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June 16, 2009

Economic Conditions: Cautiously Optimistic for a Soft Recovery



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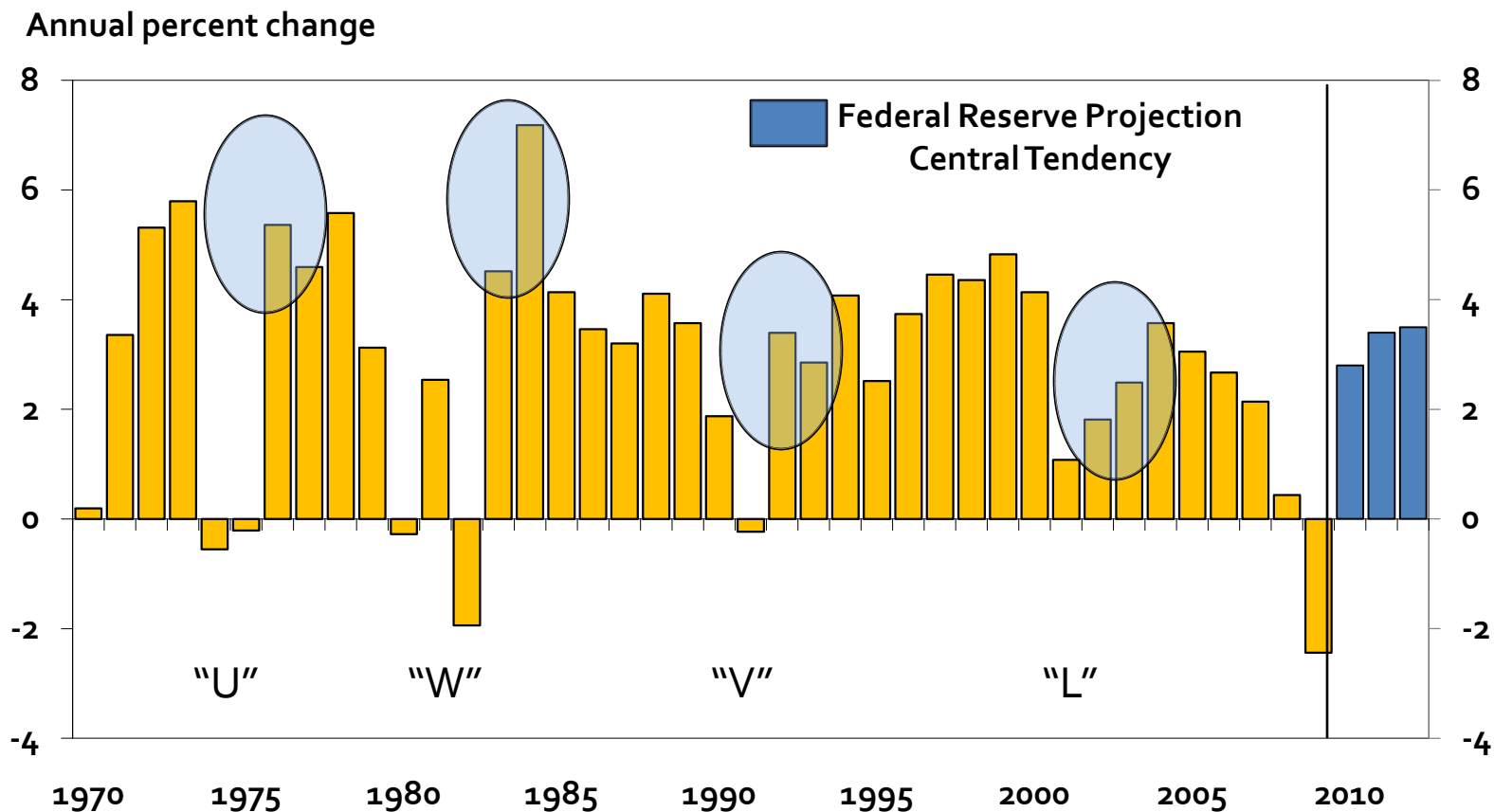
Today's Roadmap

- **The Economic Recovery is Underway**
- **Concerns Shift from Growth to Inflation**
- **Implications for Agriculture**



The U.S. economy is projected to rebound in 2010.

Real GDP Growth

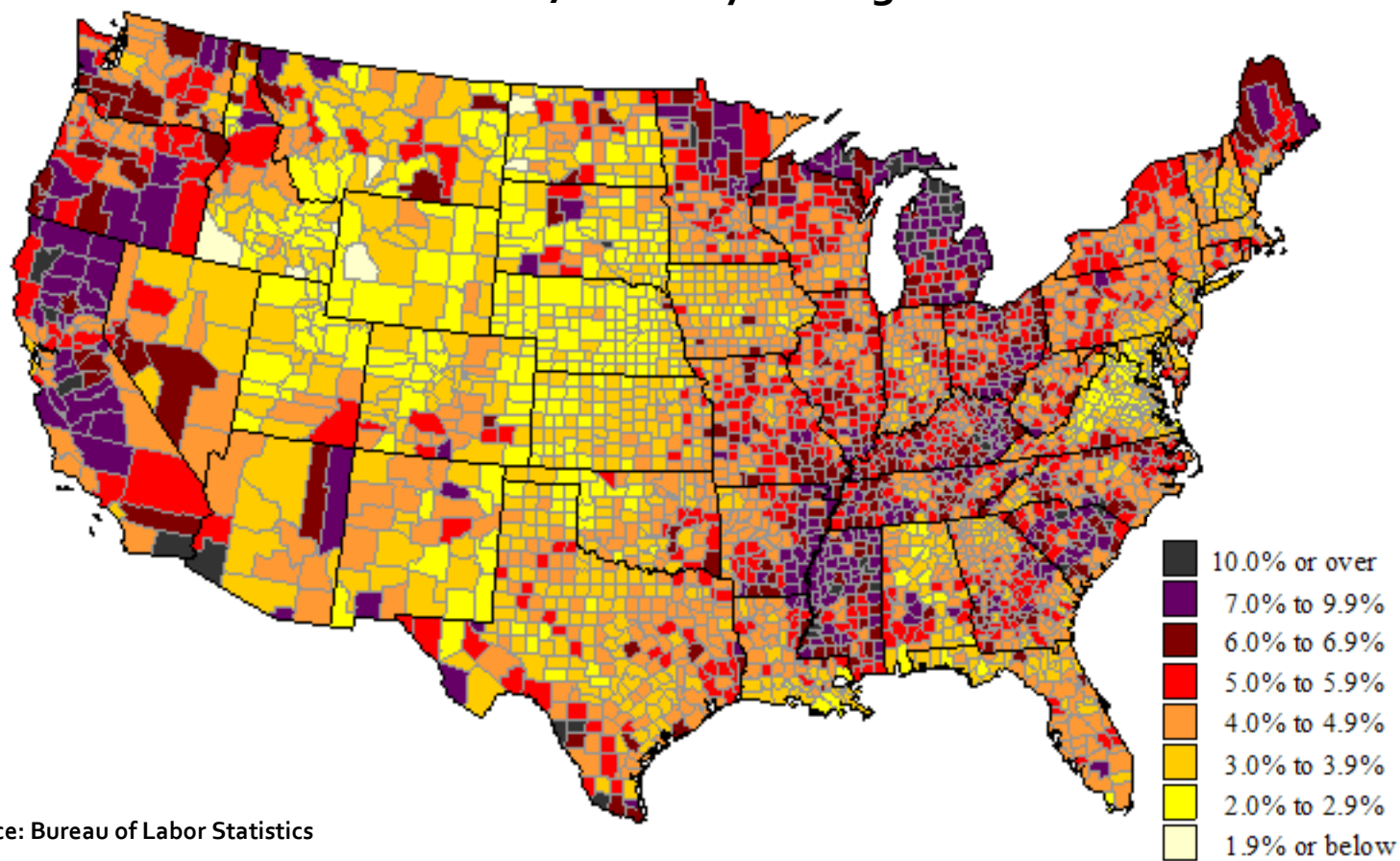


Source: Bureau of Economic Analysis Federal Reserve Board of Governors



Midwest economies are in better shape.

Unemployment Rate 2007 Monthly Average

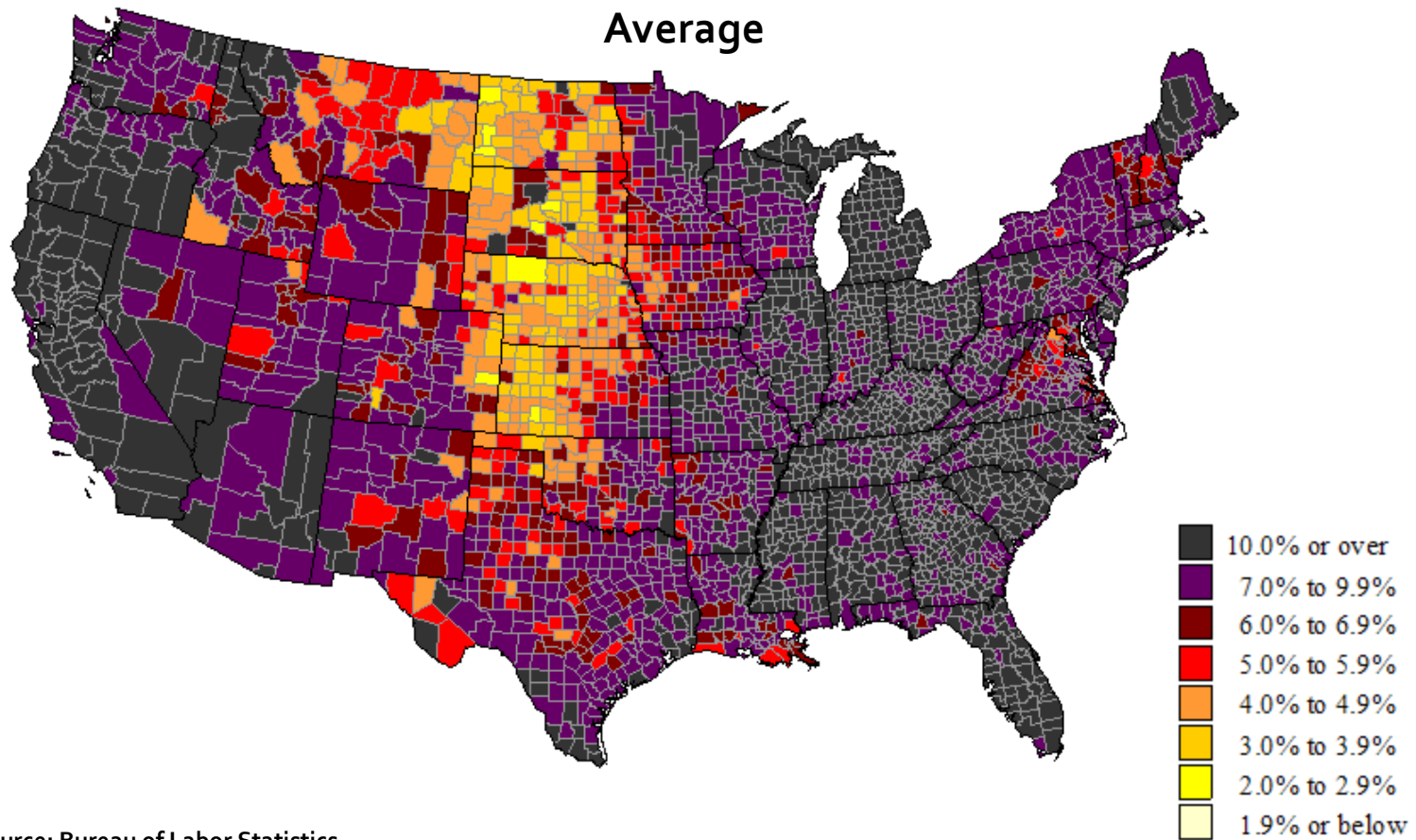


Source: Bureau of Labor Statistics



Midwest economies are in better shape.

