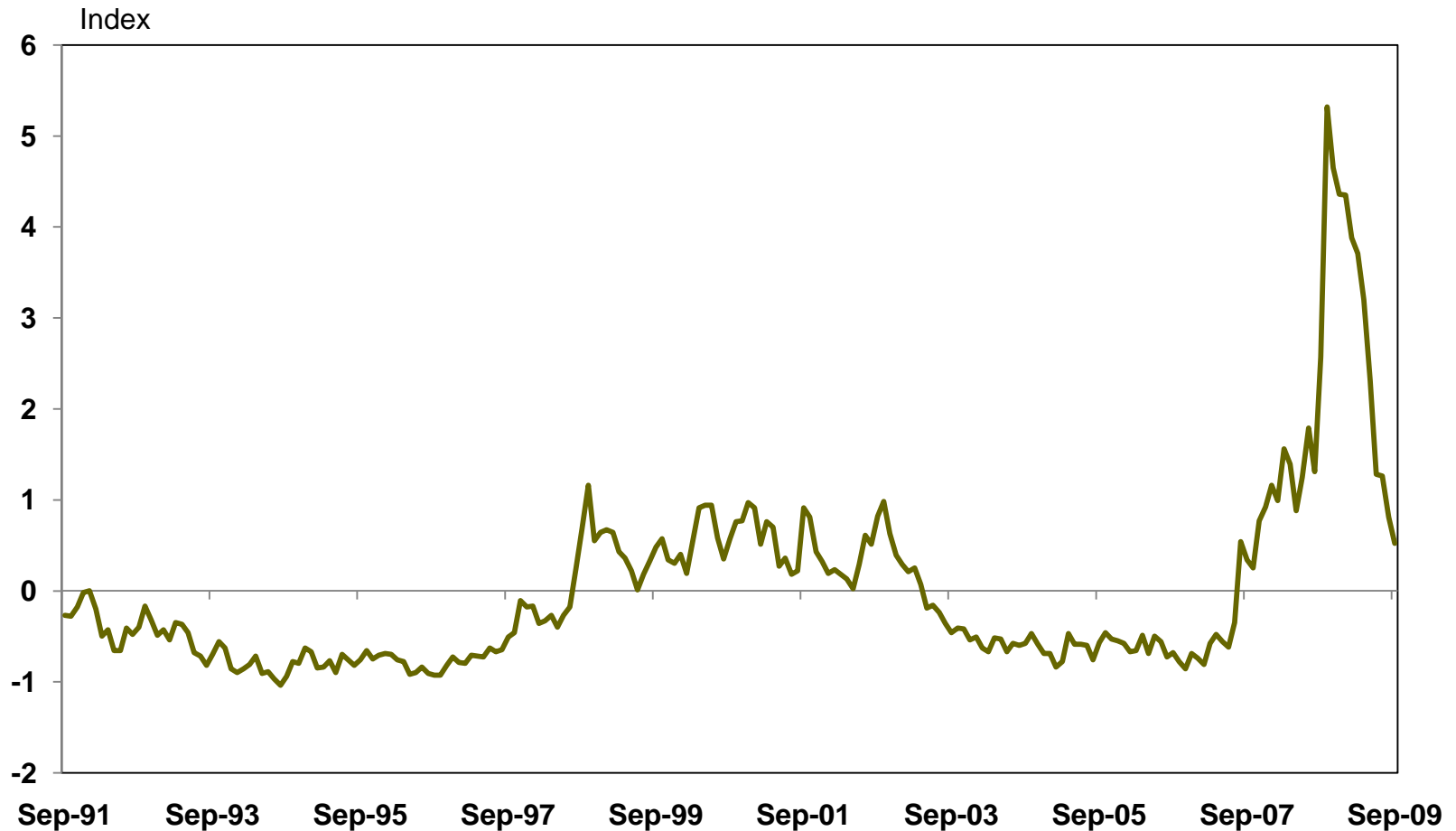
Early reads on the fourth quarter show moderate growth but continued job losses

National Business Indexes and Payroll Employment



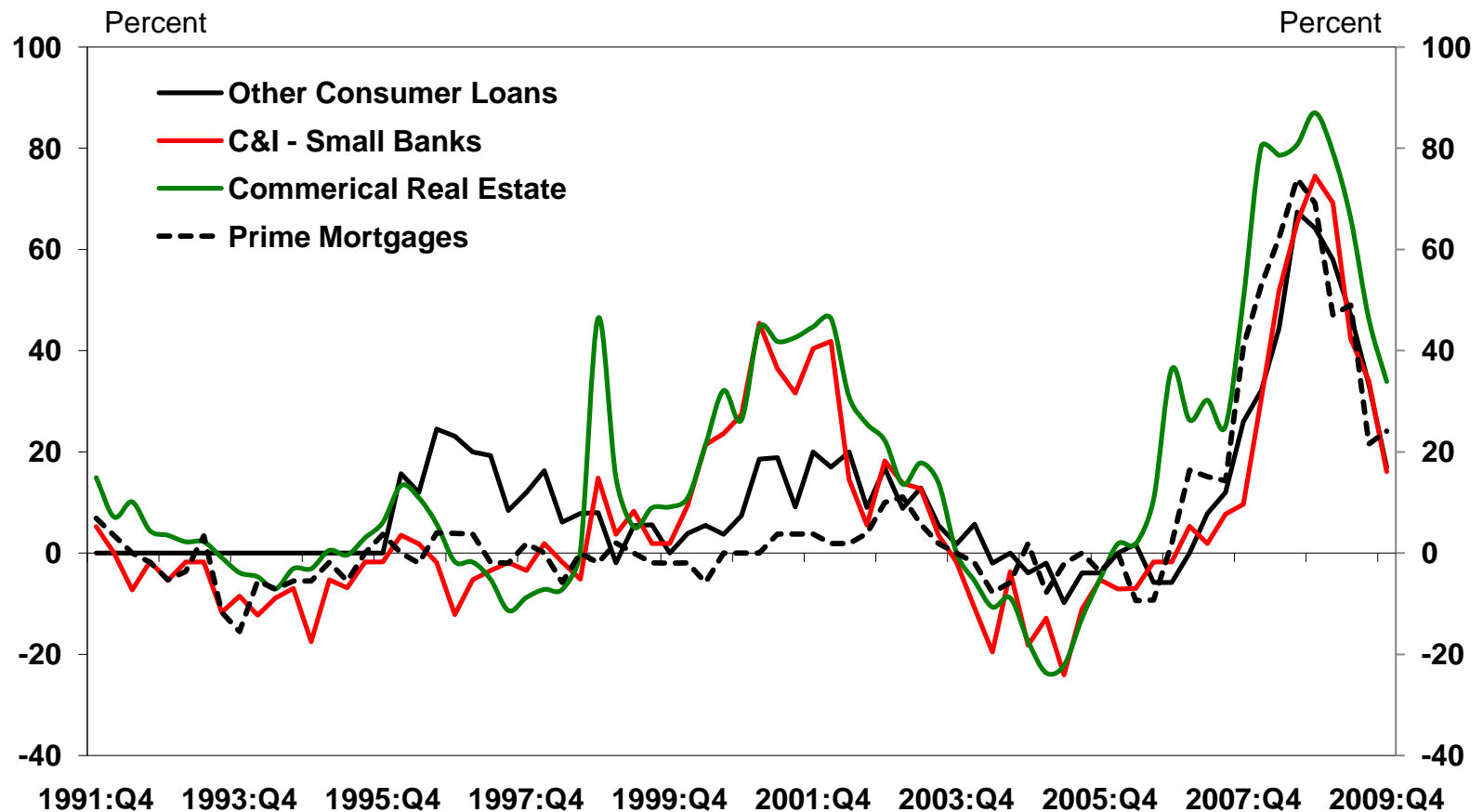
Credit market conditions have improved but remain somewhat stressed

Kansas City Financial Stress Index



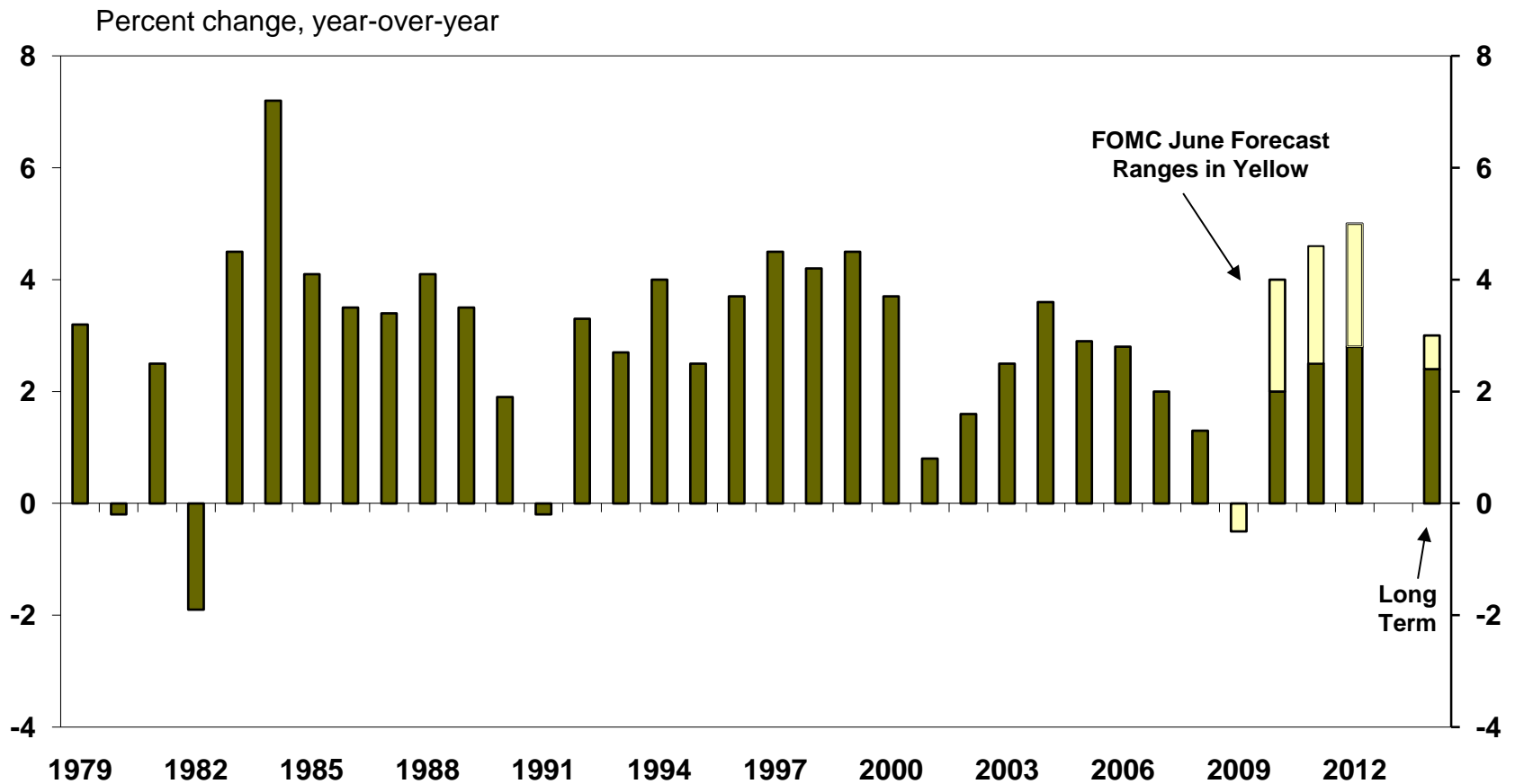
Banks' lending standards continue to tighten, but less than in recent quarters

