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Major Trends Driving Major Changes in Rural America



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.

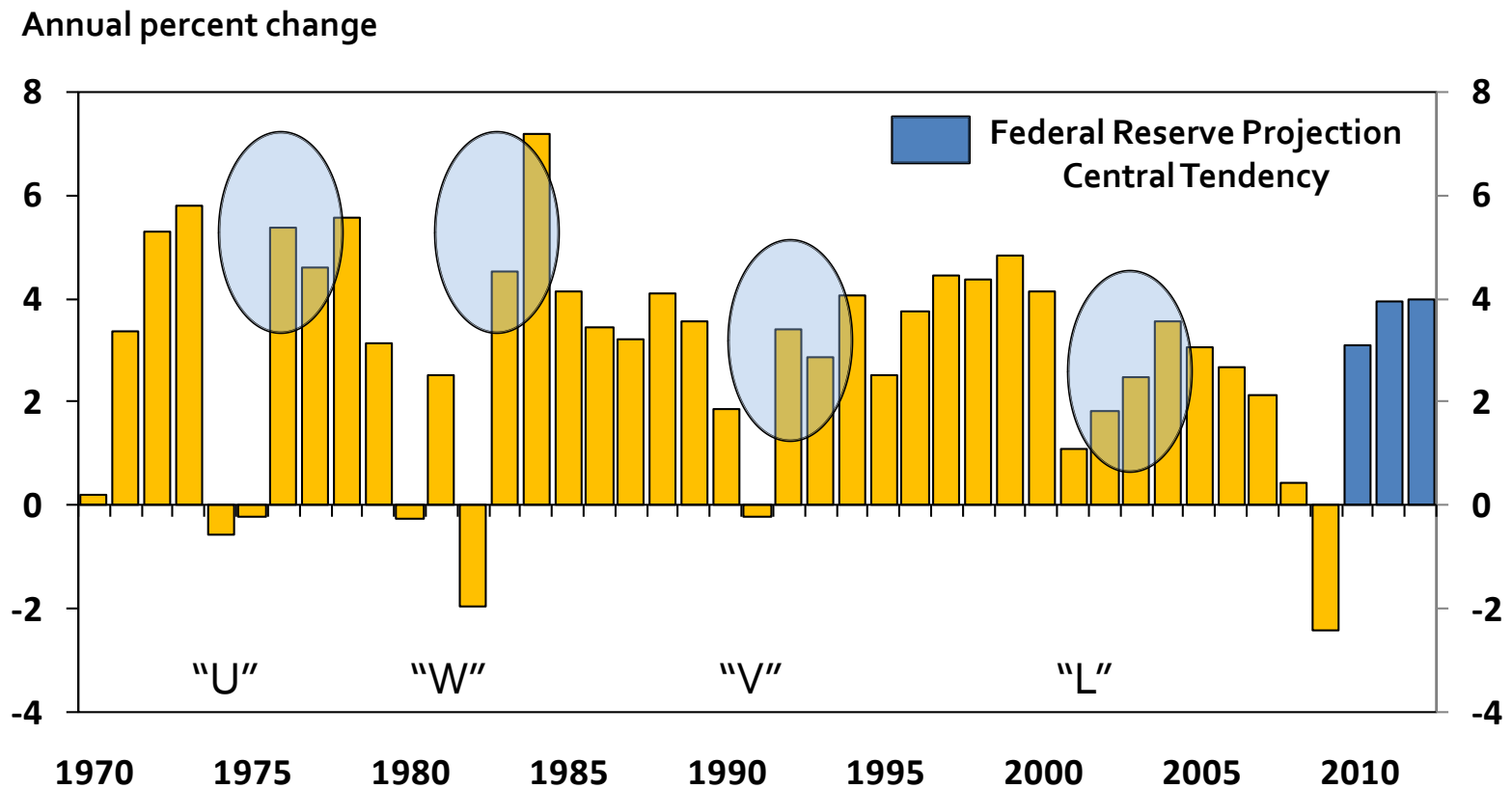
Today's Roadmap

- The economic recovery is the major trend.
- Five trends for rural America
- Can Rural America compete in the recovery?



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

Real GDP Growth

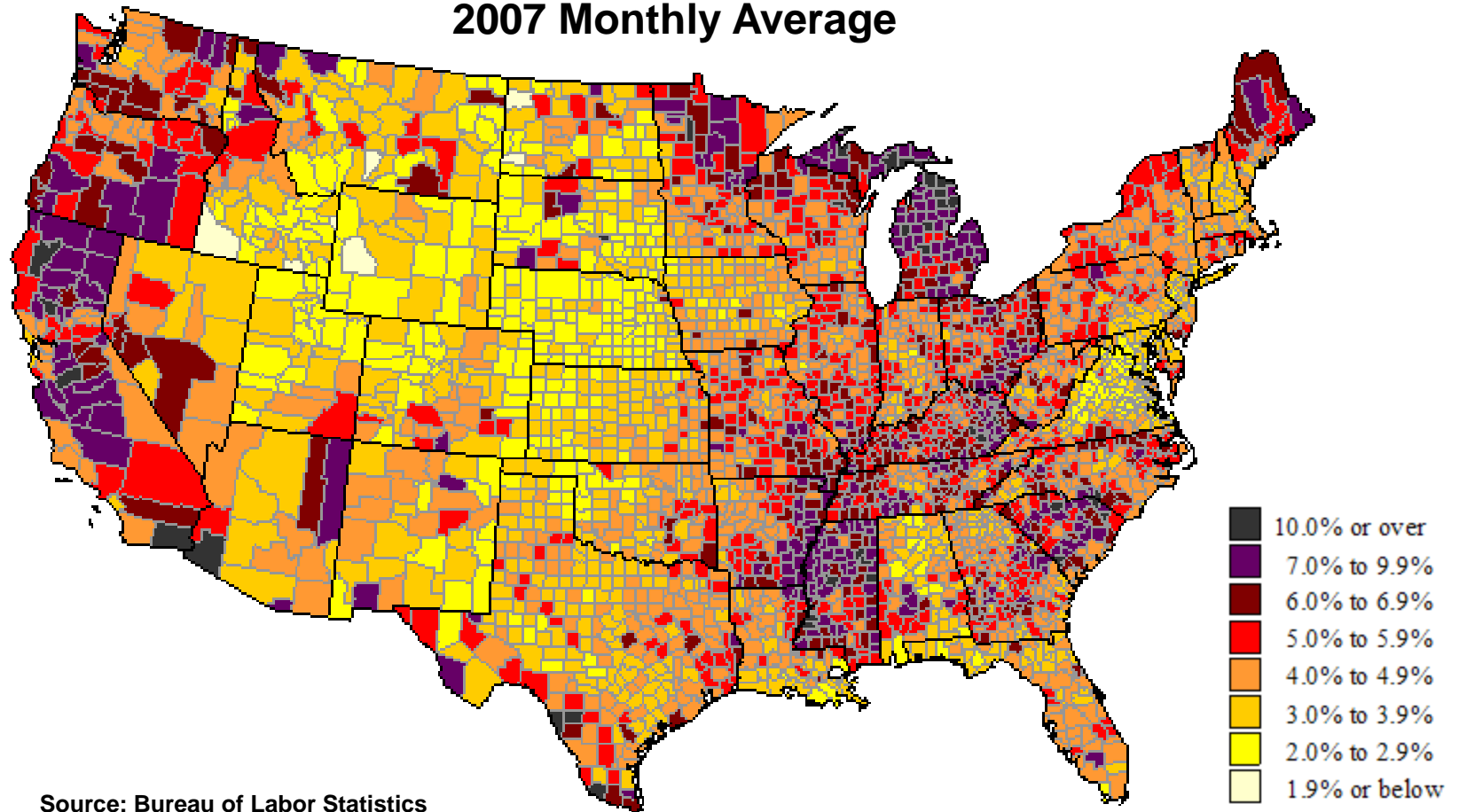


Source: Bureau of Economic Analysis Federal Reserve Board of Governors



Unemployment rates have spiked.