Unemployment Rate May 2009 – April 2010 Average

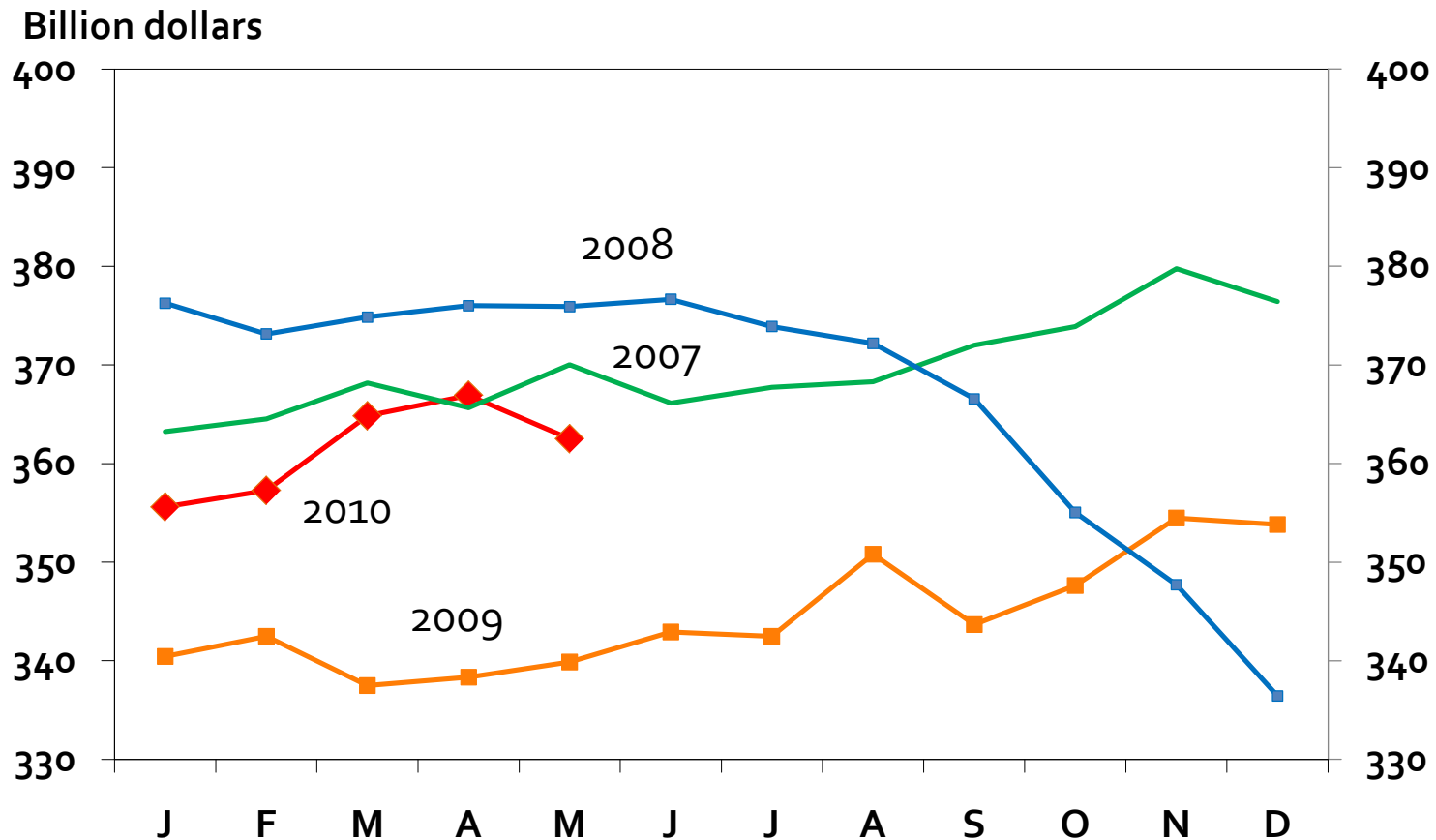


Source: Bureau of Labor Statistics



U.S. consumers are spending money.

U.S. Monthly Retail and Food Sales

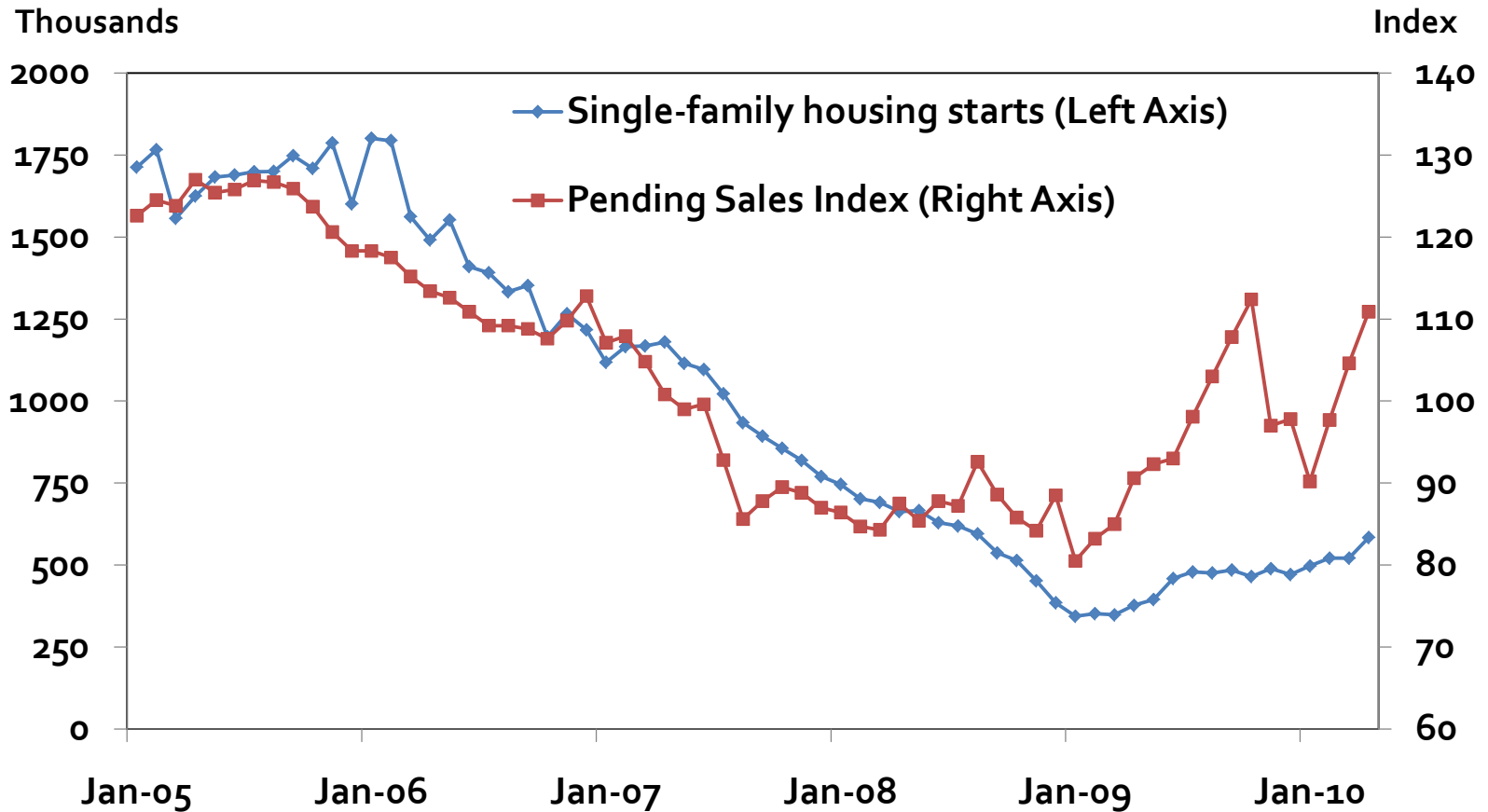


Source: U.S. Census Bureau



Have U.S. housing markets hit bottom?