Net Percentage of Banks Tightening Loan Standards
Business Loans



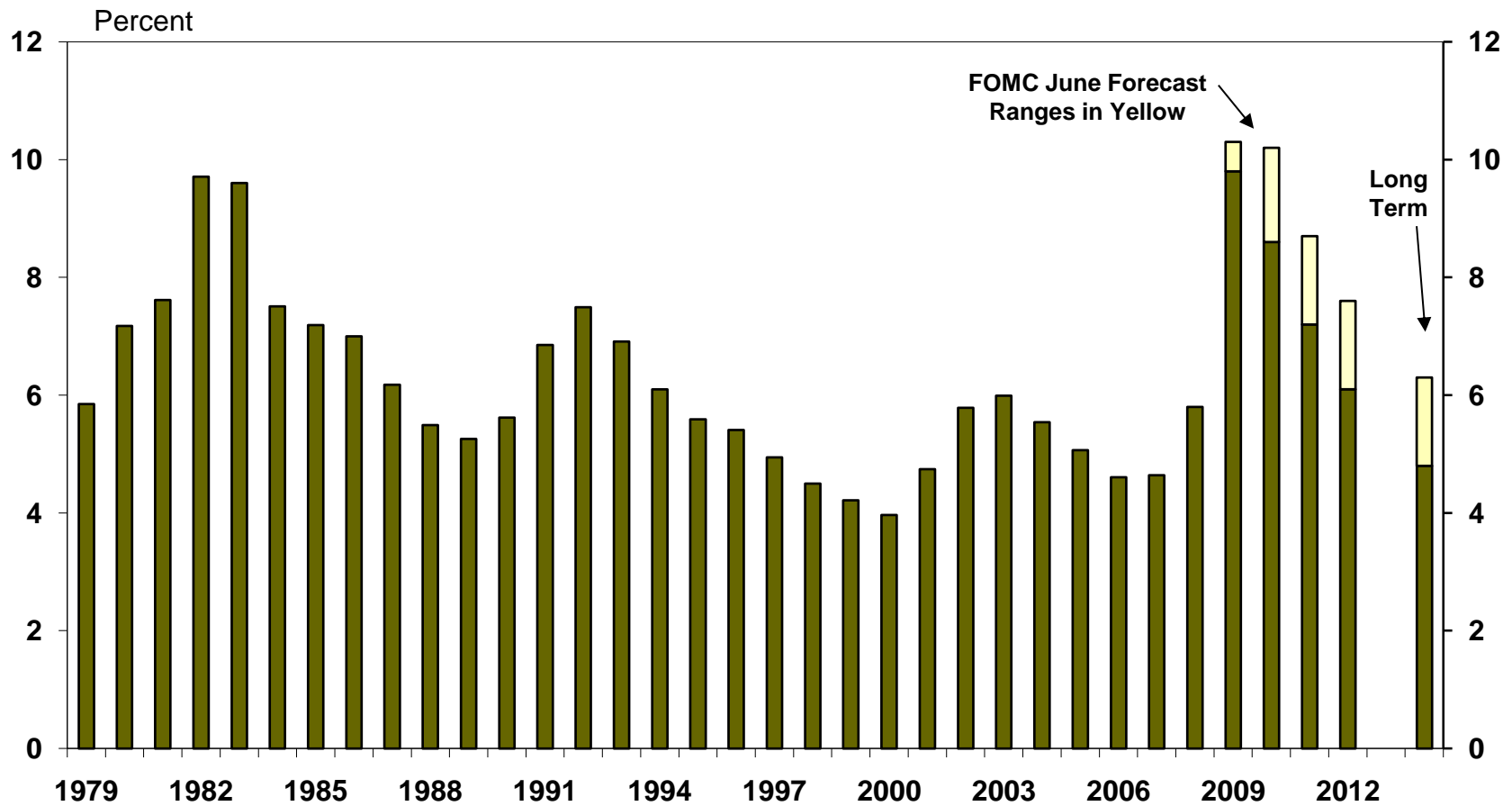
Heading forward, policy makers generally expect a gradual recovery

Gross Domestic Product



But unemployment is expected to remain high for some time

Unemployment Rate
Seasonally Adjusted

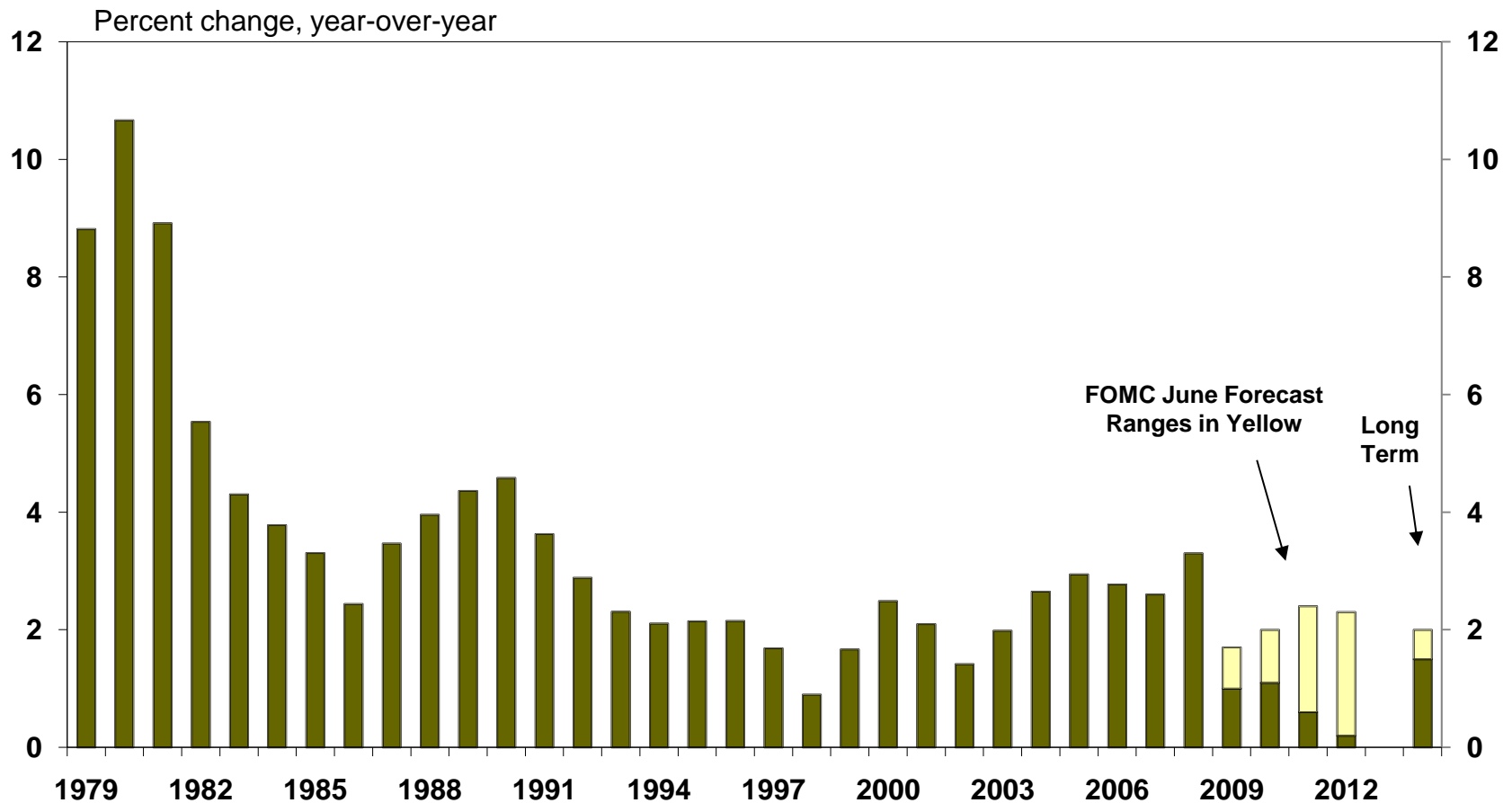


A list of reasons why U.S. recovery speed could be modest

- ❑ Some credit markets remain strained
- ❑ Consumers focus on repairing balance sheets and rebuilding wealth rather than spending
- ❑ Foreclosures and excess inventories continue to weigh on housing
- ❑ Problems in commercial real estate and general uncertainty restrain capital spending and hiring

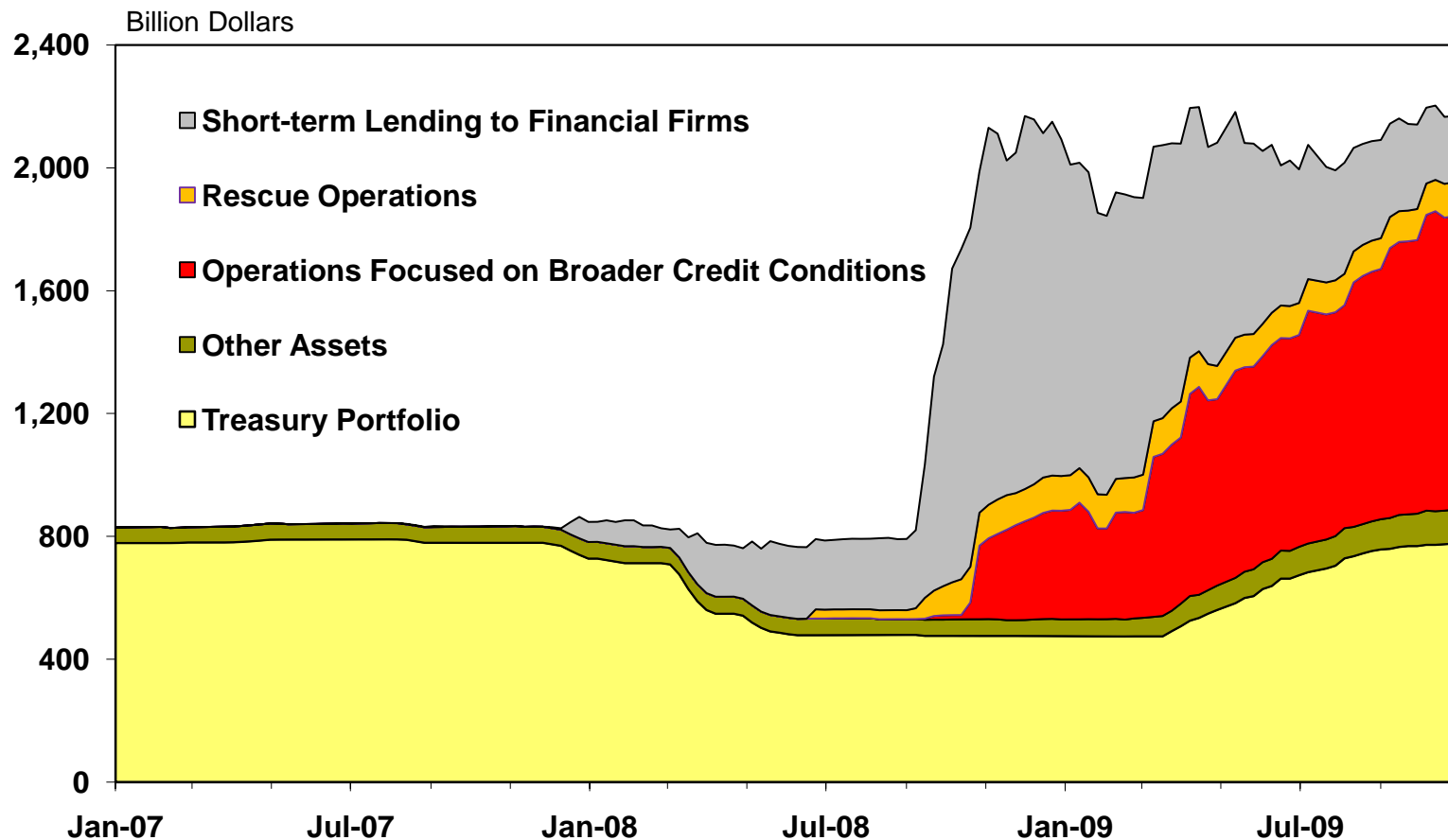
With modest growth, inflation is expected to remain fairly moderate in coming years