Unemployment Rate 2007 Monthly Average

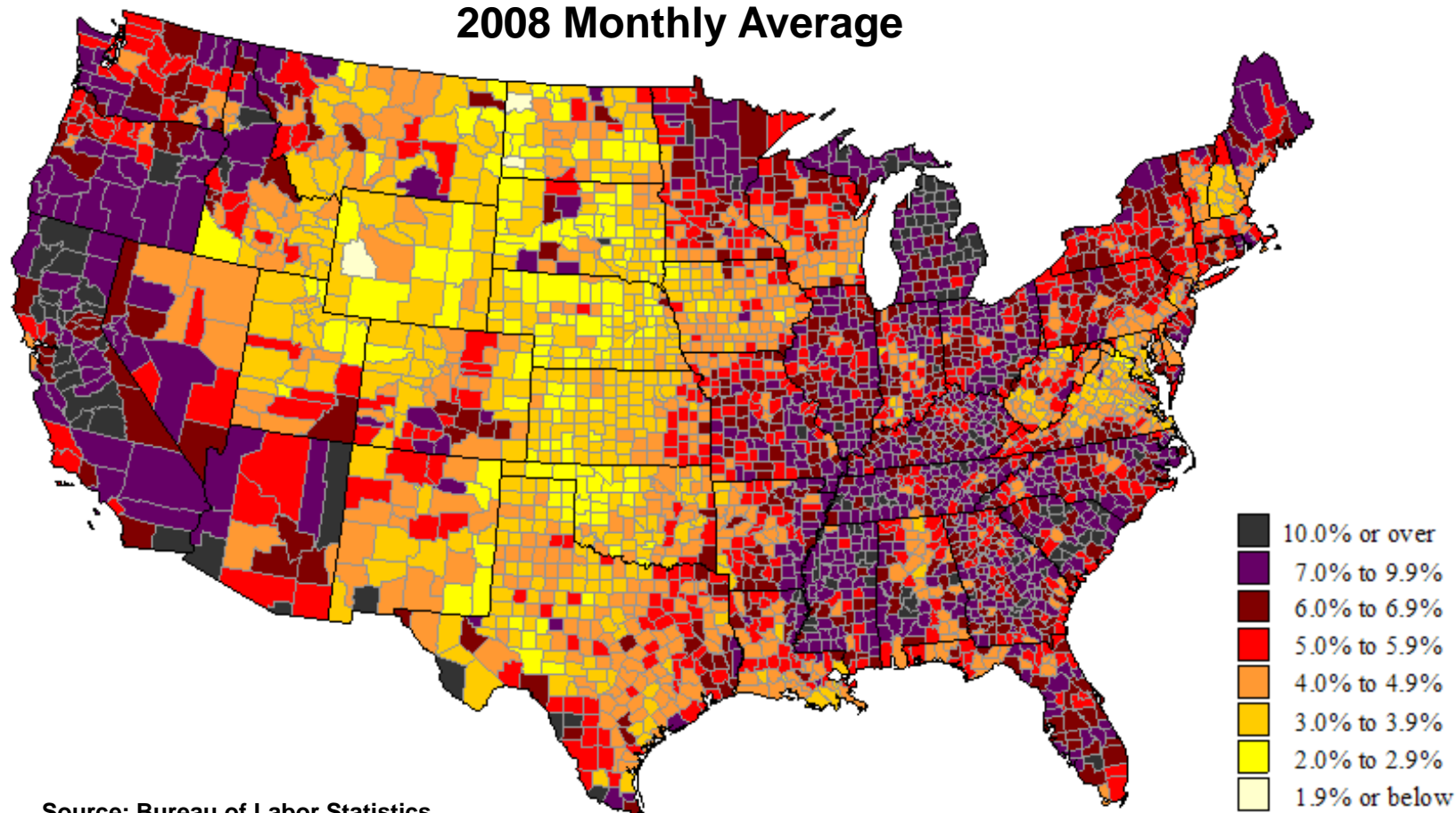


Source: Bureau of Labor Statistics



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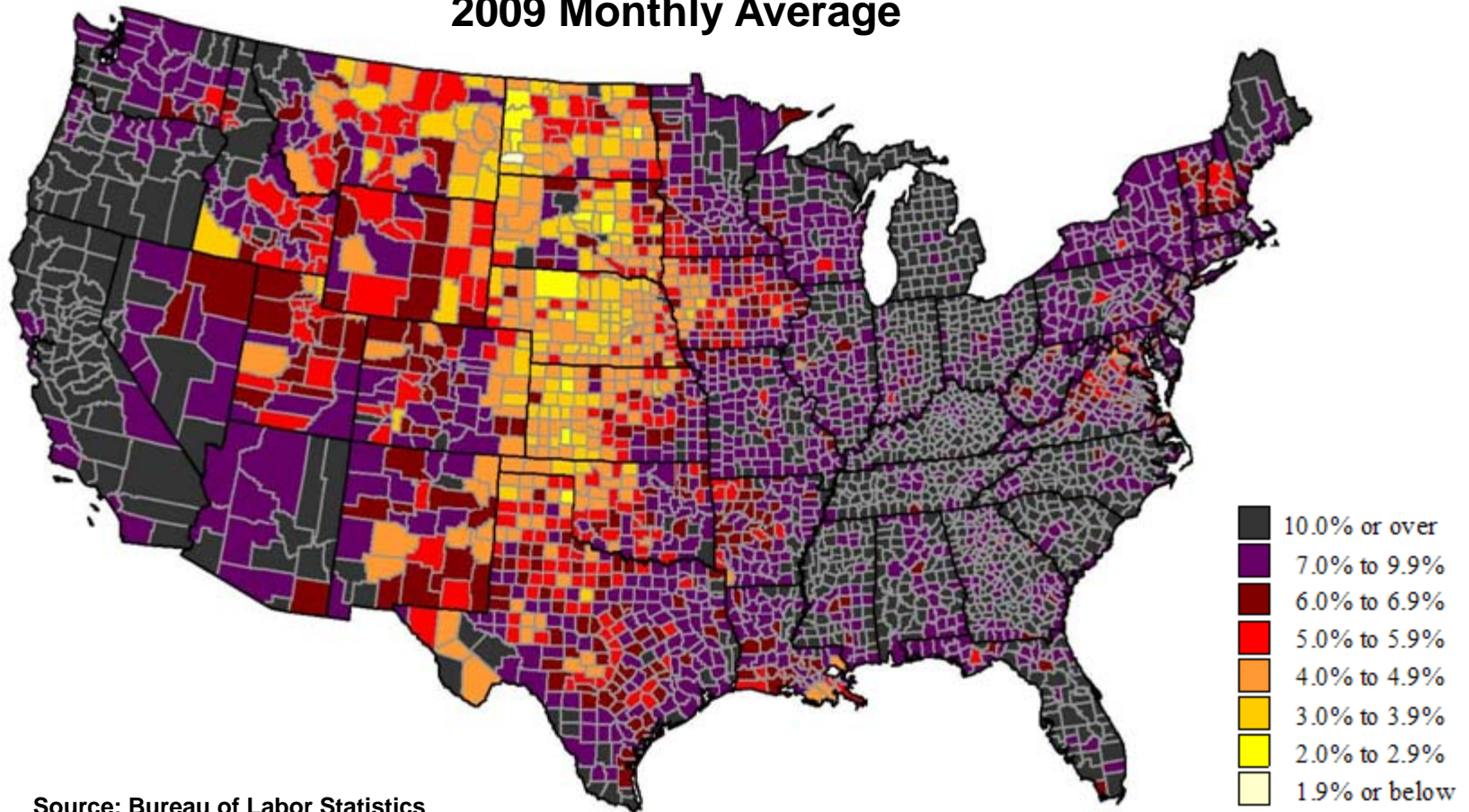


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Unemployment rates have spiked.