U.S. Housing Markets

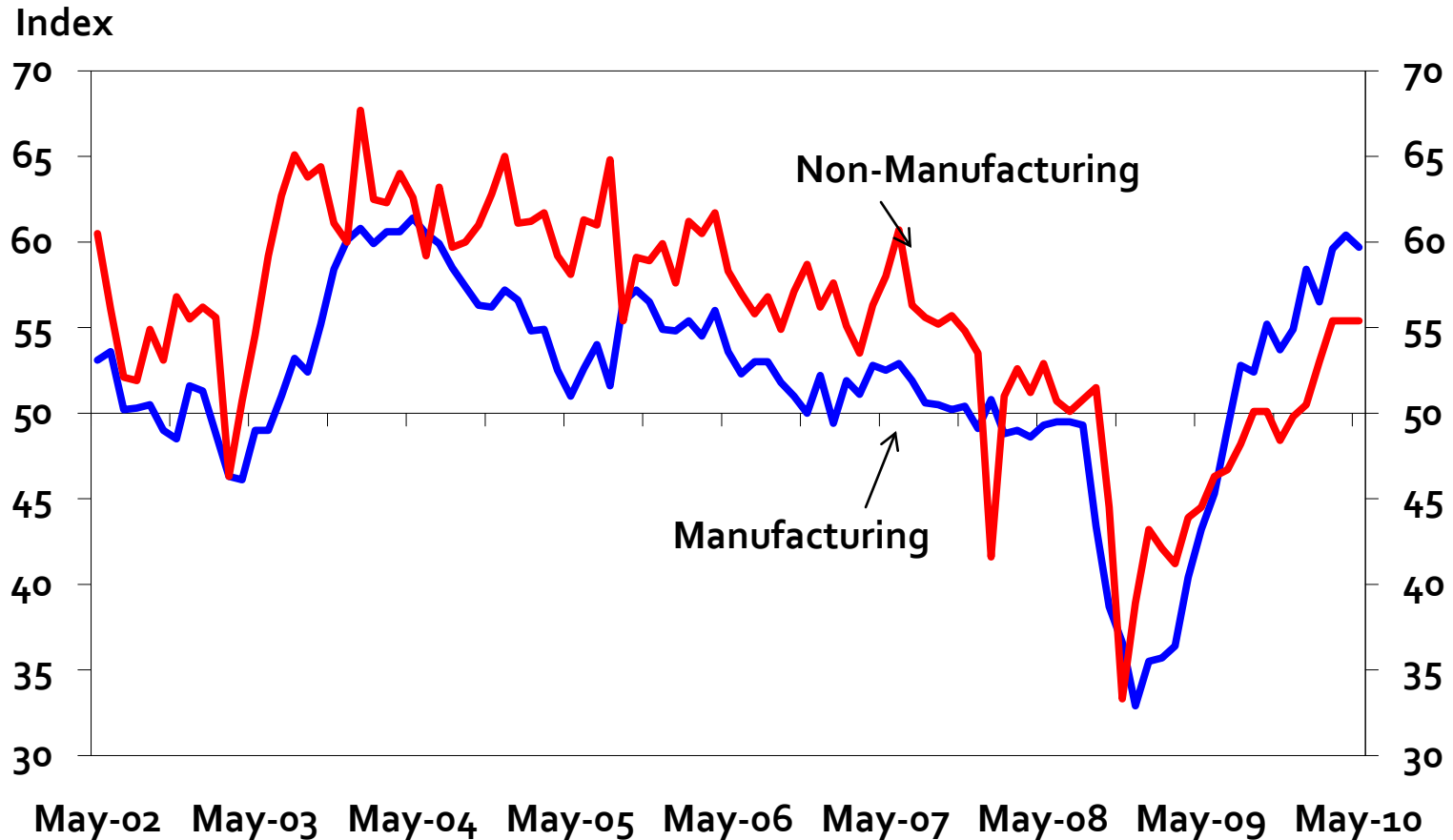


Source: U.S. Census Bureau



Business activity is expanding.

U.S. Manufacturing Activity Indices

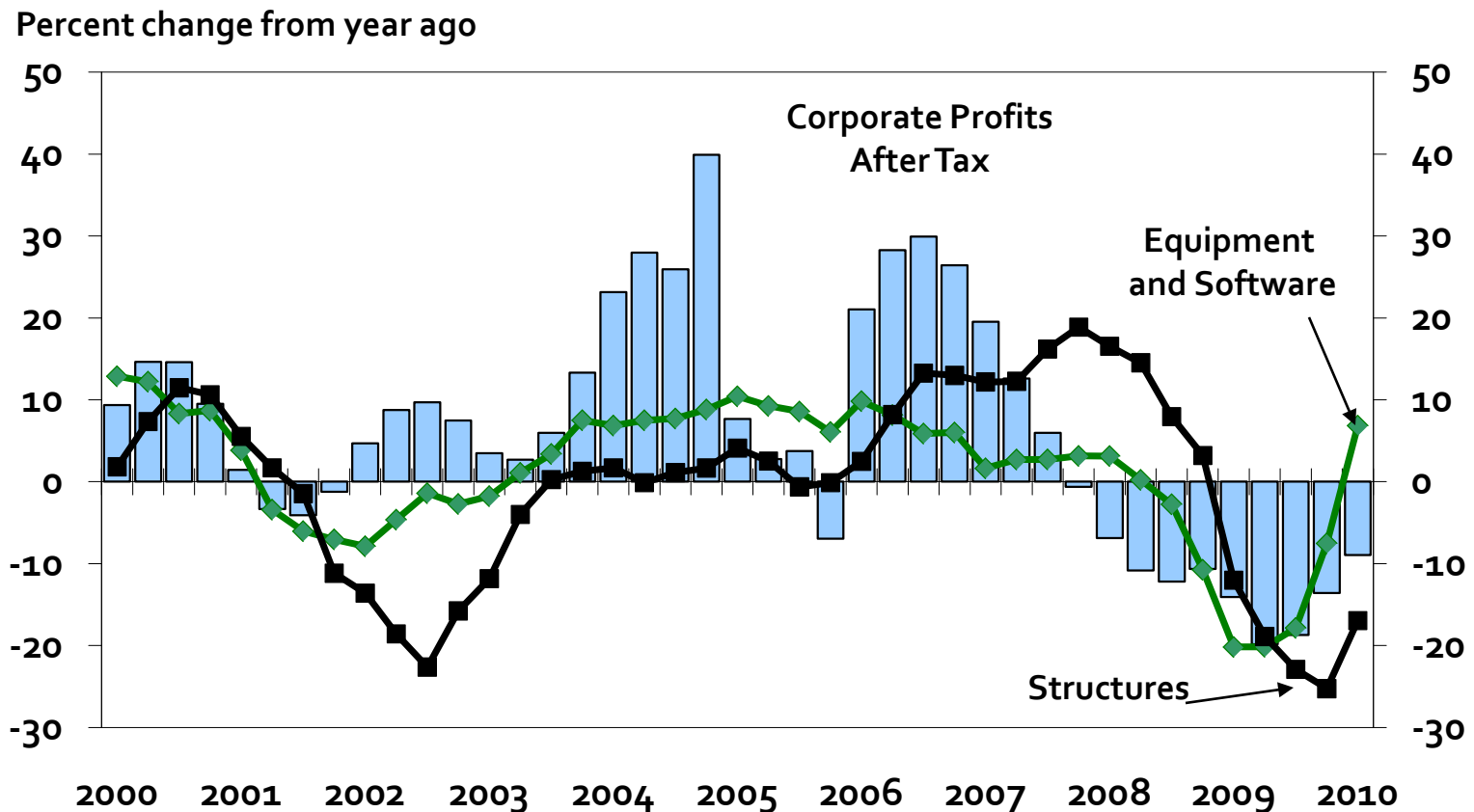


Source: Institute of Supply Management



Corporate profits and business investment are beginning to rebound.

Corporate Profits and Nonresidential Fixed Investment

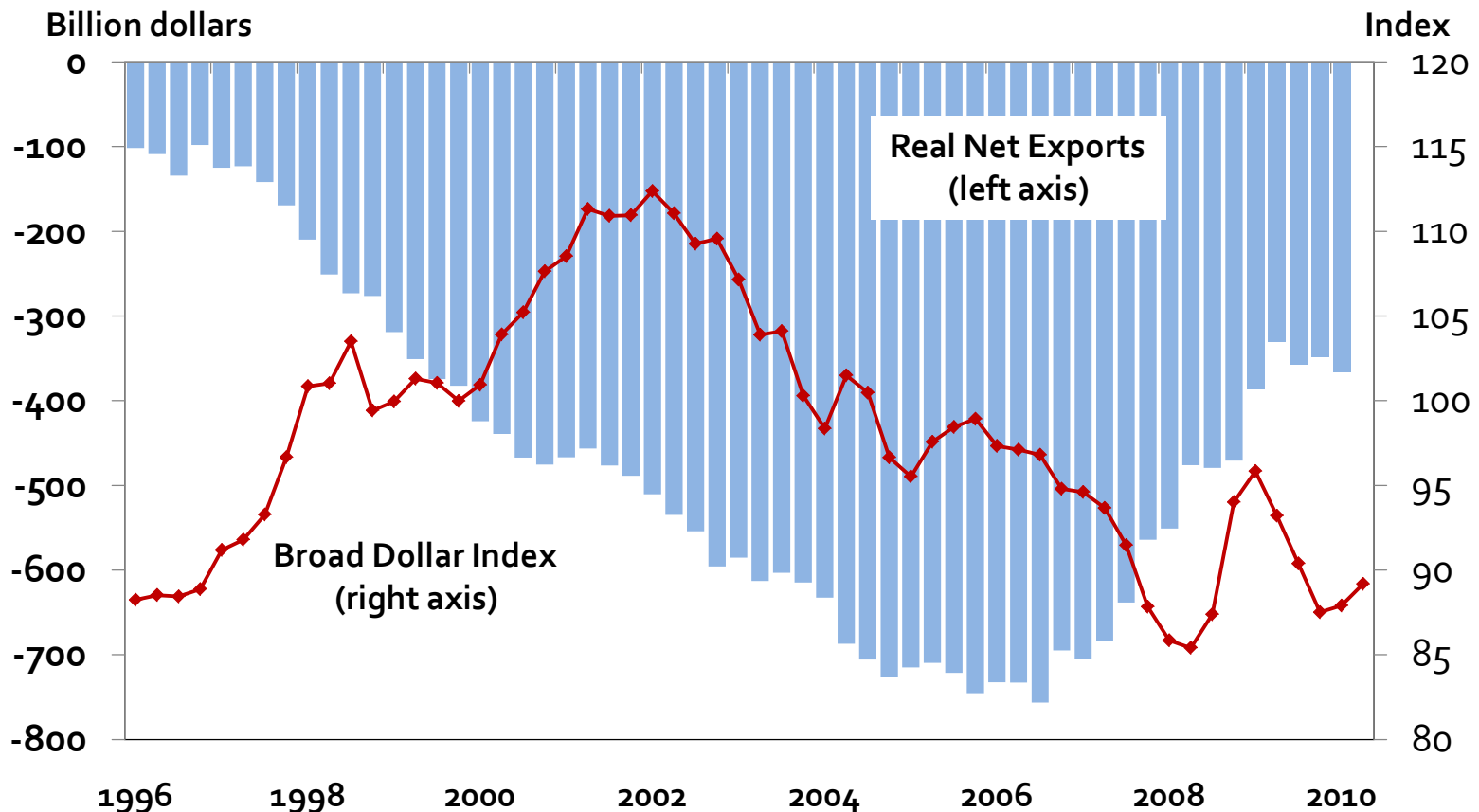


Source: Bureau of Economic Analysis



After dramatic improvements since 2007, U.S. net exports have stabilized.