PCE Inflation Index



The Fed's balance sheet has grown

Federal Reserve Balance Sheet: Assets



November 4 FOMC statement

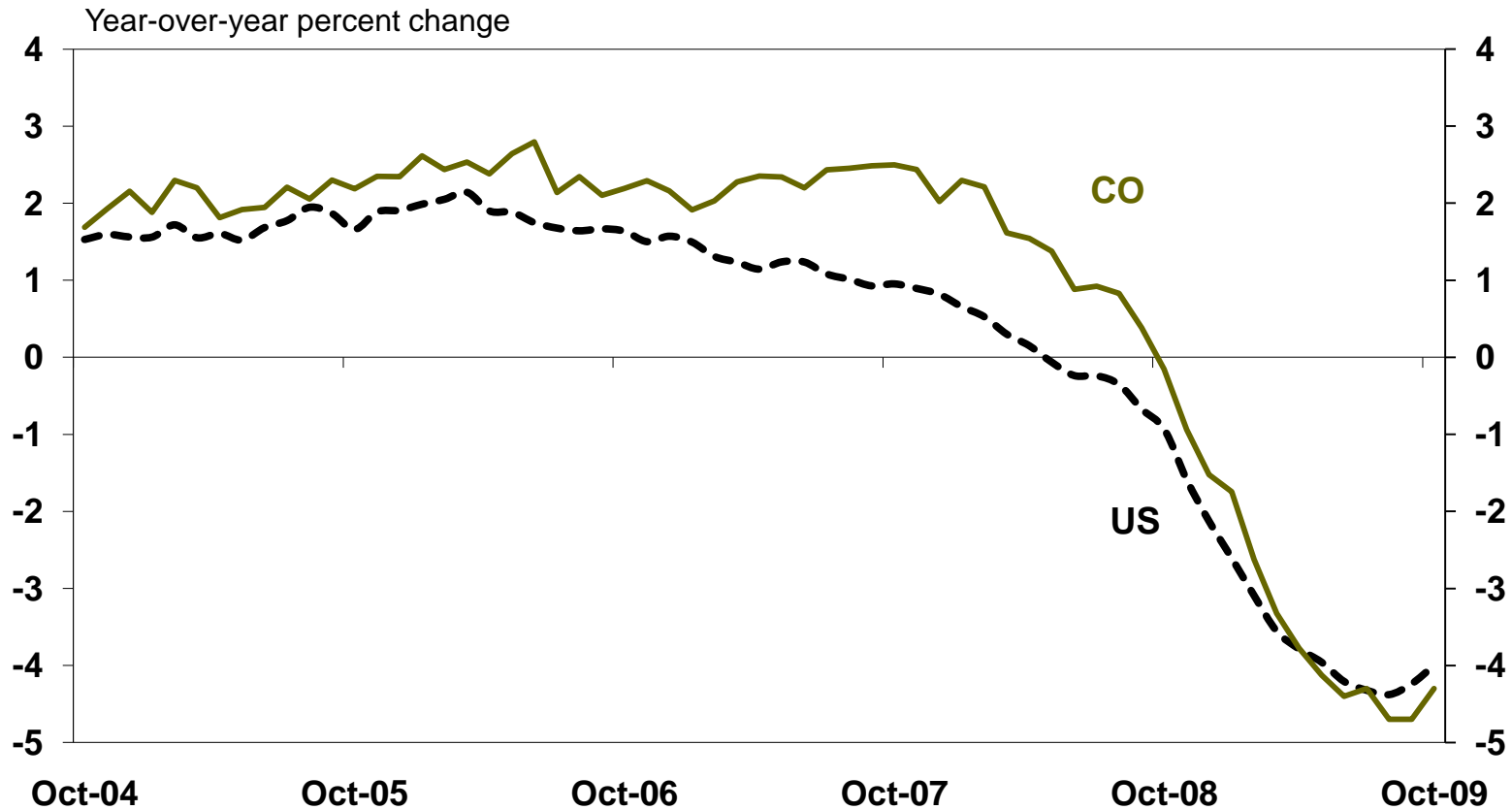
- **In these circumstances, the Federal Reserve will continue to employ a wide range of tools to promote economic recovery and to preserve price stability. The Committee will maintain the target range for the federal funds rate at 0 to 1/4 percent and continues to anticipate that economic conditions, including low rates of resource utilization, subdued inflation trends, and stable inflation expectations, are likely to warrant exceptionally low levels of the federal funds rate for an extended period....**
- **In order to promote a smooth transition in markets, the Committee will gradually slow the pace of its purchases of both agency debt and agency mortgage-backed securities and anticipates that these transactions will be executed by the end of the first quarter of 2010. The Federal Reserve is monitoring the size and composition of its balance sheet and will make adjustments to its credit and liquidity programs as warranted.**

The Colorado Economy

- The state has seen a sharp drop in jobs and declining home values in 2009
- However, both labor market and housing conditions remain better than the nation
- Historically, the state tends to rebound from recessions before or at the same time as the nation

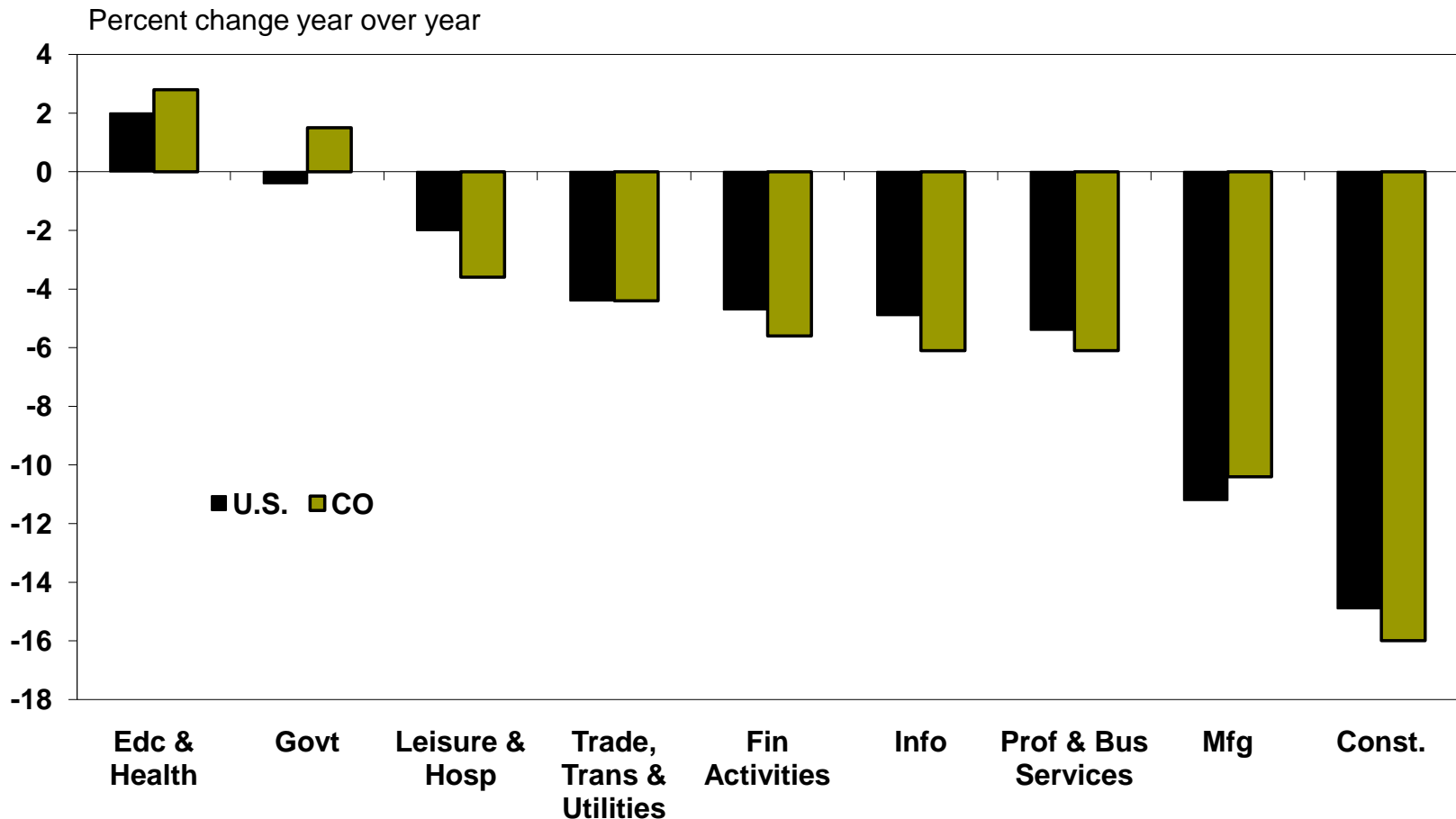
Colorado employment has fallen sharply in 2009, but may have bottomed with the nation