Unemployment Rate 2009 Monthly Average



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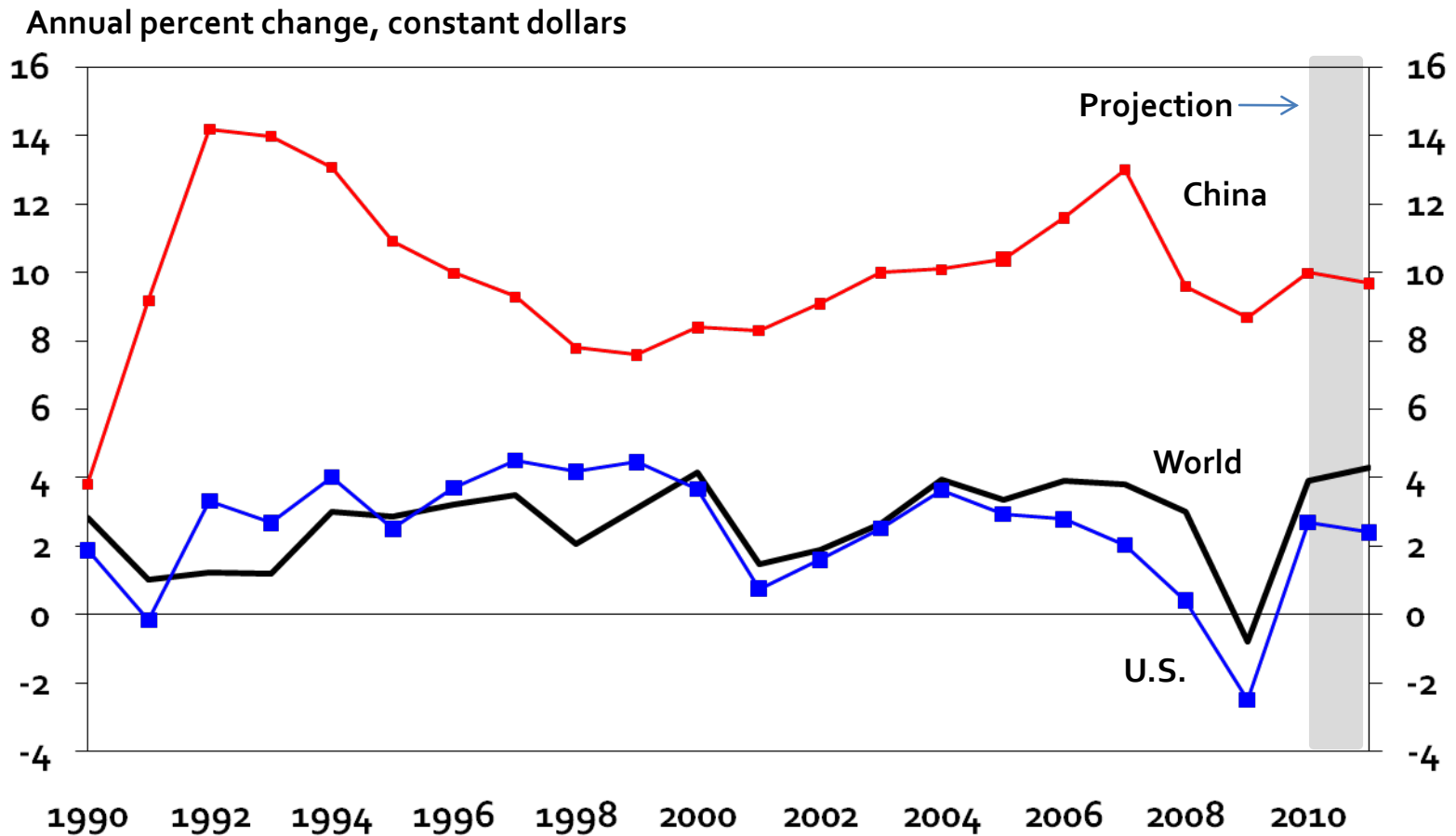
The Fundamental Question

*Is the “Great Recession”
the “Great Depression”
for our generation?*



Where are tomorrow's consumers?

GDP Growth

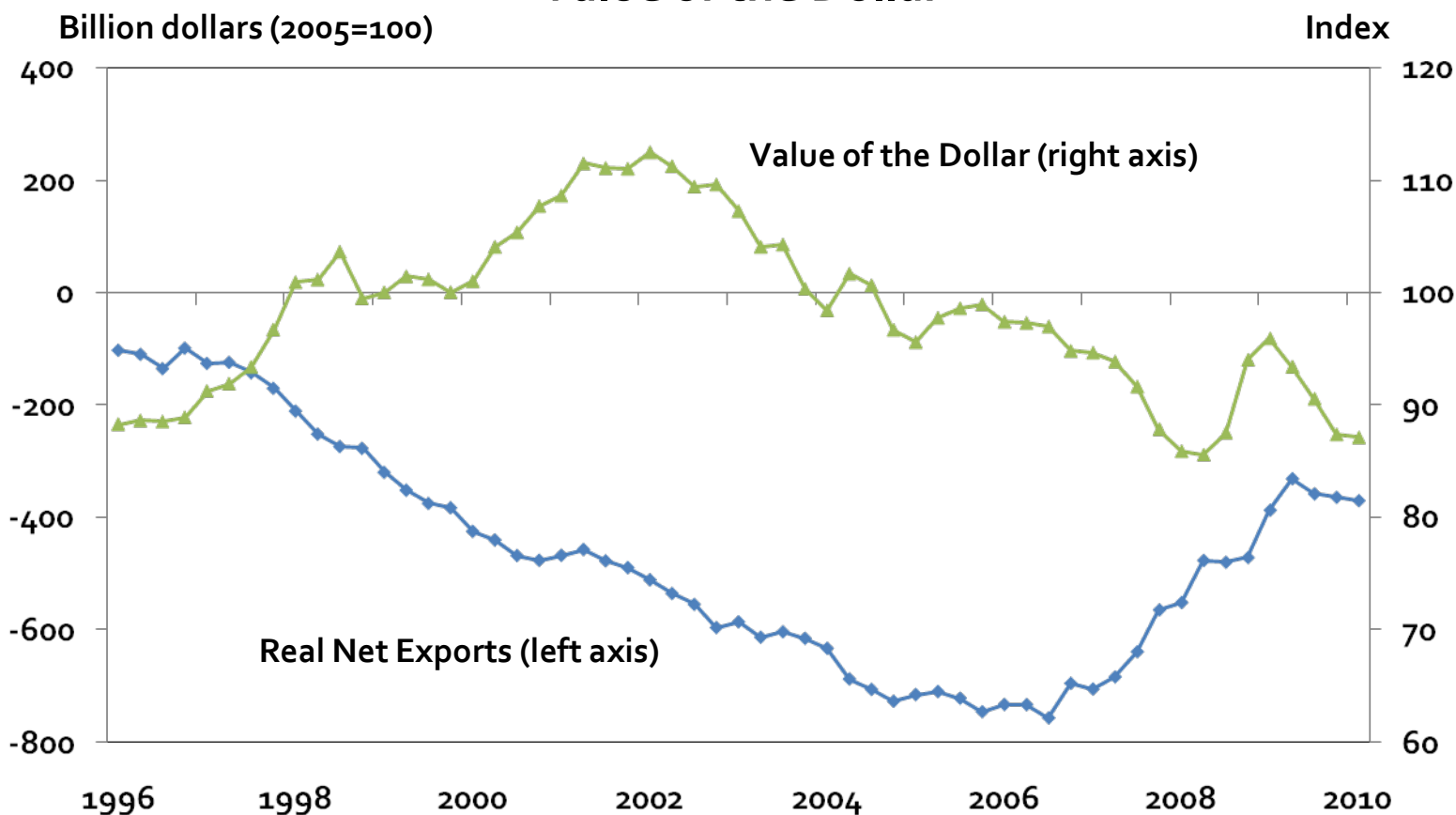


Source: International Monetary Fund, January 2010



Can stronger global economies and a weaker dollar spur further improvements in the trade balance?