U.S. Real Net Exports of Goods and Services and Value of the Dollar

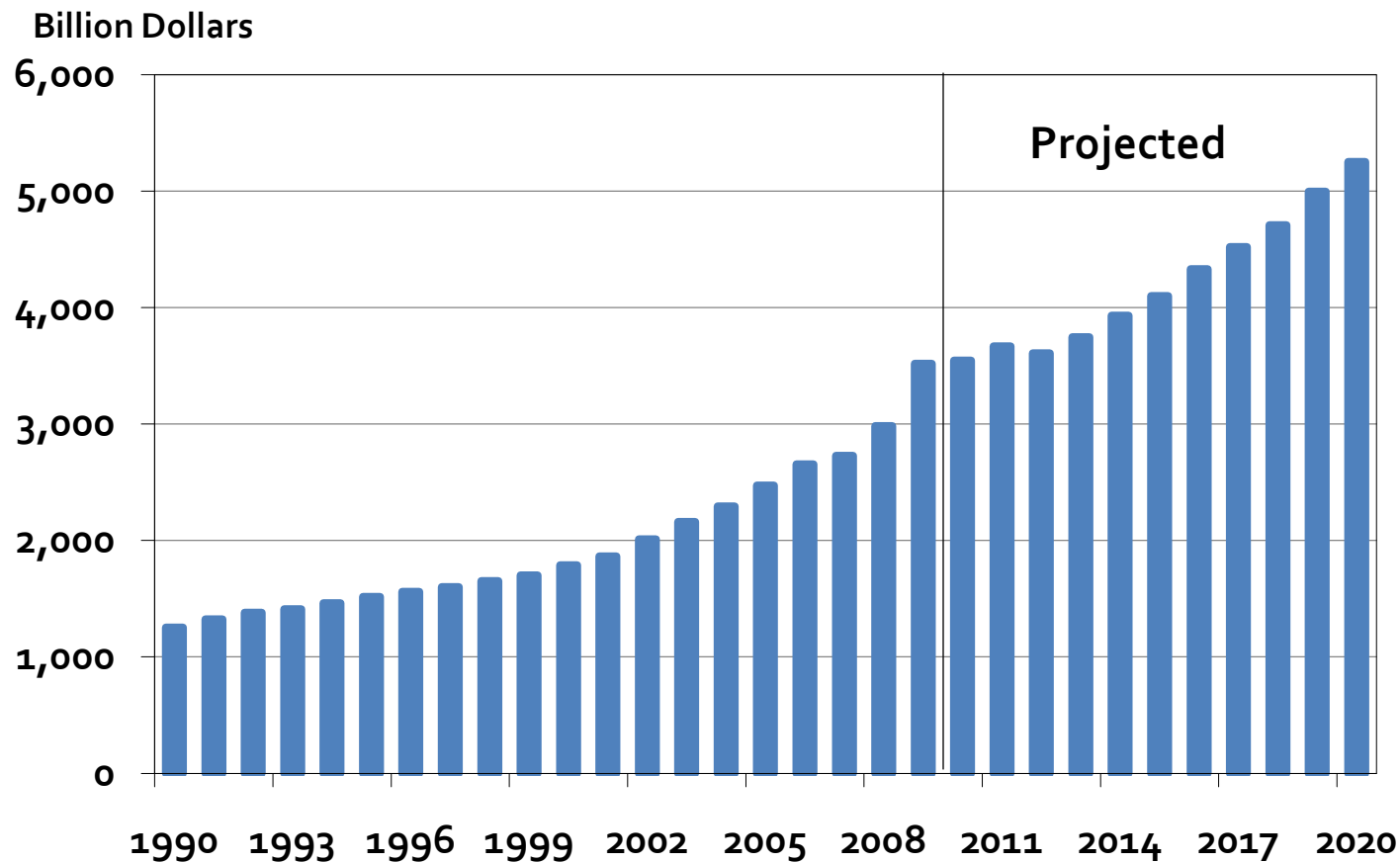


Source: Bureau of Economic Analysis and Federal Reserve Board of Governors



In the short run, deficit spending is an economic stimulus.

U.S. Government Outlays



Source: Congressional Budget Office, March 2010



Today's Roadmap

- **The Economic Recovery is Underway**
- **Concerns Shift from Growth to Inflation**



Inflation is based on money and velocity.

Quantity Theory of Money

$$\text{Price} = \frac{\text{Money} * \text{Velocity}}{\text{Quantity}}$$

Definition of Inflation:

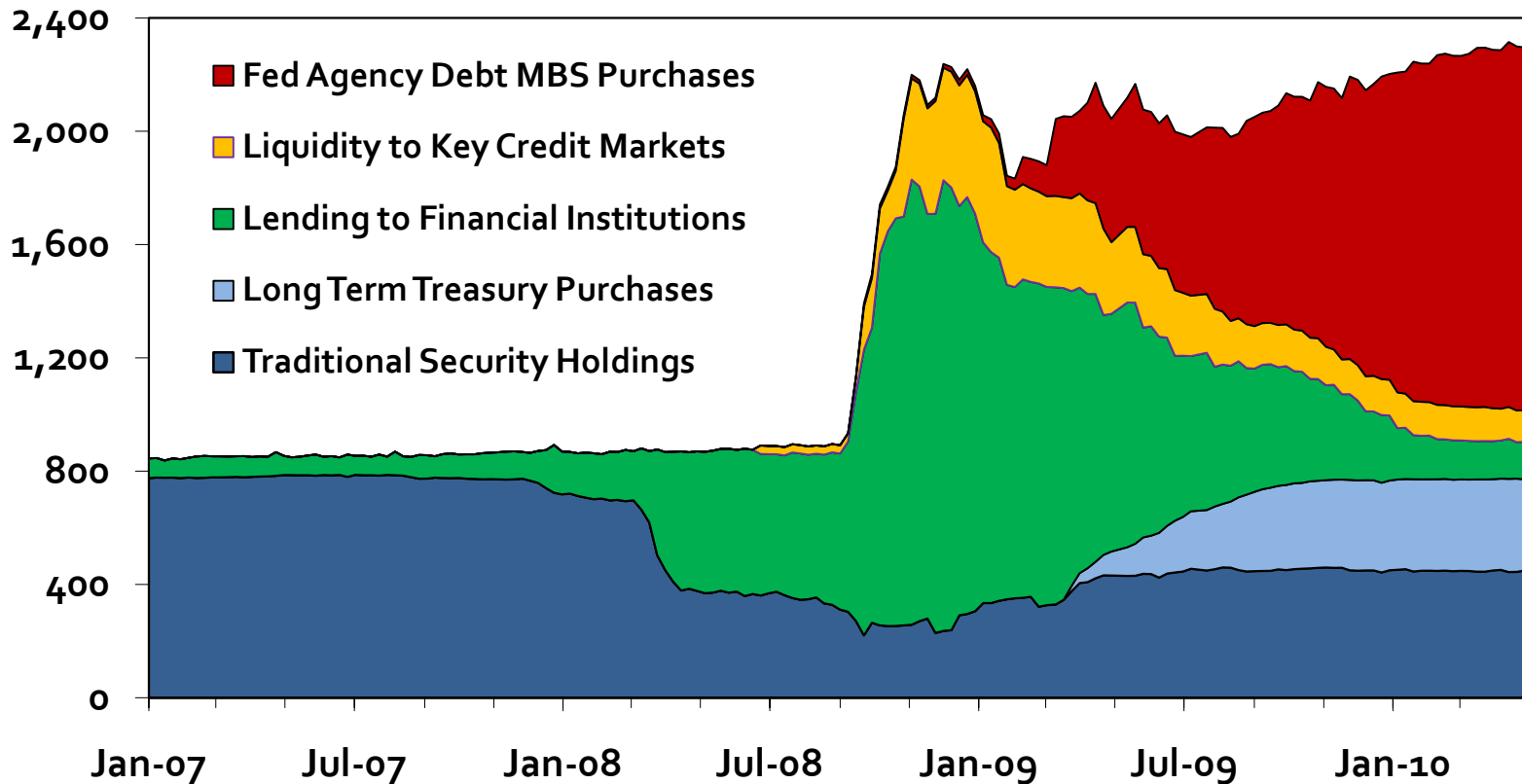
Too much money $M \uparrow$
chasing $V \uparrow$
too few goods $Q \downarrow$



*The Fed has increased the monetary base.
But, the bulk of it is in excess reserves.*

Federal Reserve Balance Sheet: Assets

Billion Dollars



Source: Federal Reserve Bank of Cleveland



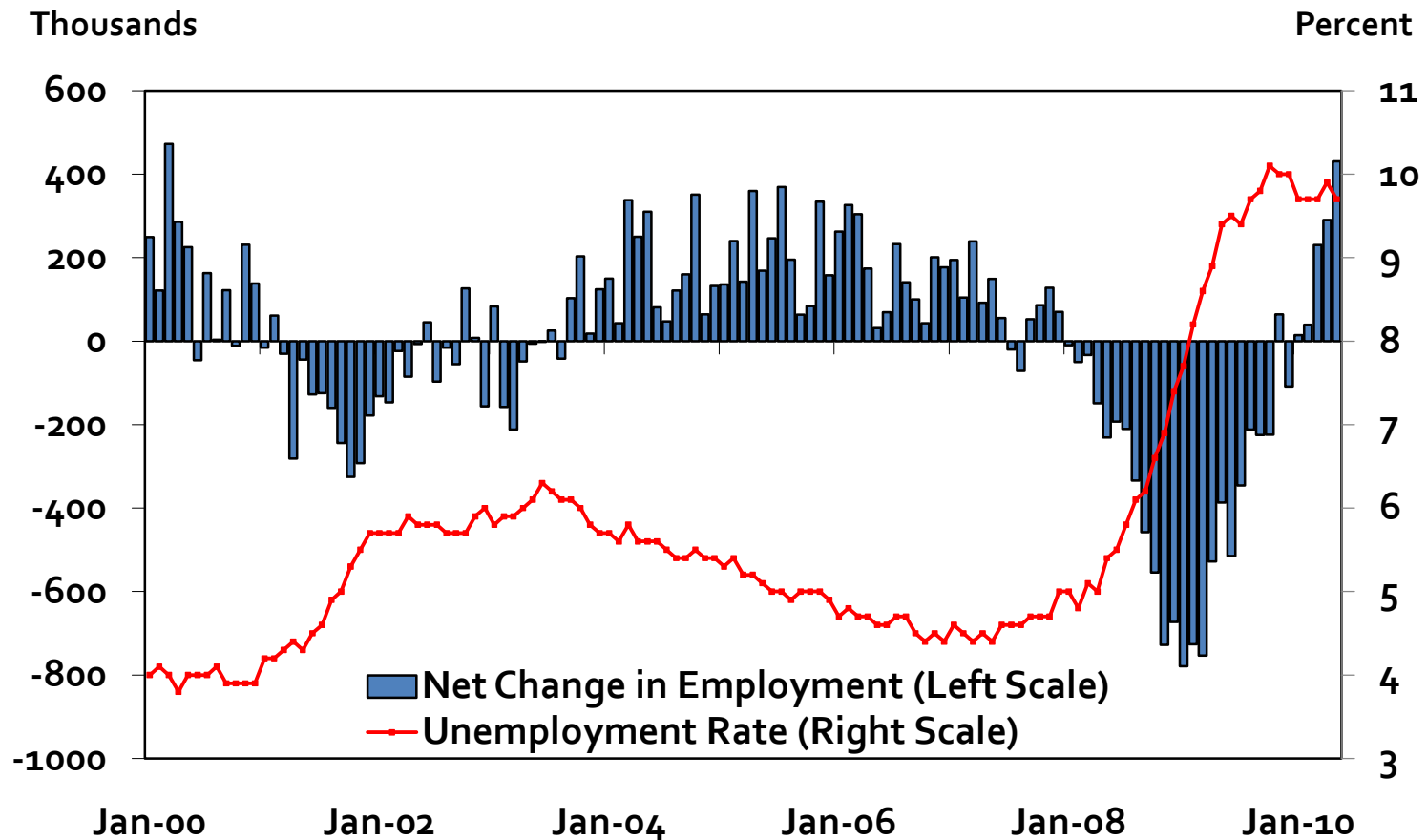
How will the Federal Reserve shrink its balance sheet with Agency and MBS debt?

- Hold to maturity
- Sell assets
- Keep reserves on deposit at the Fed.
 - **Interest on excess reserves**
 - **Reverse repurchase agreements**
 - **Term deposits**
- All strategies lead to higher interest rates.
 - **When?**
 - **How fast?**



Labor markets are key to "chasing" and inflation.