Nonfarm Payroll Employment Growth



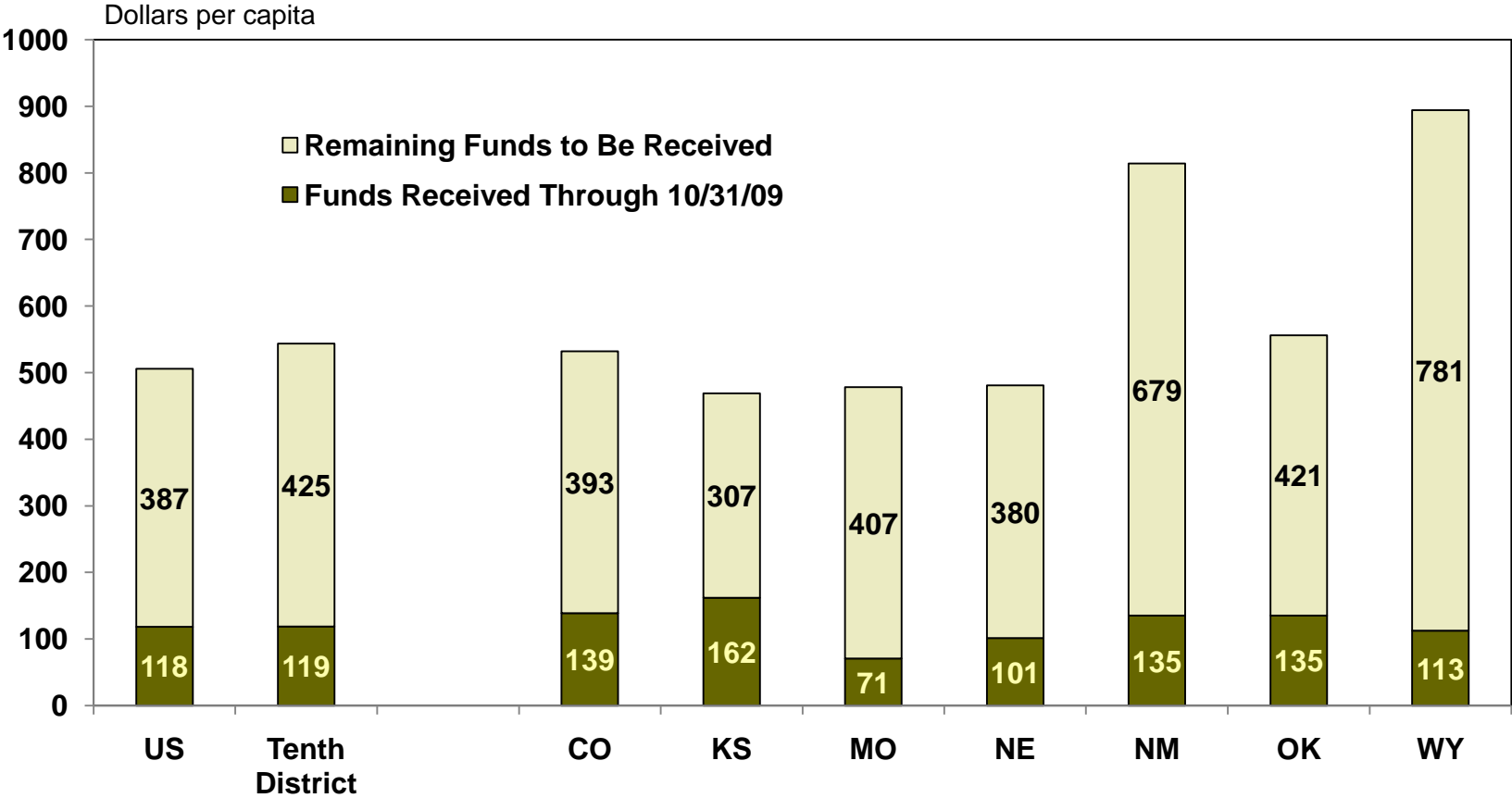
Employment is down from a year ago in almost all Colorado industries

Employment Growth by Industry, October 2009



And our region and state are receiving slightly more fiscal stimulus than the nation

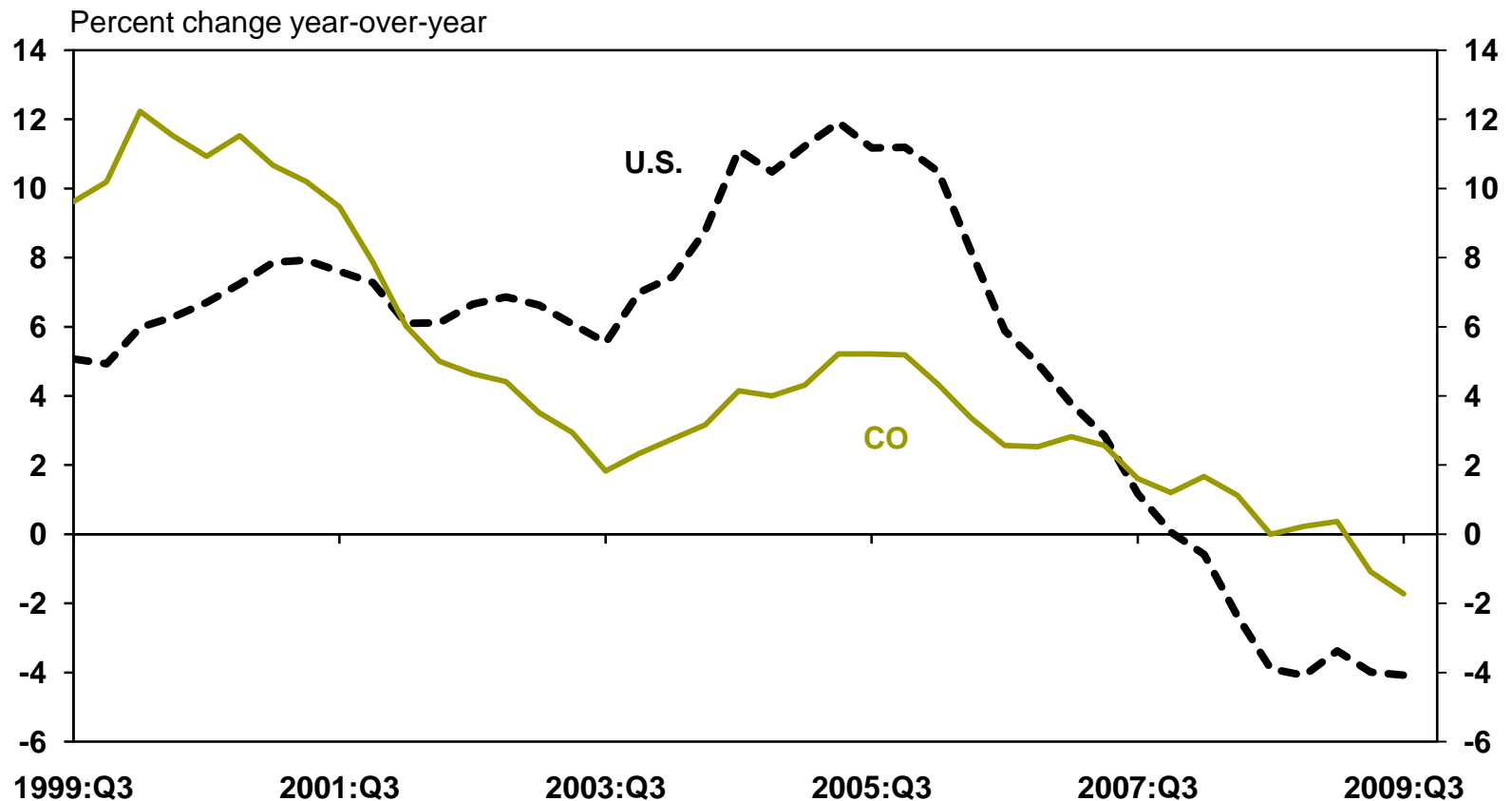
Per Capita Stimulus Package Spending U.S. and Tenth District States



Source: Recovery.gov

Local home prices have also held up better than in the nation

Quality-Adjusted Home Price Growth



Foreclosures have risen in Colorado, but still aren't in a league with CA, NV, AZ, & FL