Real Net Exports of Goods and Services Value of the Dollar

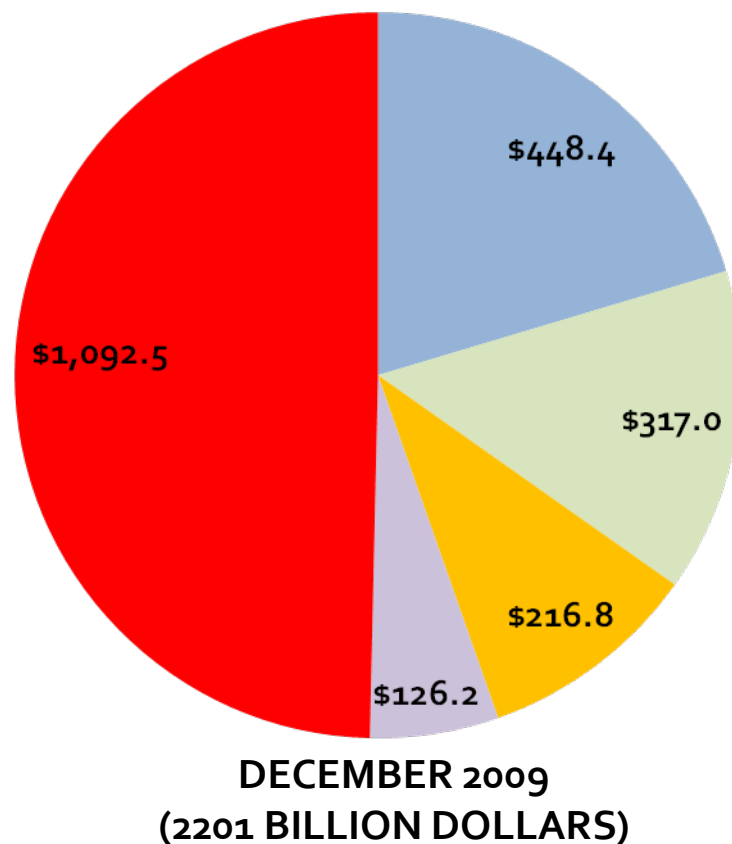
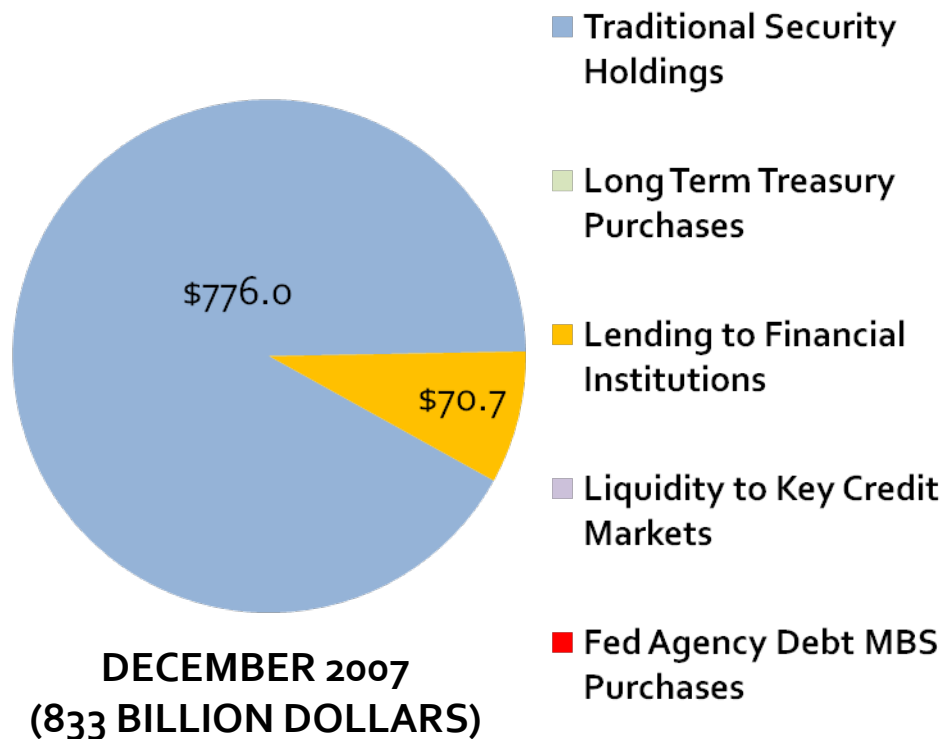


Source: Bureau of Economic Analysis



In the future, the Federal Reserve will need to shrink its balance sheet

Federal Reserve Balance Sheet: Assets



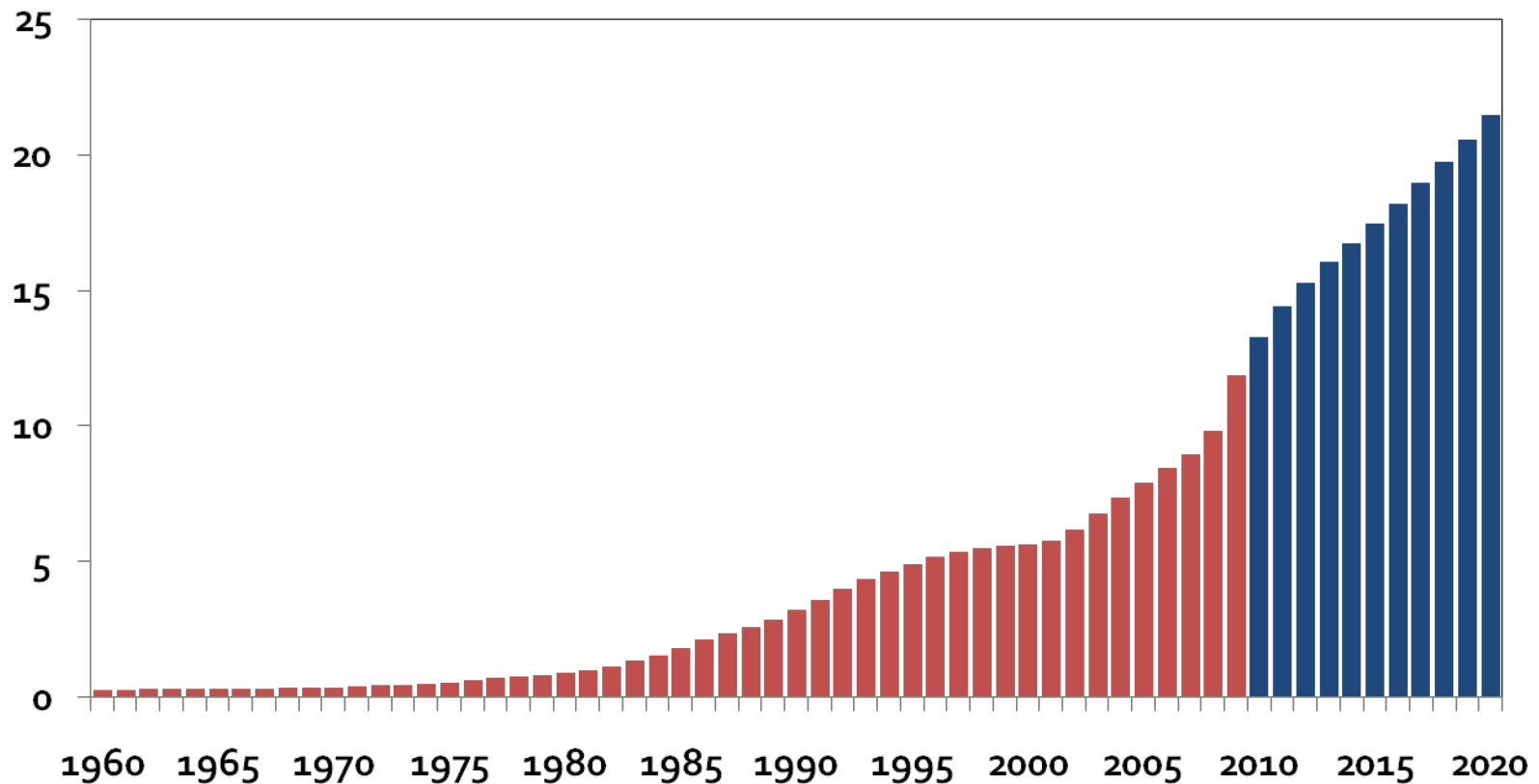
Source: Federal Reserve Bank of Cleveland