Nonfarm Employment Change and Unemployment Rate



Source: Bureau of Labor Statistics



Implications for Agriculture



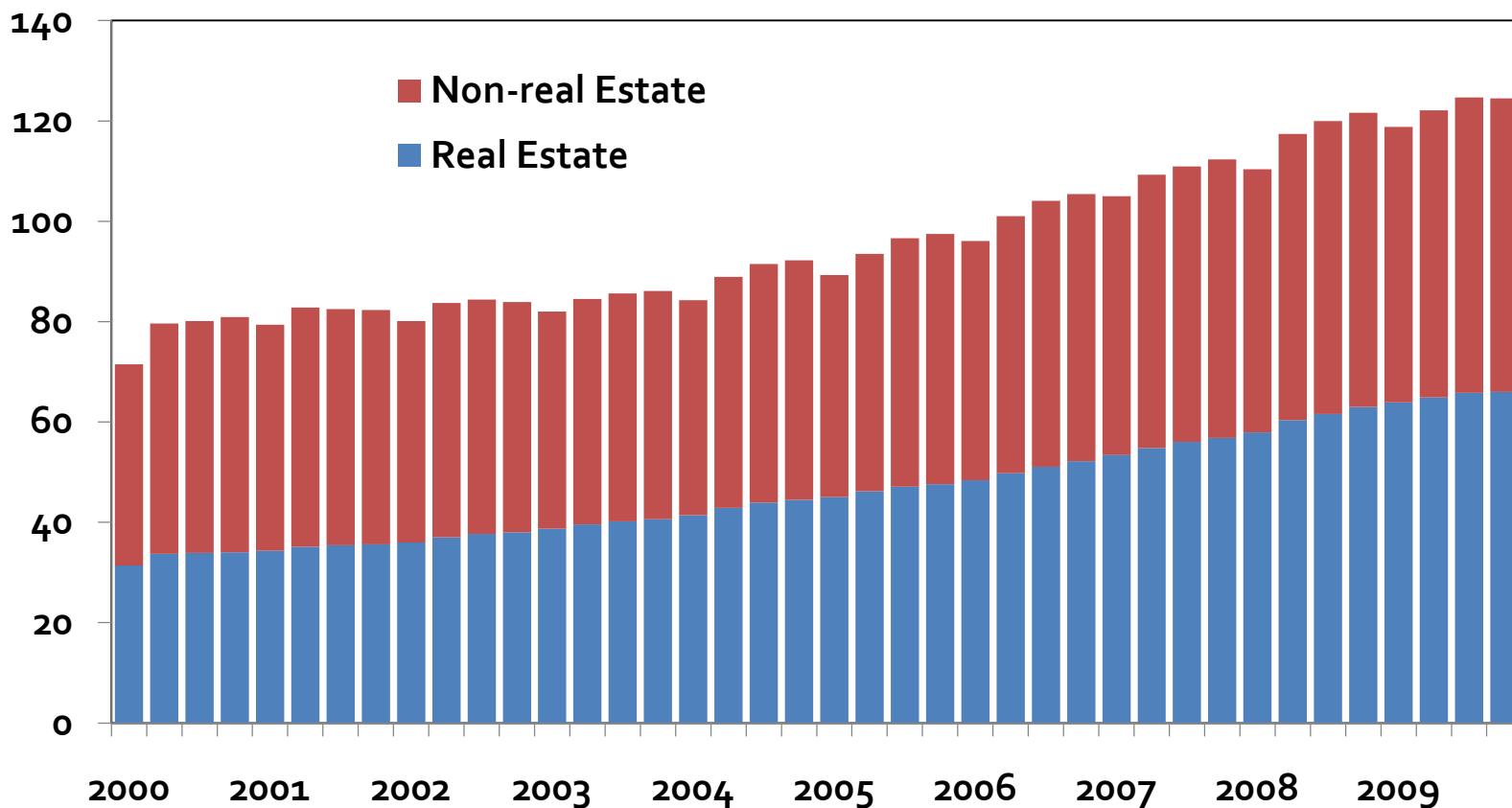
- Financial markets



Farm debt continues to rise at commercial banks.

Farm Debt Outstanding at Commercial Banks

Billion dollars



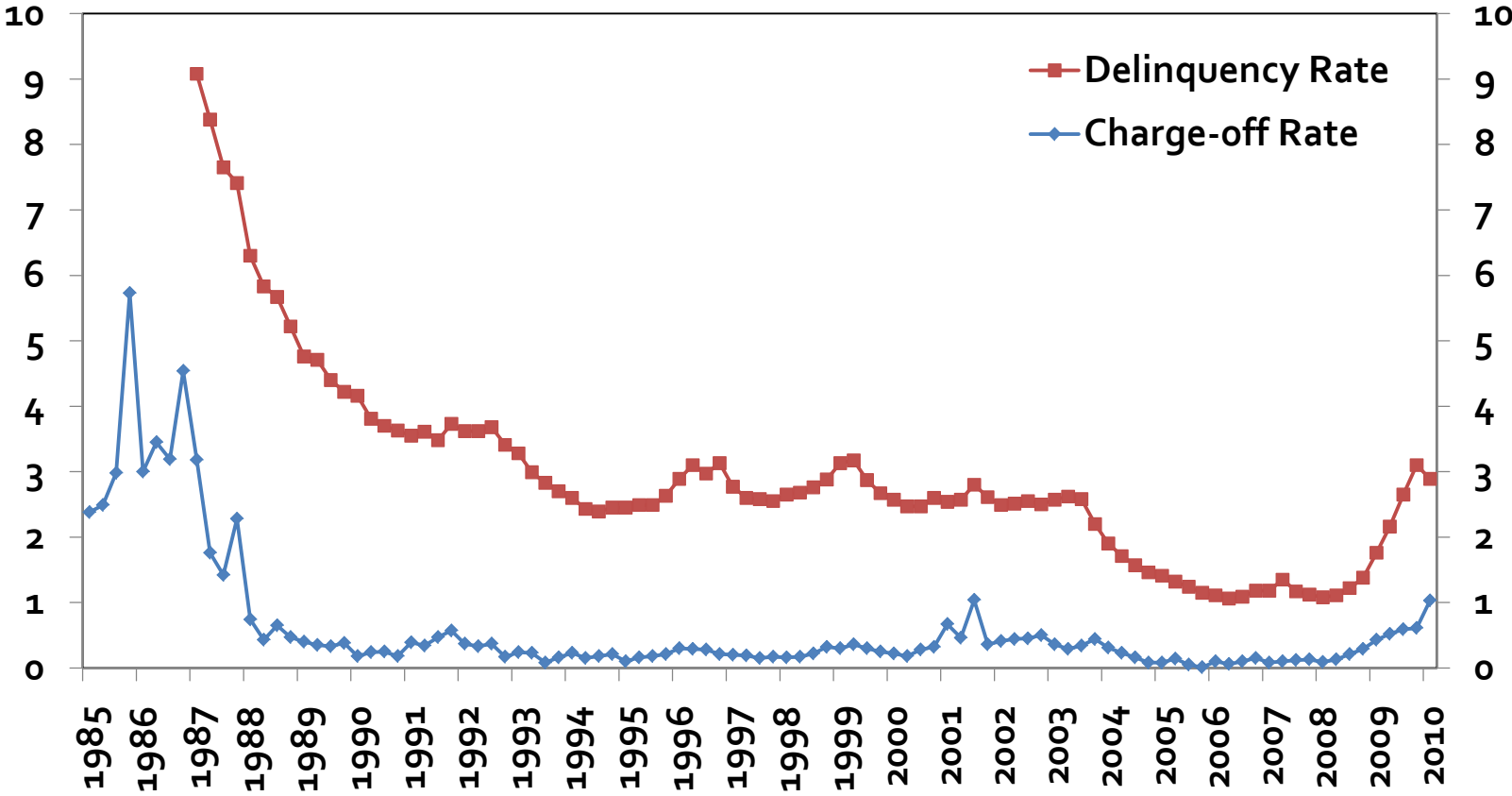
Source: Federal Reserve Board of Governors



How is U.S. export activity?

Charge-off and Delinquency Rates On Agricultural Loans

Percent



Source: Federal Reserve Board of Governors



Implications for Agriculture



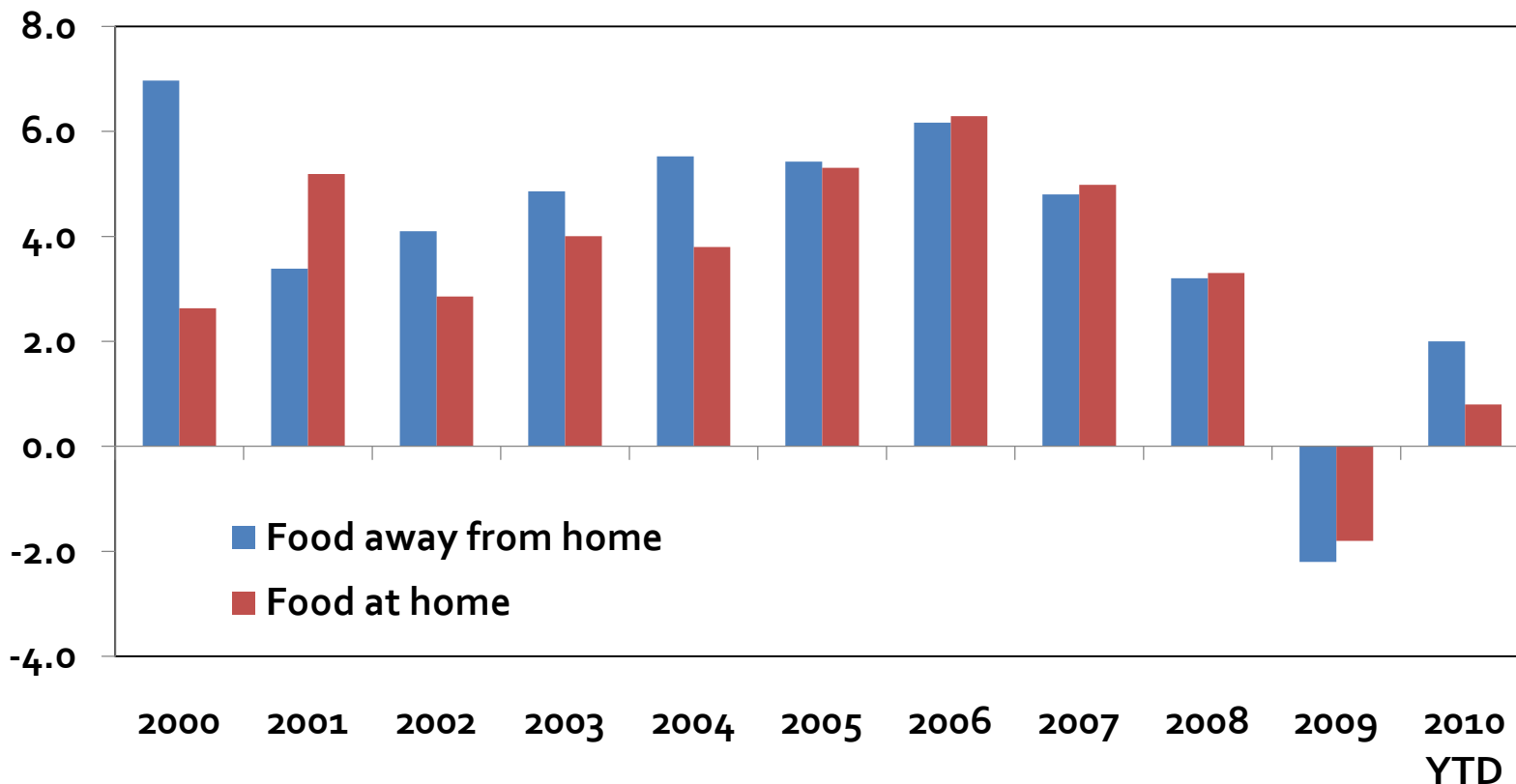
- Financial markets
- U.S. consumer demand



How strong will U.S. food spending rebound?