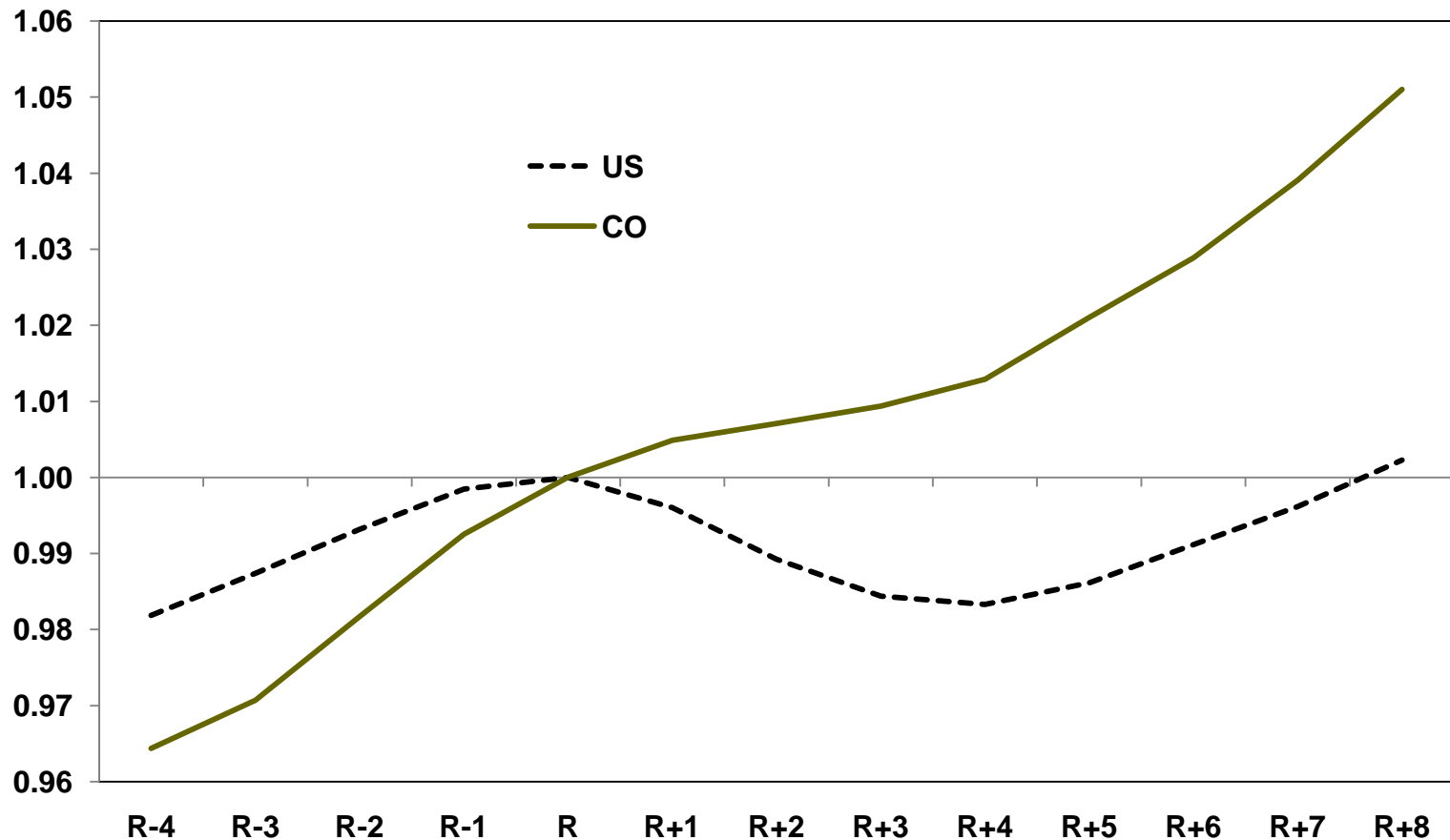
Foreclosure Rate, October 2009



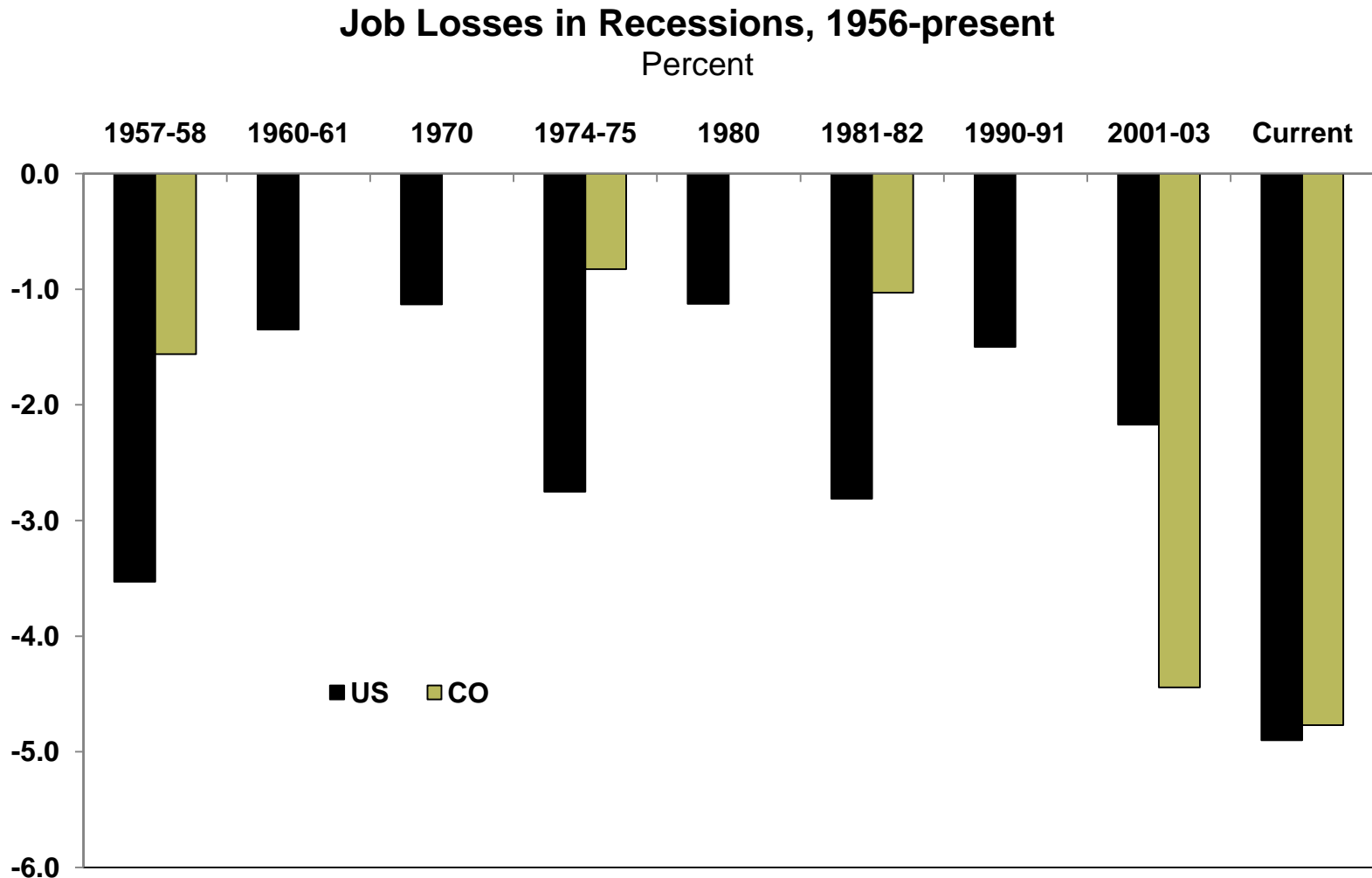
Historically, Colorado fares much better than the nation during recessions

Average Recession Path, 1956-2006

Employment level 4 quarters before and 8 quarters after U.S. jobs peak



The state has generally experienced fairly mild recessions until recently



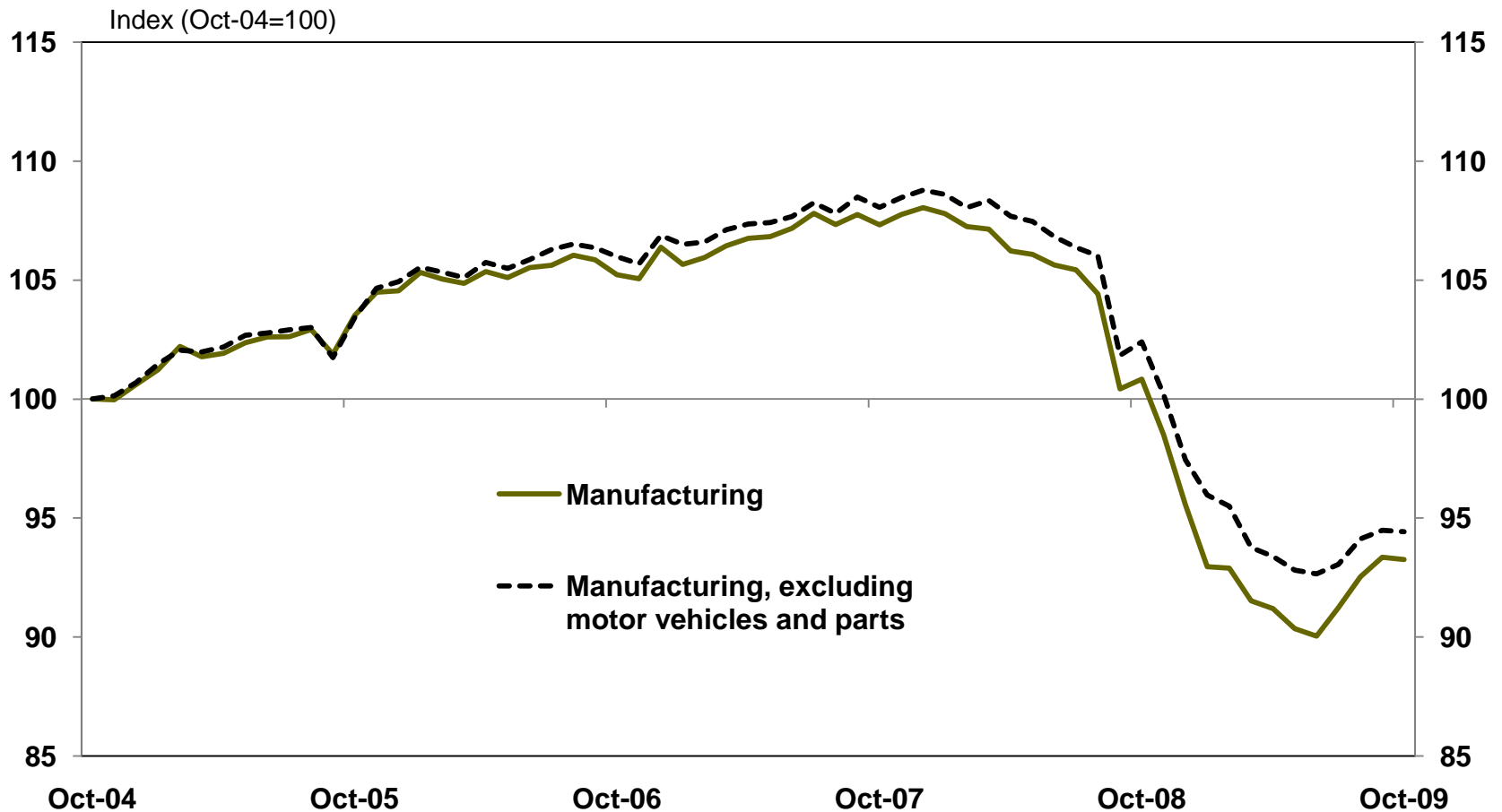
Source: Bureau of Labor Statistics

The Manufacturing Sector

- National manufacturing indicators are up from early summer lows
- Regional factory indicators are showing moderate expansion in recent months
- Firms' optimism is growing, but capital spending plans are modest

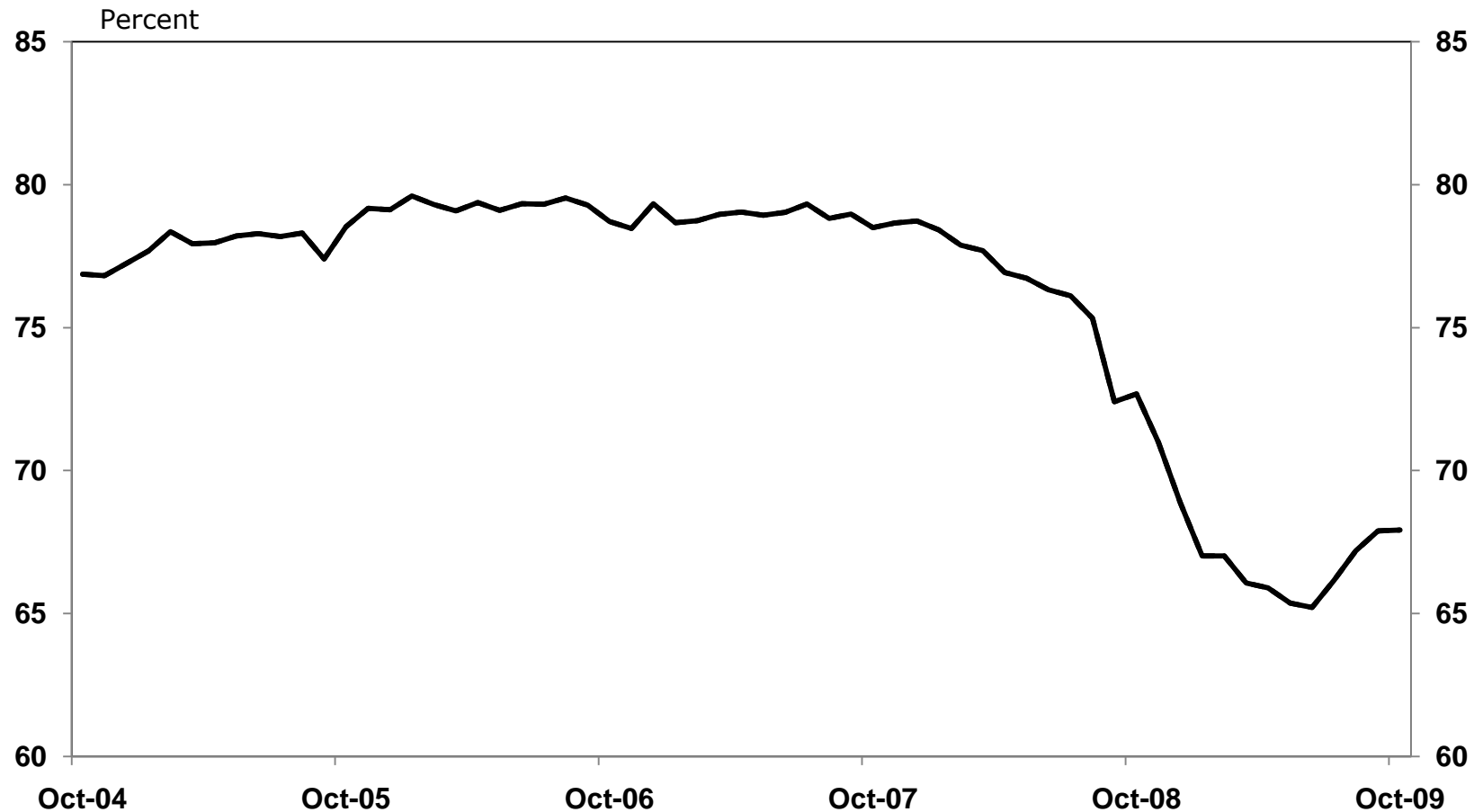
U.S. industrial production appeared to bottom in June, even excluding autos