In the short run, deficit spending stimulates the economy. What about the long-term consequences?

U.S. Gross Federal Debt

Trillion Dollars

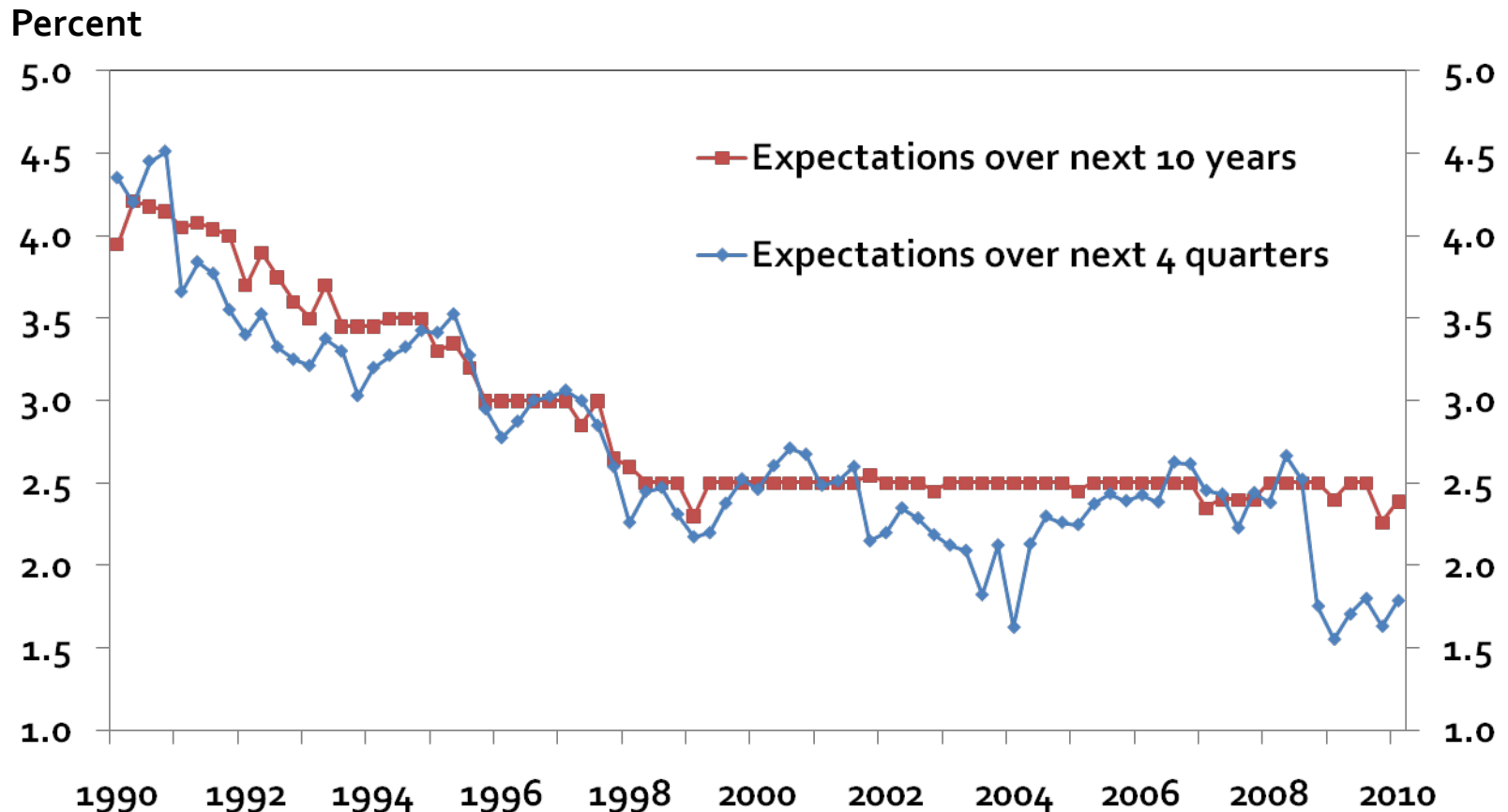


Source: Congressional Budget Office



Inflation expectations remain low.

U.S. Inflation Expectations



Source: Survey of Professional Forecasters



Today's Roadmap

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- Five trends for rural America



1) Money may NOT be Cheap

- Due to the zero bound, the Fed Funds rate can only go up.
- Interest rate risk for banks and businesses.
- Do not forget about credit standards and collateral requirements.



2) *The Consumer is King*

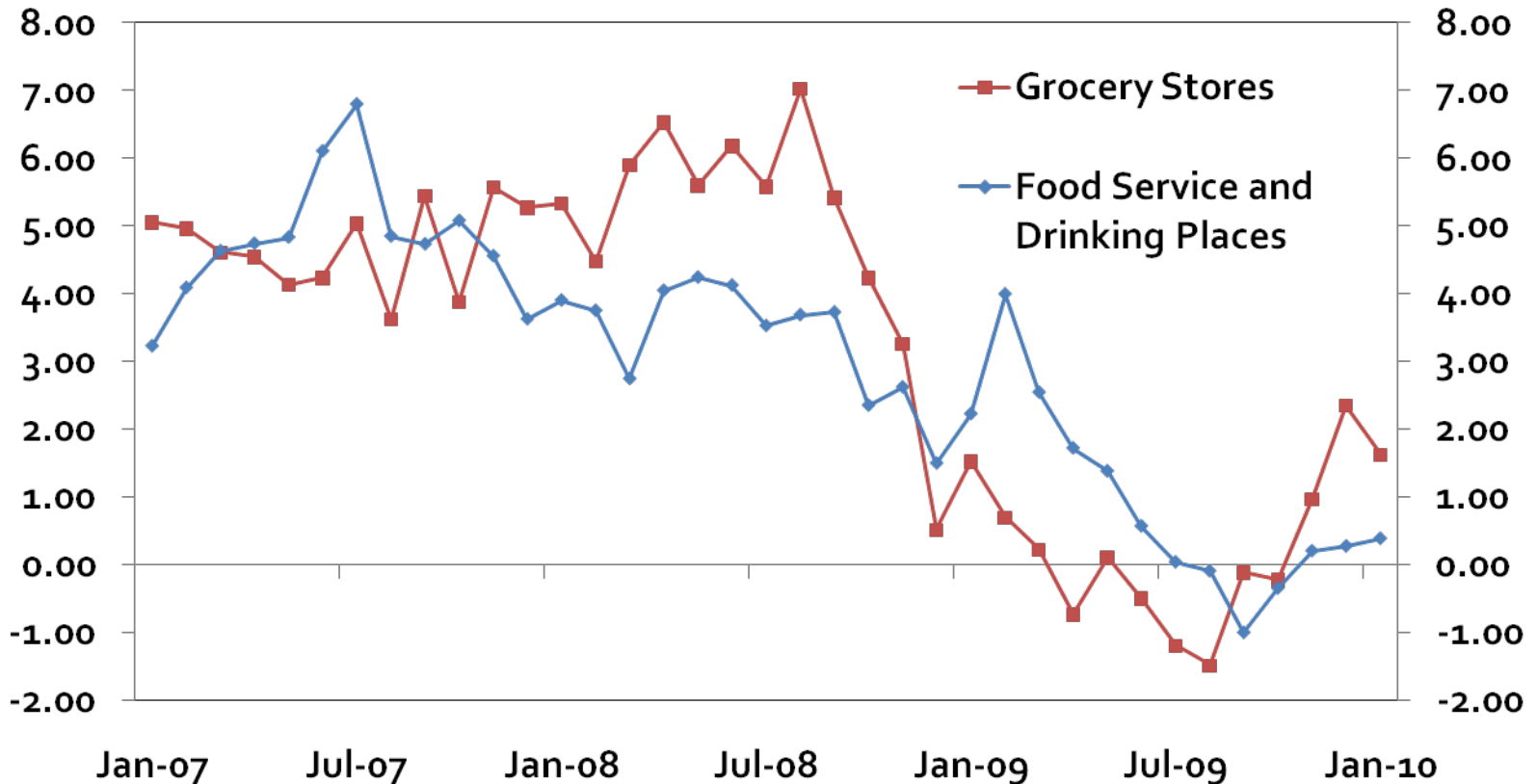
- The “Great Recession” was caused by a collapse in demand.
- When will domestic demand rebound?
- Who are tomorrow’s consumers?