U.S. Food Expenditures

Percent change from previous year



Source: USDA
2010 data through March



Implications for Agriculture



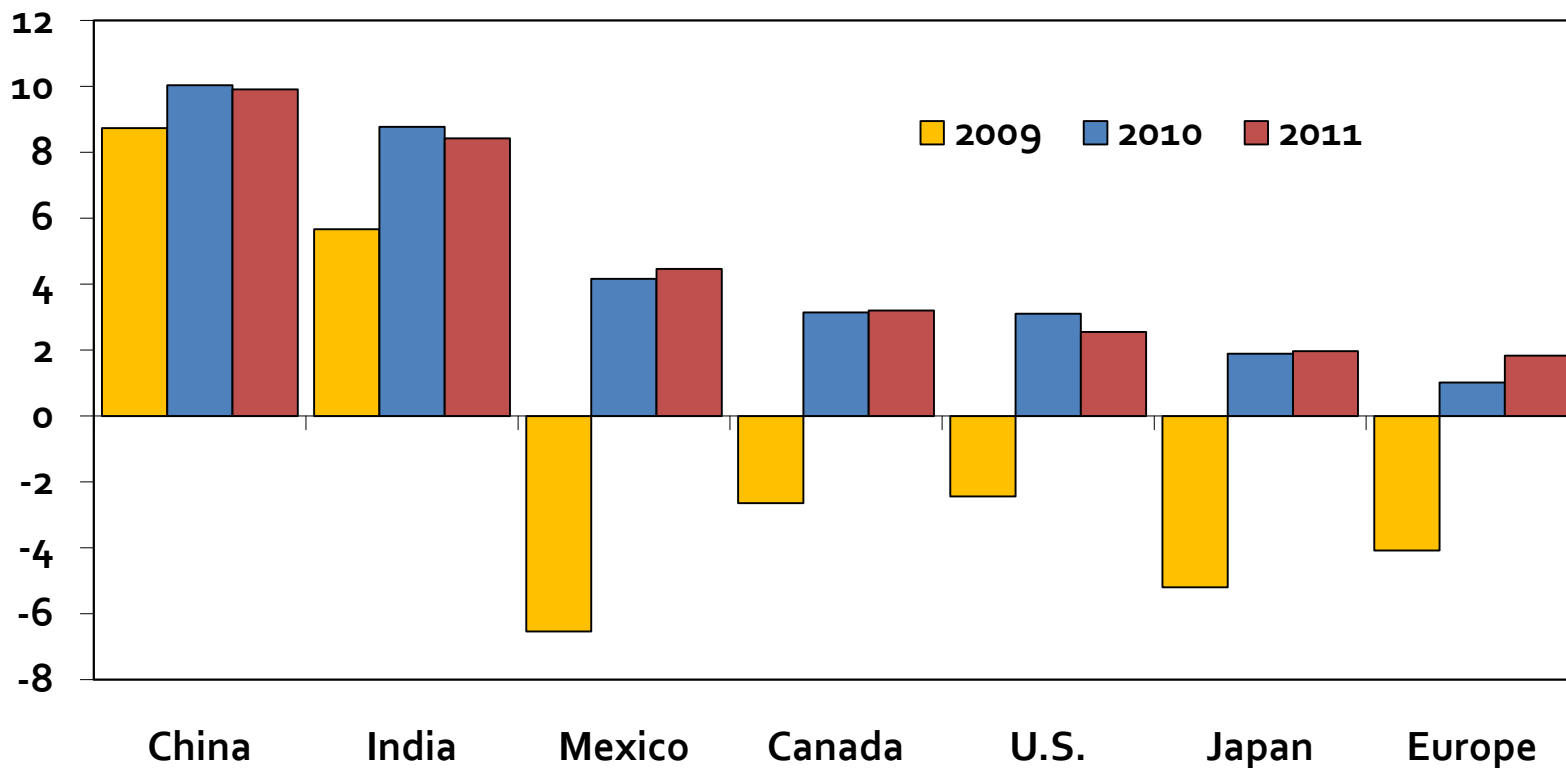
- Financial markets
- U.S. consumer demand
- Export activity



Stronger economic growth is expected through 2011.

GDP Growth

Percent Change



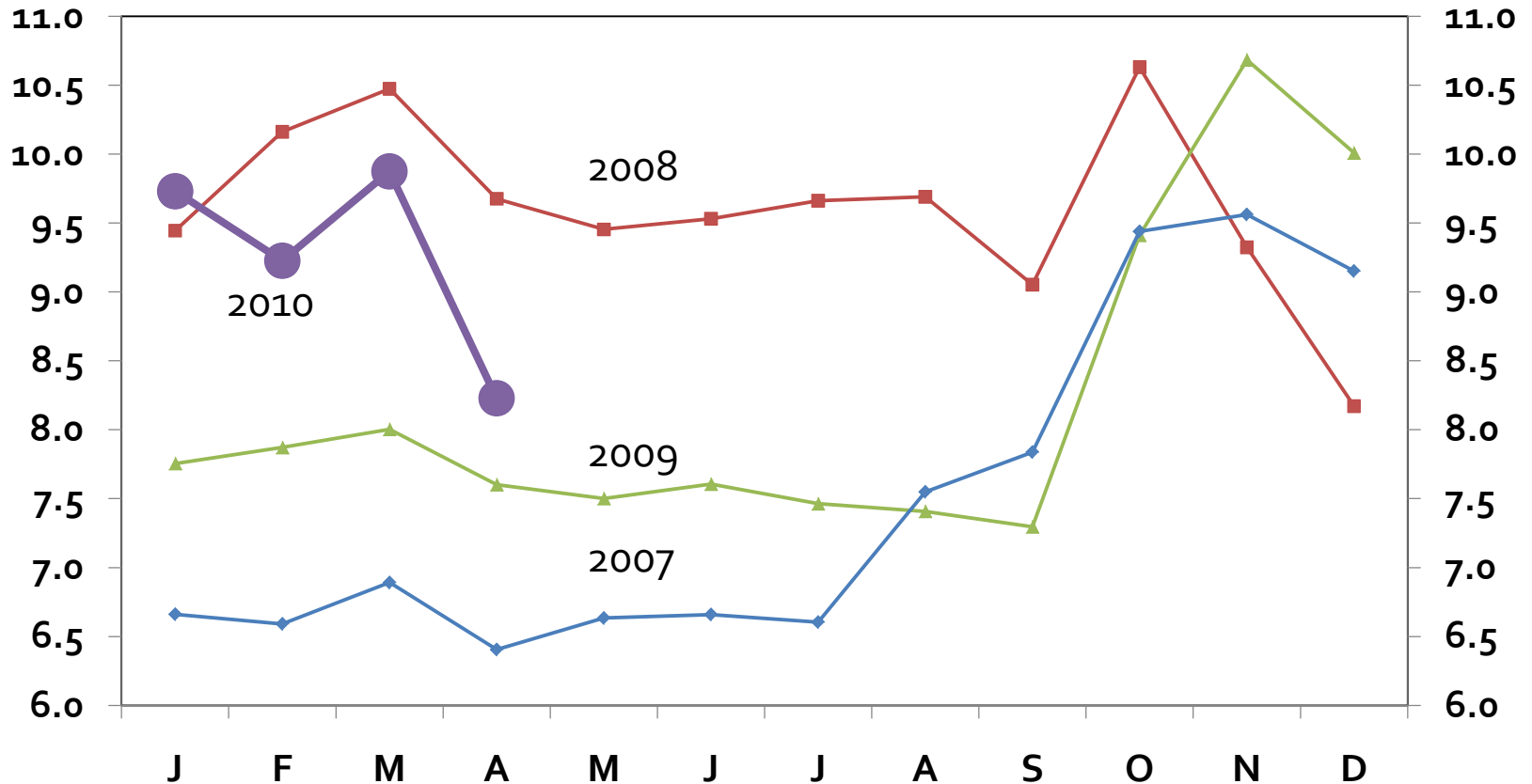
Source: IMF, April 2010



How sustainable is U.S. export activity?