U.S. Industrial Production Index
Seasonally Adjusted



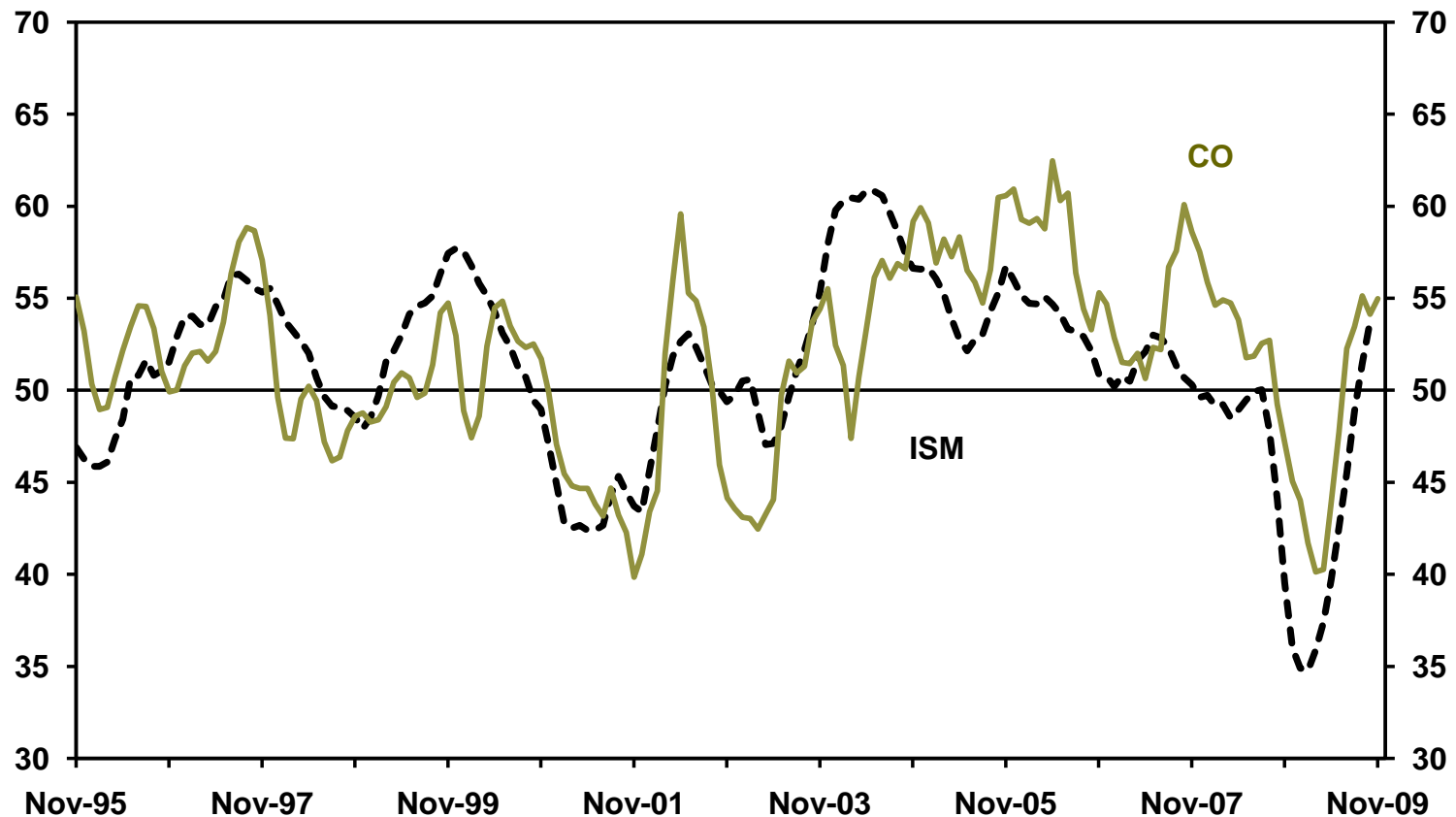
Capacity utilization has risen in recent months, but much excess remains

U.S. Manufacturing Capacity Utilization Rate
Seasonally Adjusted



Manufacturing activity in Colorado has expanded the past few months

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

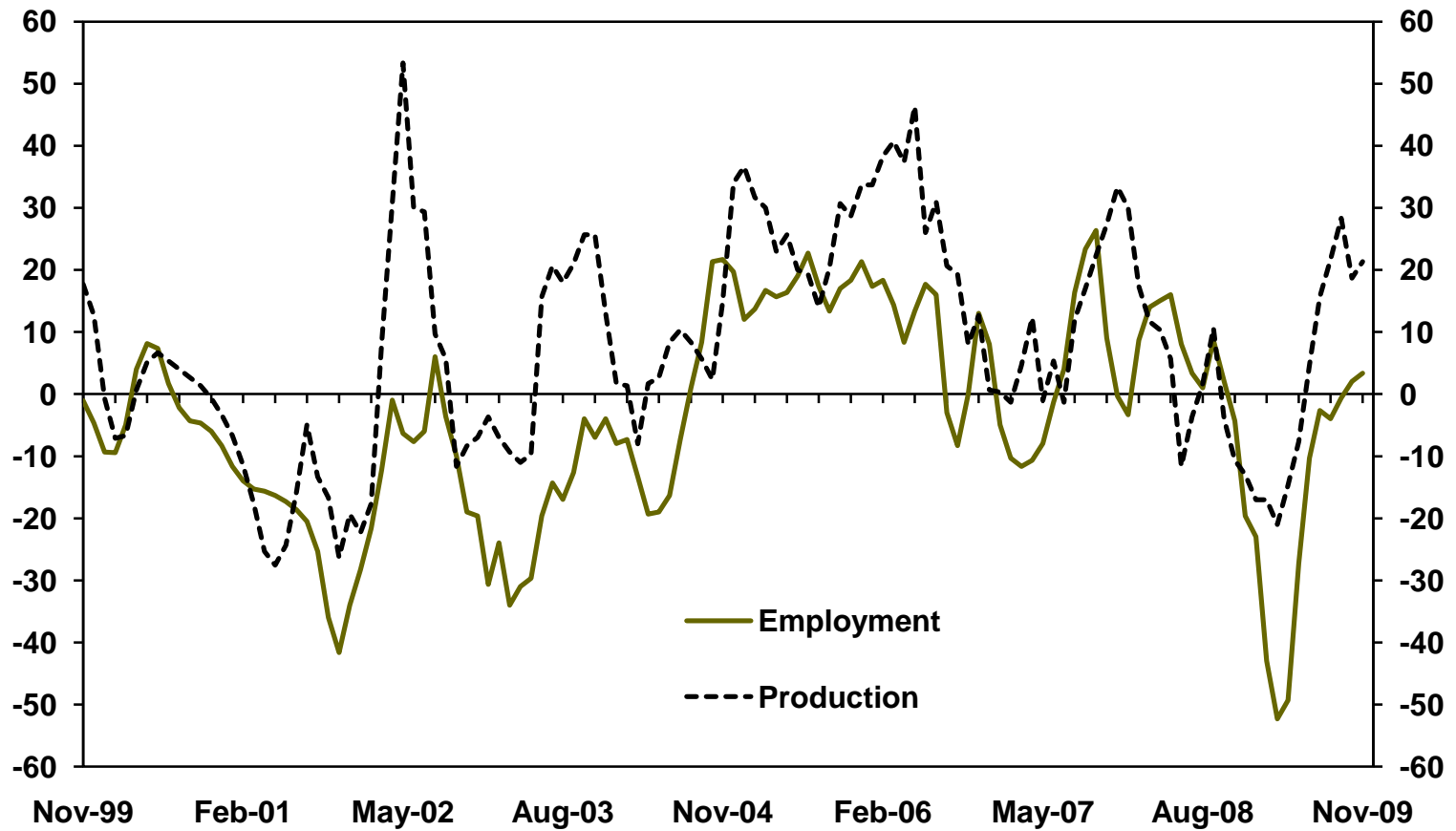


Note: CO index is computed on ISM basis (50 = zero change)