Rural America is in the Food Business.

U.S. Retail Sales at Grocery Stores and Restaurants

Percent change from year ago



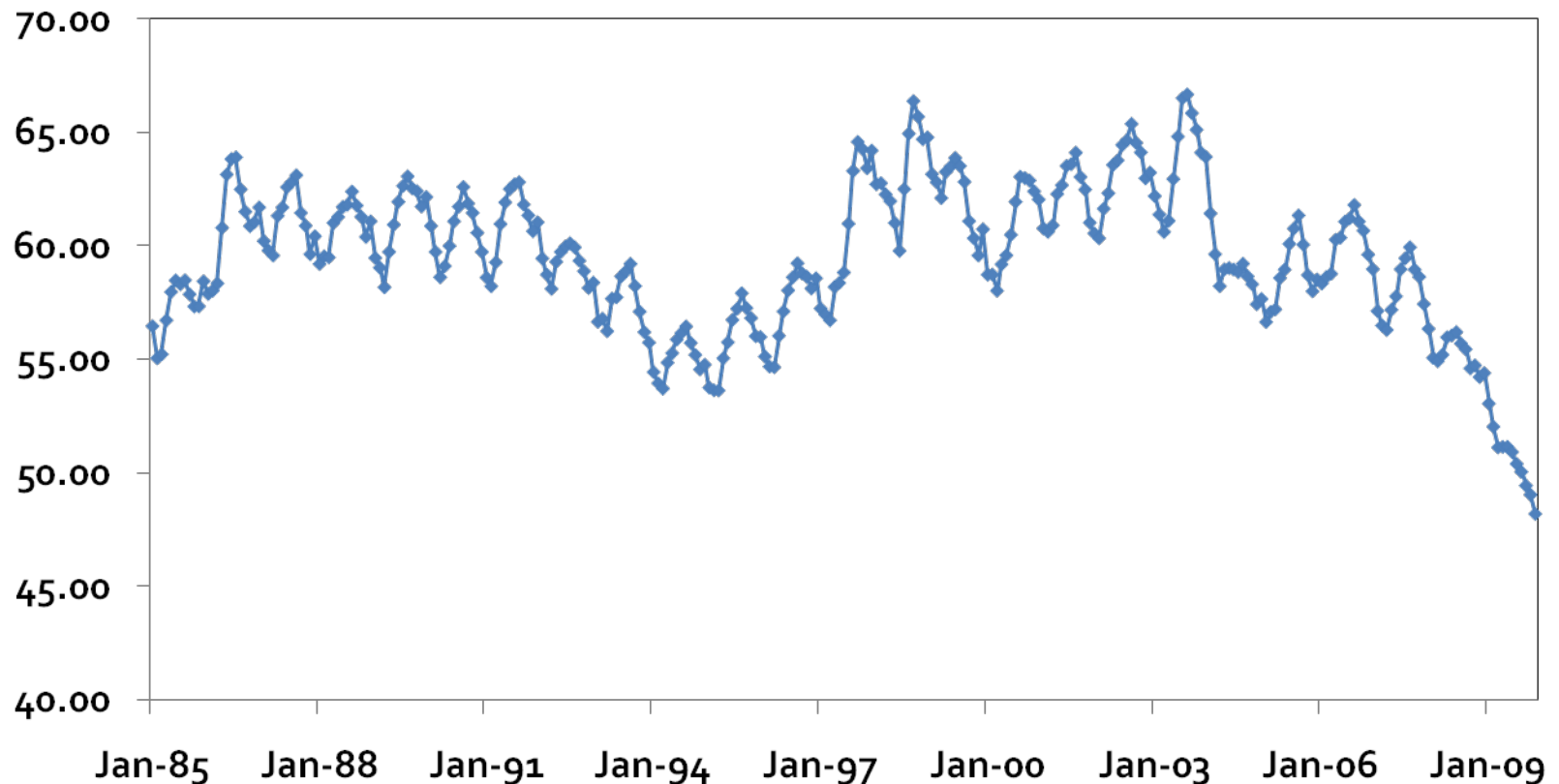
Source: Census Bureau



Gasoline demand has also plummeted.

Total Gasoline Retail Deliveries

Million gallons per day (three month moving average)