U.S. Agricultural Exports

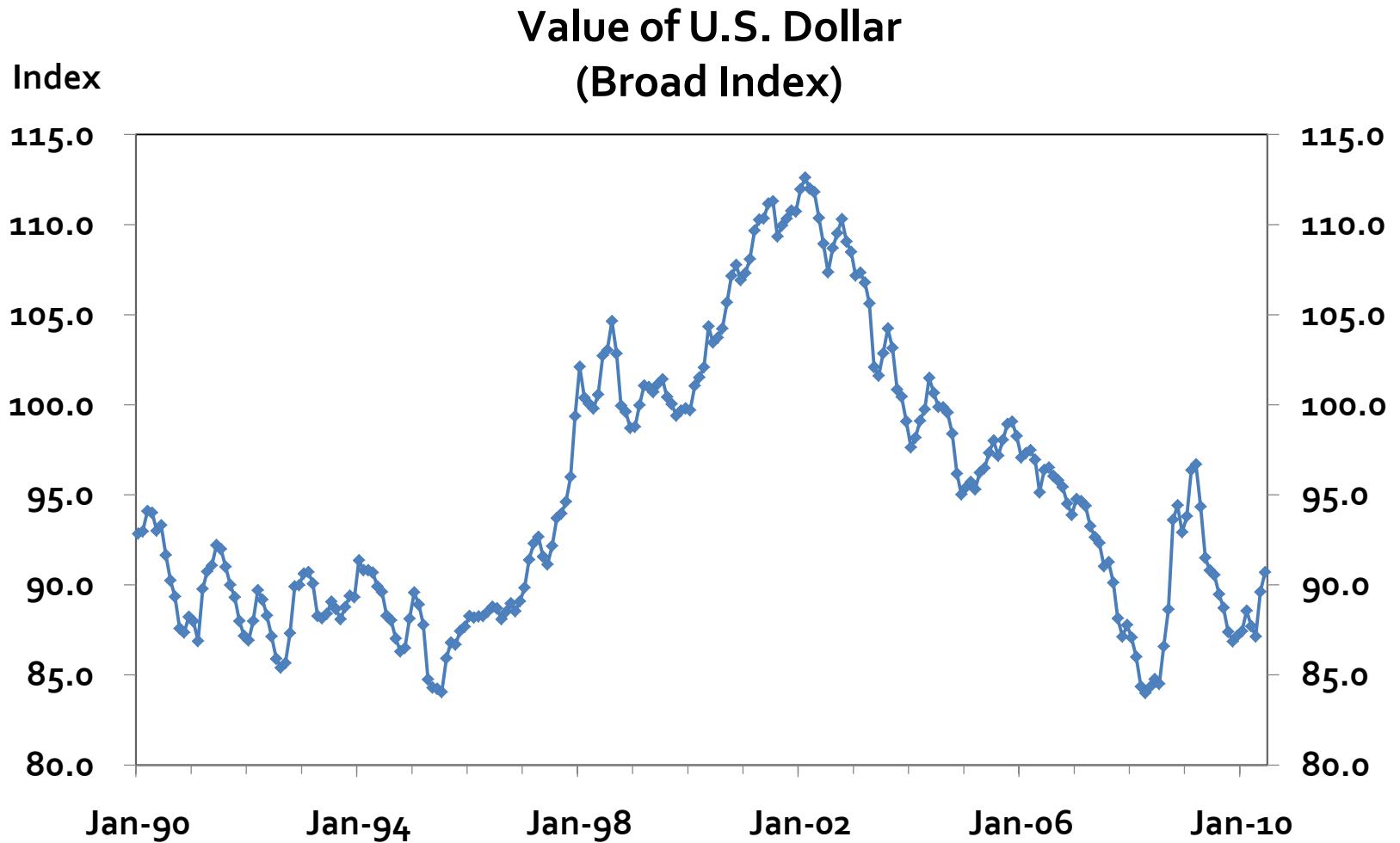
Billion dollars



Source: USDA



How is U.S. export activity?



Source: Federal Reserve Board of Governors



Implications for Agriculture

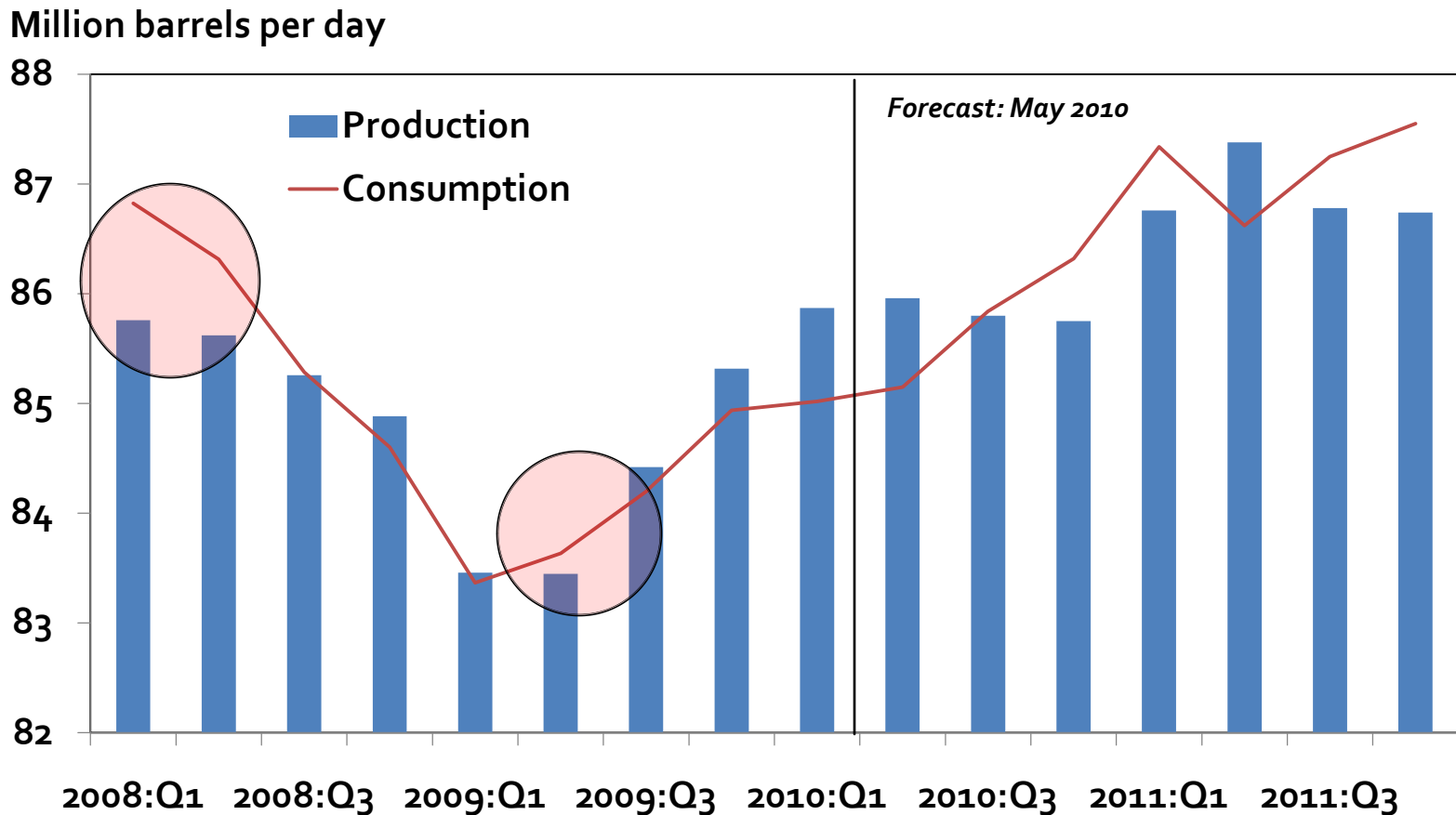


- Financial markets
- U.S. consumer demand
- Export activity
- Energy markets



What will happen to crude oil prices if consumption outpaces production?

World Crude Oil Supply Balance

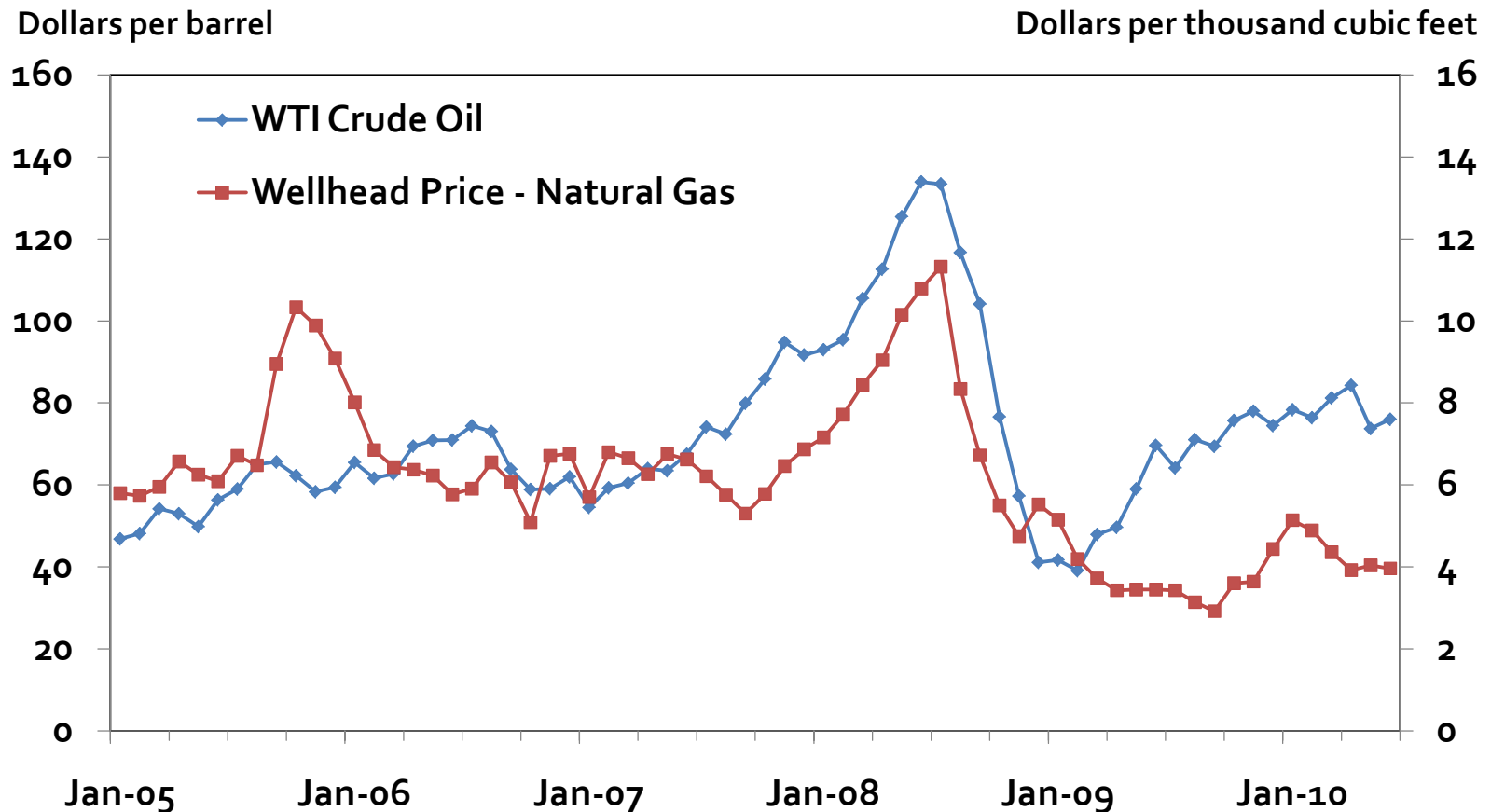


Source: Energy Information Administration



Energy markets: A boon or bane for agriculture?