Source: ISM, FRBKC Manufacturing Survey

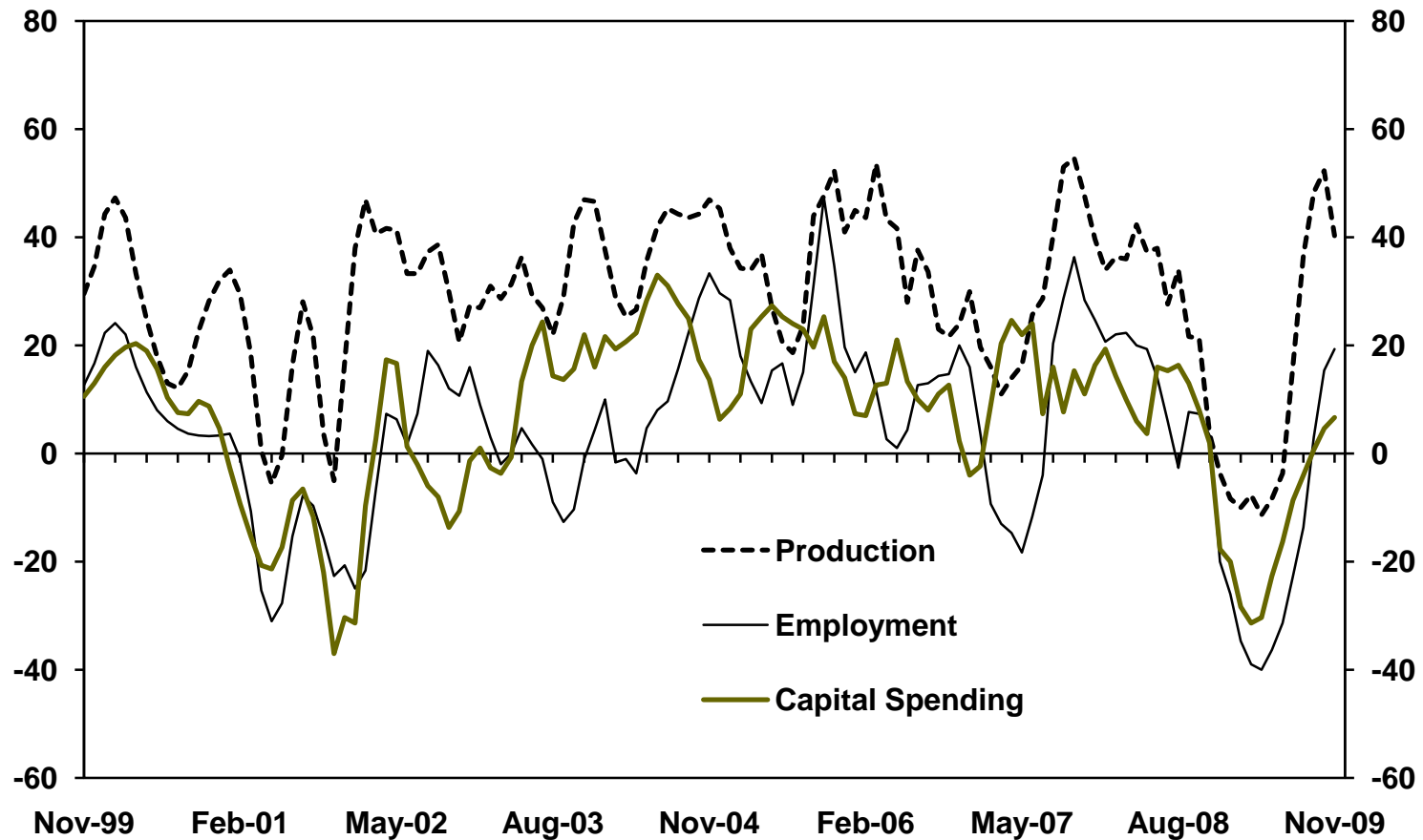
Productivity growth has been strong

CO Manufacturing Indexes
Month-over-month, 3-month moving avg.



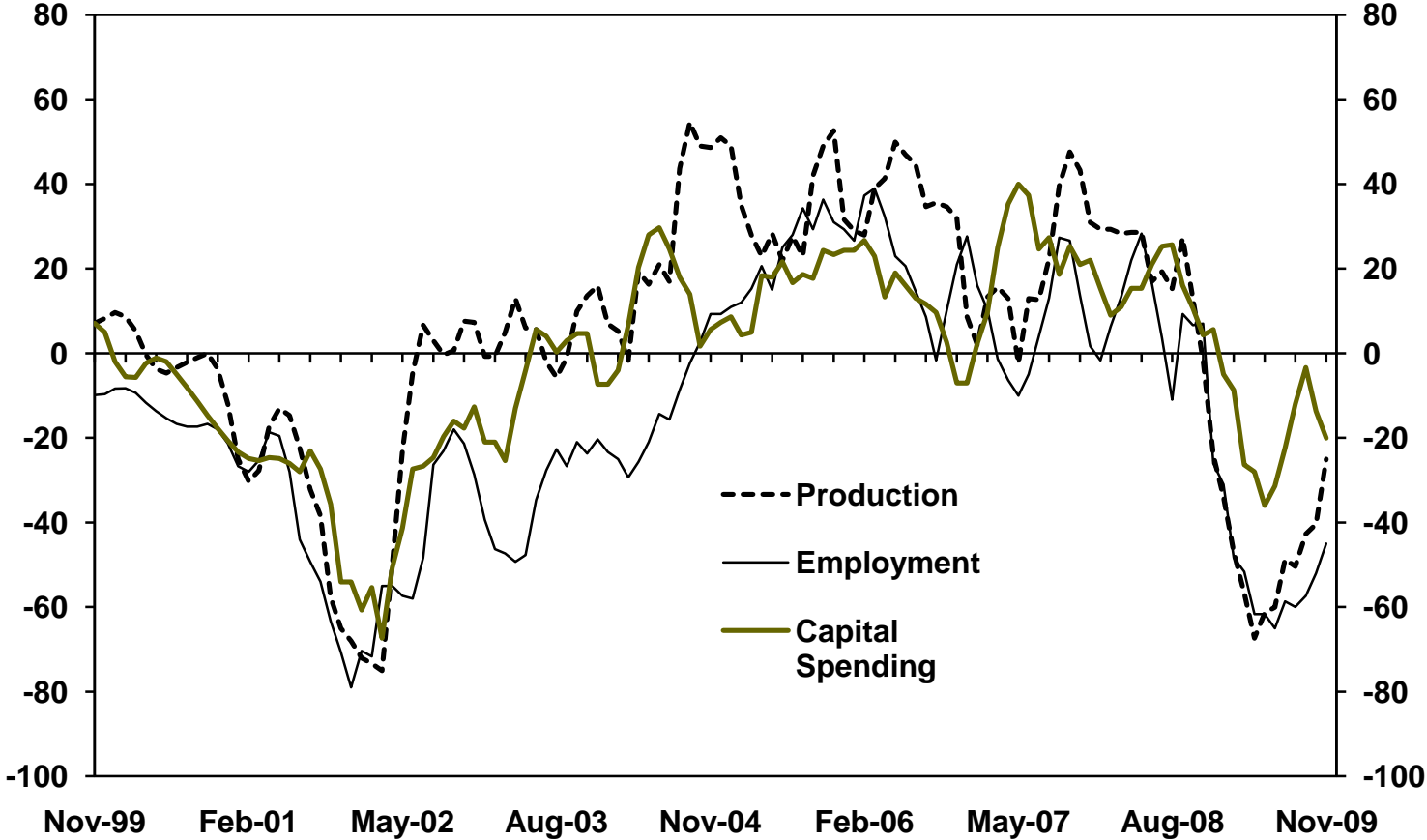
Hiring is expected to pick up somewhat in coming months, but little capex is planned

CO Manufacturing Indexes
Six-month ahead, 3-month moving avg.



But as in the nation, factory activity in the state remains well below year-ago levels

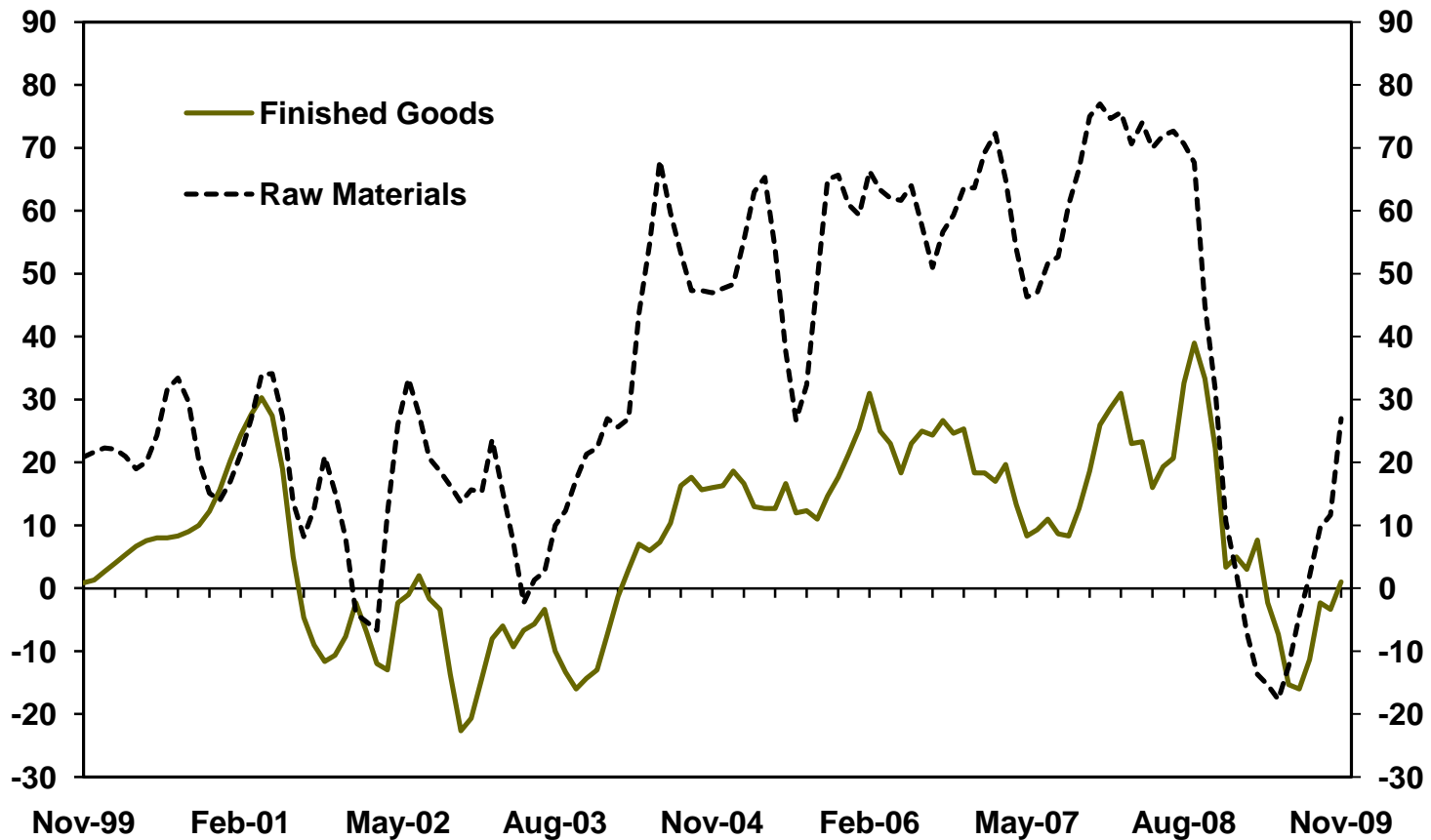
CO Manufacturing Indexes
Year-over-year, 3-month moving avg.