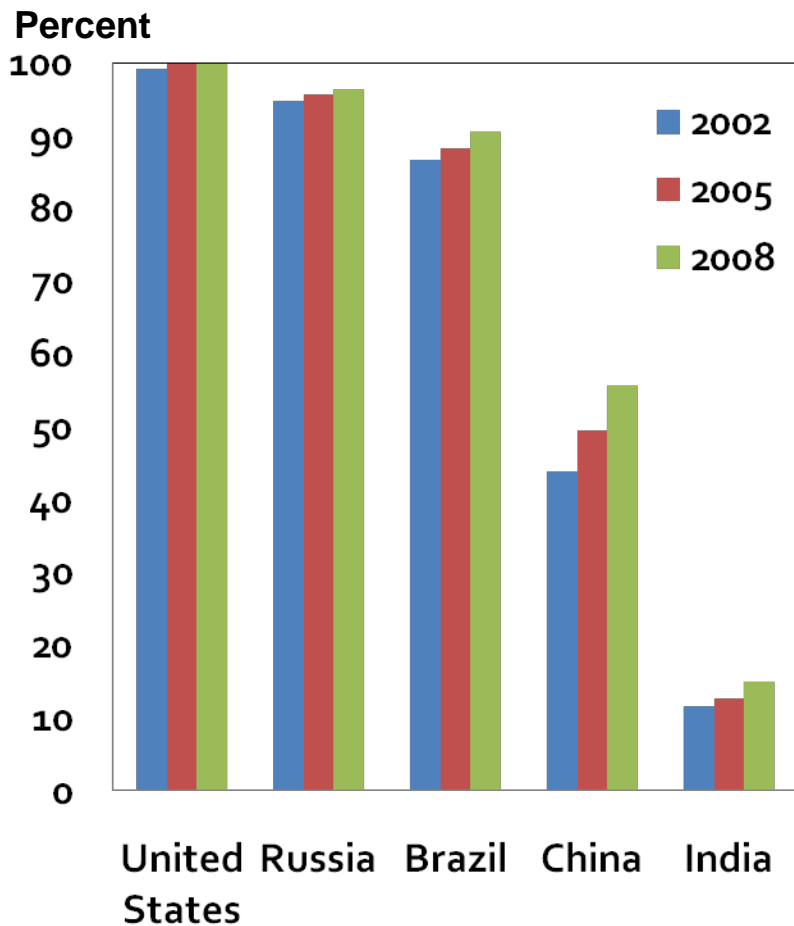


Source: Energy Information Administration

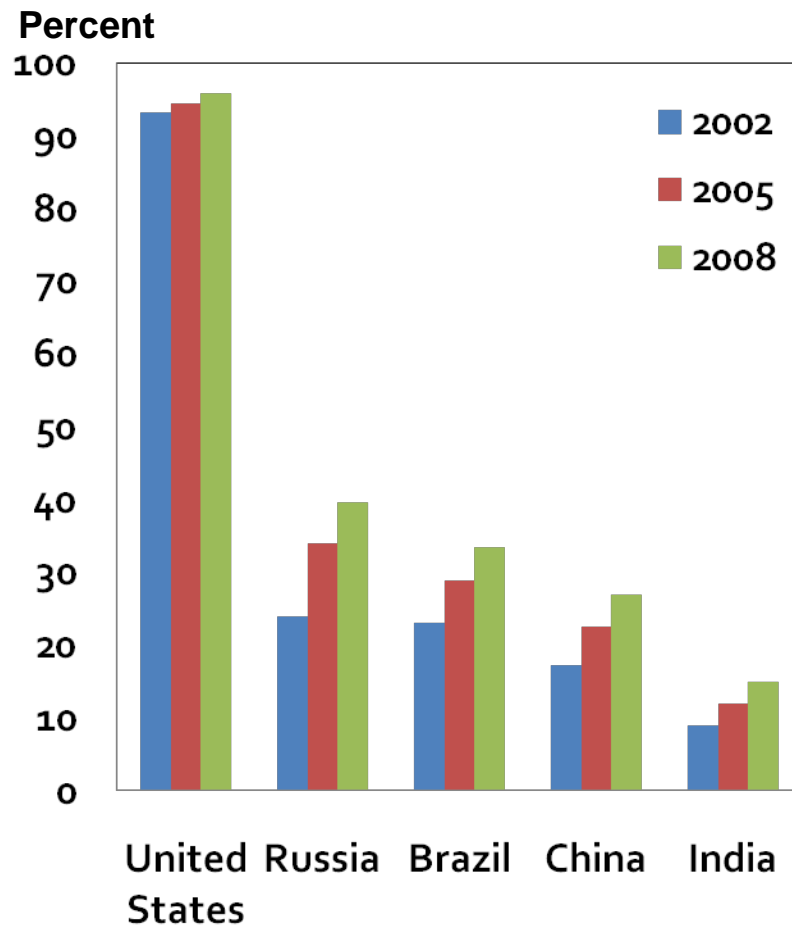


As incomes rise, how people purchase and prepare food changes.

Households Owning a Refrigerator



Households Owning a Microwave Oven



Source: USDA, Euromonitor



3) U.S. Ag: High Hopes, Uncertain Profits

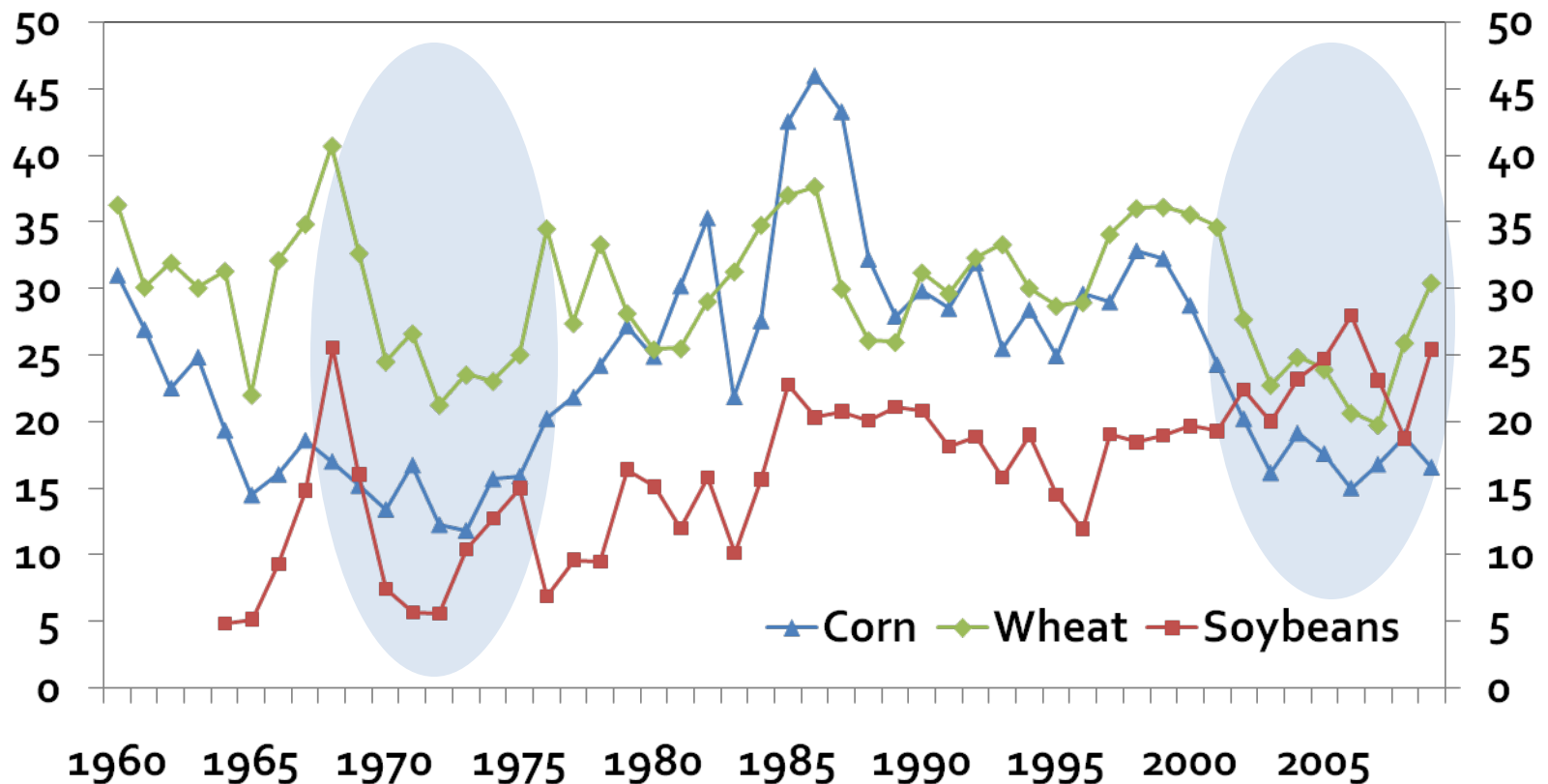
- If we can get \$4 corn with weak demand, what happens when demand rebounds?



Crop inventories remain low.