Crude Oil and Natural Gas Prices



Source: Energy Information Administration



Implications for Agriculture

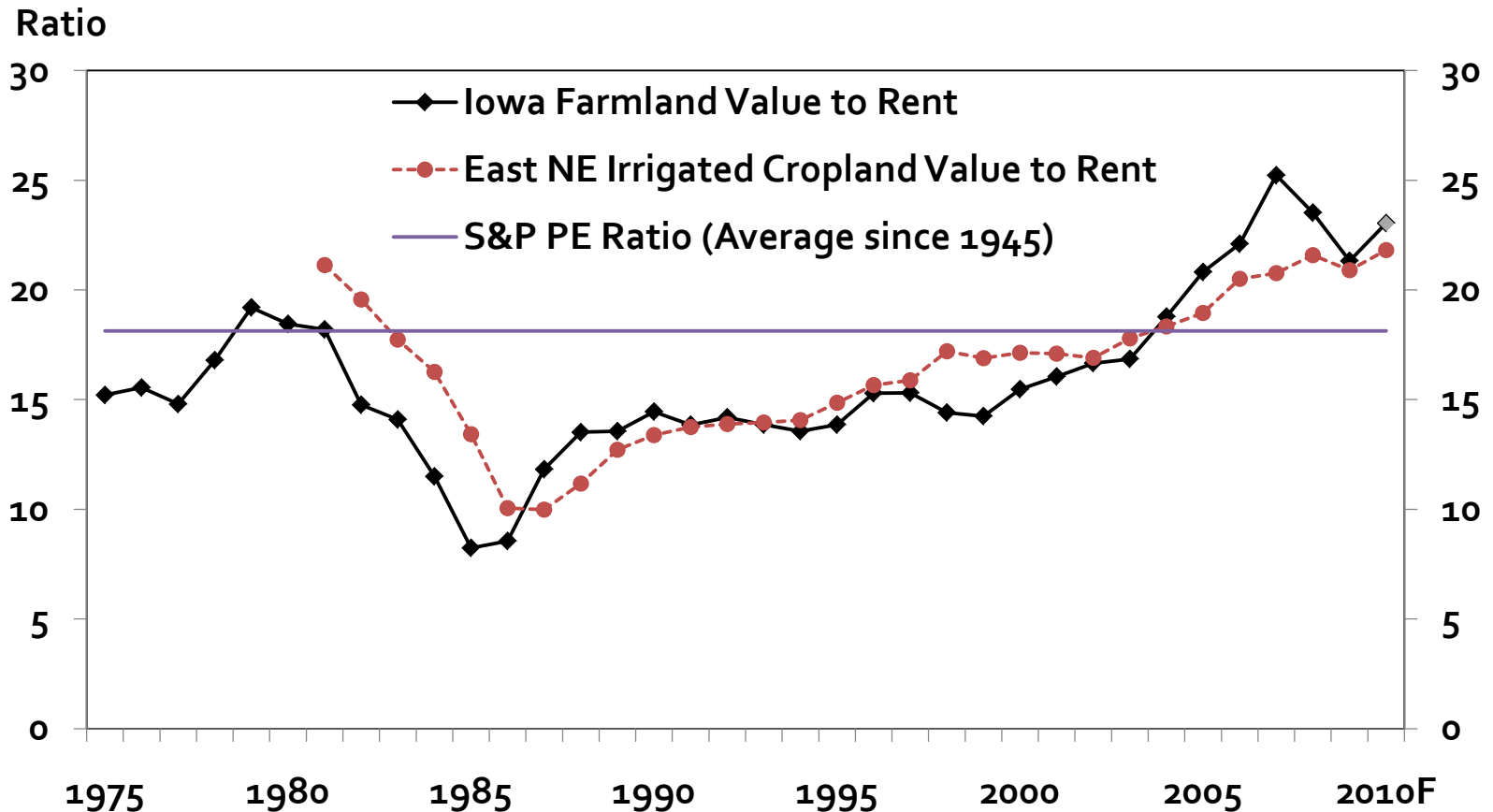


- Financial markets
- U.S. consumer demand
- Export activity
- Energy markets
- Farmland values



Is a farmland bubble brewing?

Farmland Values to Rent Ratio

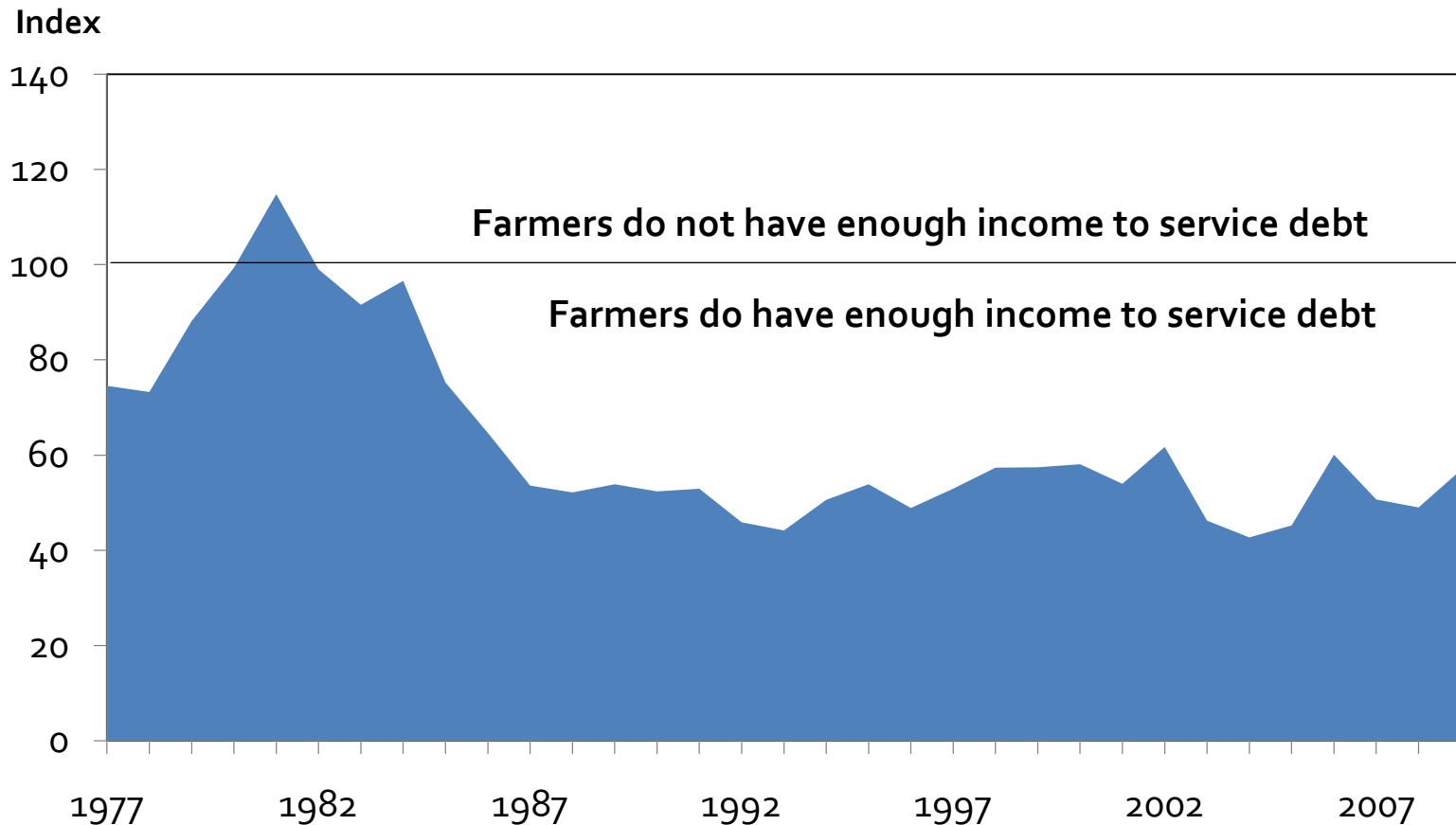


Calculations based on Iowa State University and University of Nebraska data



To identify a bubble, follow the debt.

U.S. Debt Repayment Capacity Utilization



Source: USDA



Implications for Agriculture

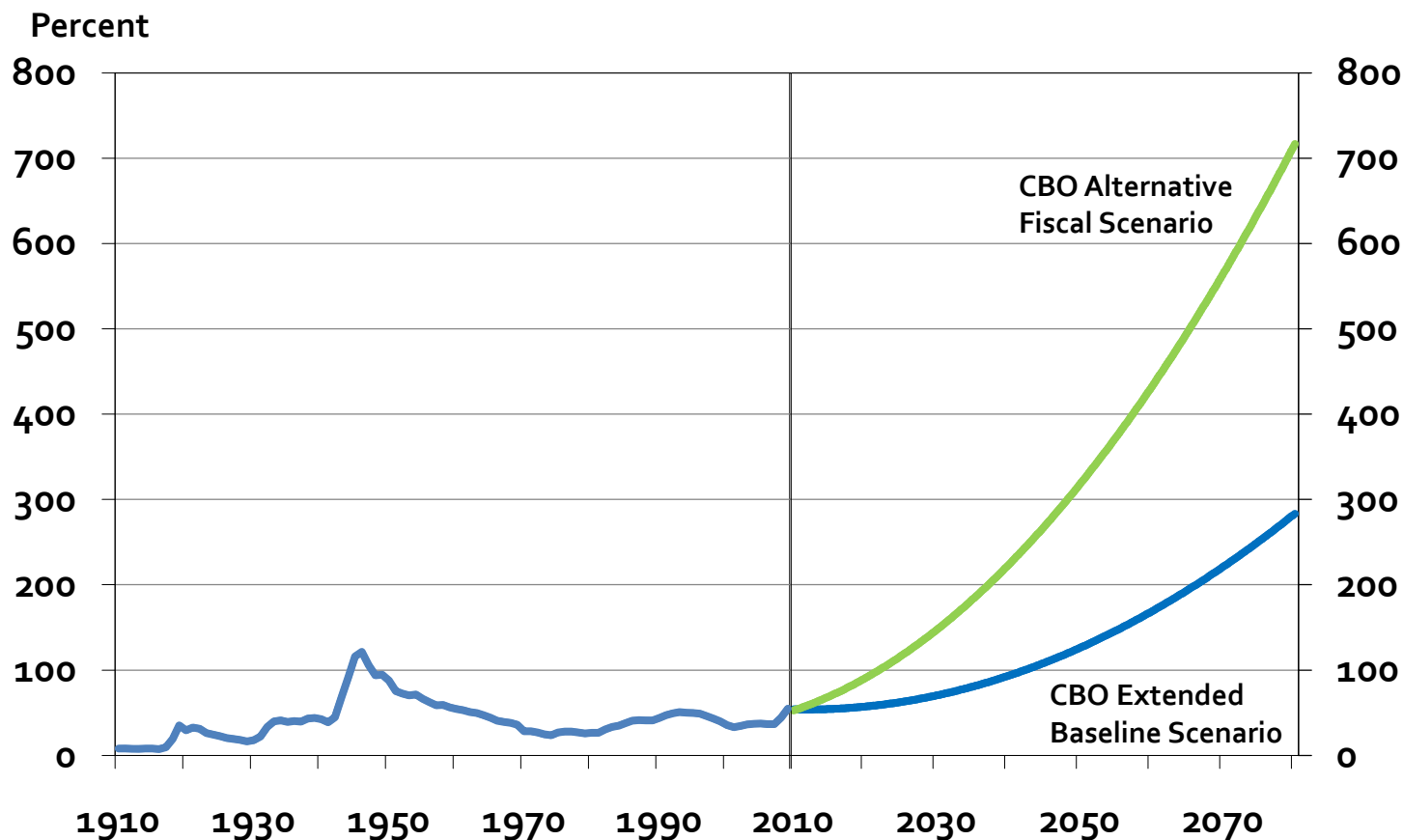


- Financial markets
- U.S. consumer demand
- Export activity
- Energy markets
- Farmland values
- Government policy



How will surging federal debt levels affect farm policy?

U.S. Debt as a Percent of GDP



Source: Congressional Budget Office, November 2009



Conclusions

- **The economic recovery is underway.**
 - Stronger consumer demand is boosting business activity.
 - But, deleveraging will limit the recovery.
- **Questions will switch from growth to inflation.**
 - Will high unemployment limit inflation?
 - What will start the “chasing”?
- **The recovery brings opportunities and risks to the farm sector.**