Source: FRBKC Manufacturing Survey

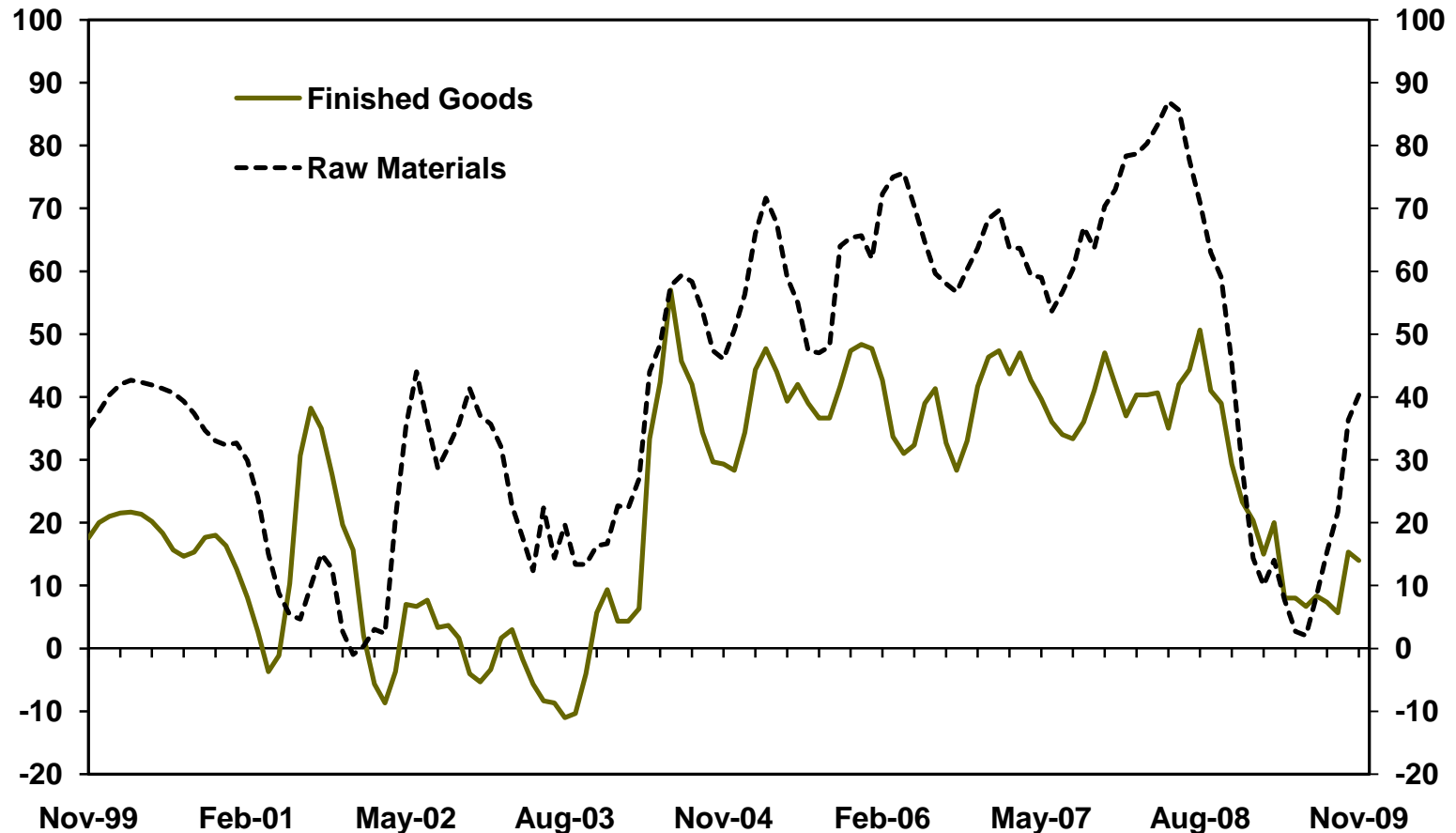
Input prices have begun rising again, while output prices have leveled

CO Manufacturing Price Indexes
Month-over-month, 3-month moving avg.



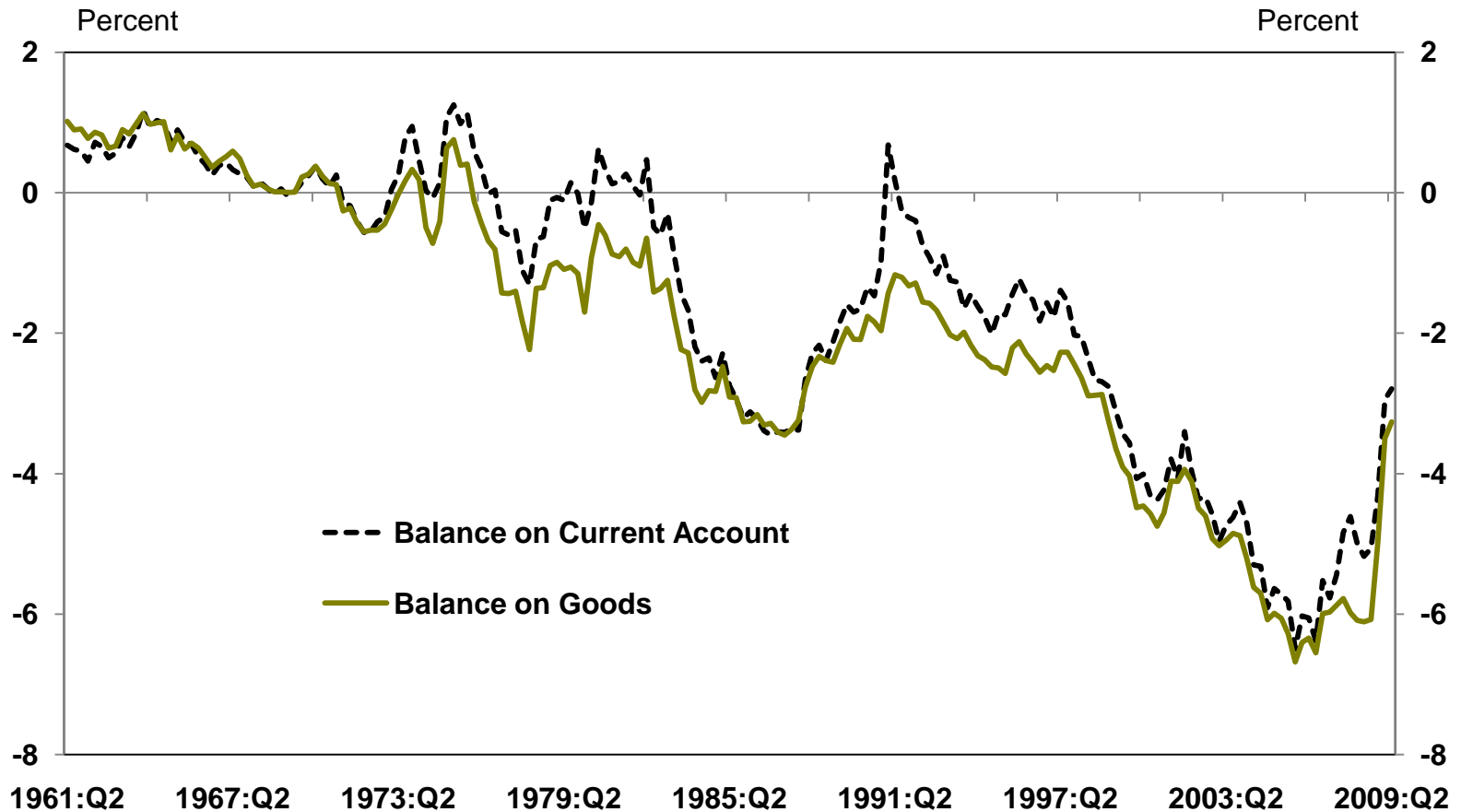
Expectations are for continued increases in material costs but little ability to pass through

CO Manufacturing Price Indexes
Six-month ahead, 3-month moving avg.



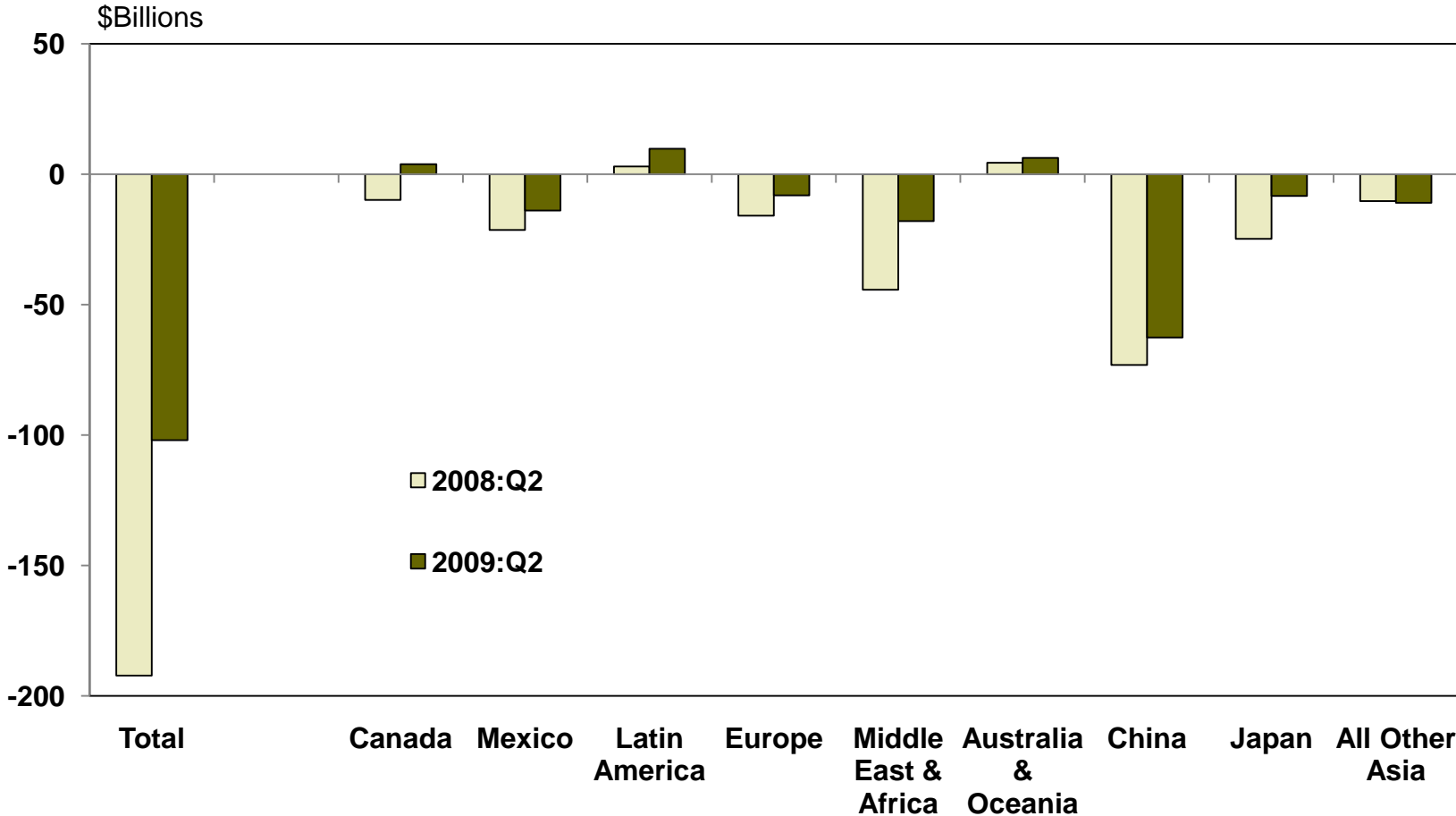
Longer-term, the U.S. trade imbalance provides a future opportunity

U.S. Trade Deficit As a Share of GDP



The largest U.S. trade deficits are with Asia and Mexico

U.S. Trade Balance by Export Destination



Source: WISERTrade, U.S. Bureau of Economic Analysis

Colorado currently exports more to Asia than the U.S.

Exports by Destination, 2008



Summary

- ❑ The U.S. economy is growing again, but recovery speed is expected to be modest
- ❑ Colorado's economy remains in better shape and usually recovers with the nation
- ❑ Manufacturing activity both nationally and locally is rebounding, and exports present future opportunities