World Crop Inventories

Ending stocks to use ratio (percent)



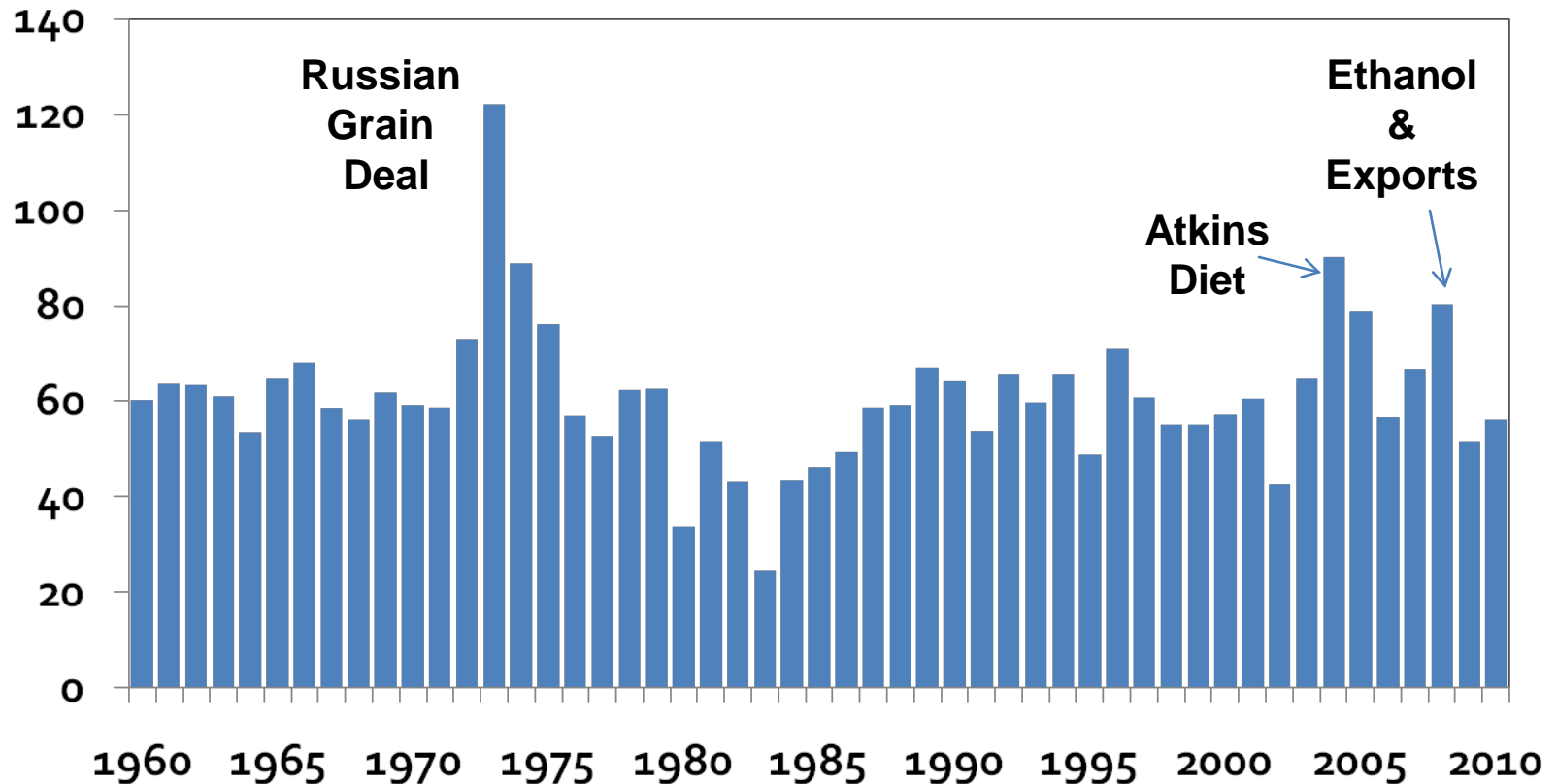
Source: USDA



Traditionally, farm booms are driven by demand.

Real U.S. Net Farm Income

Billion dollars



Source: USDA

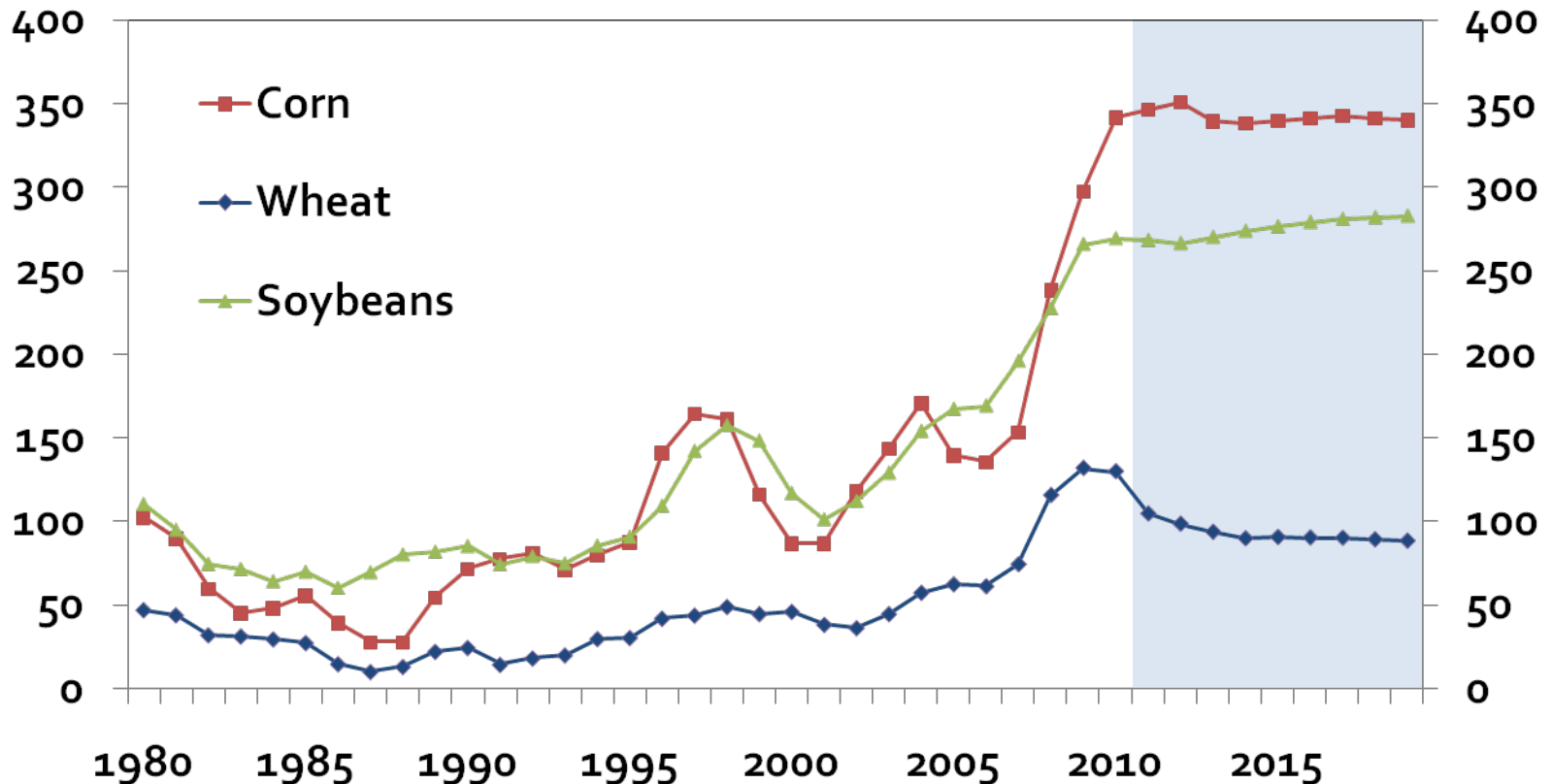


A decade of high crop profits?

Net Returns to Crop Production

(Gross Market Returns Less Variable or Cash Costs)

Dollars per acre (three year moving average)



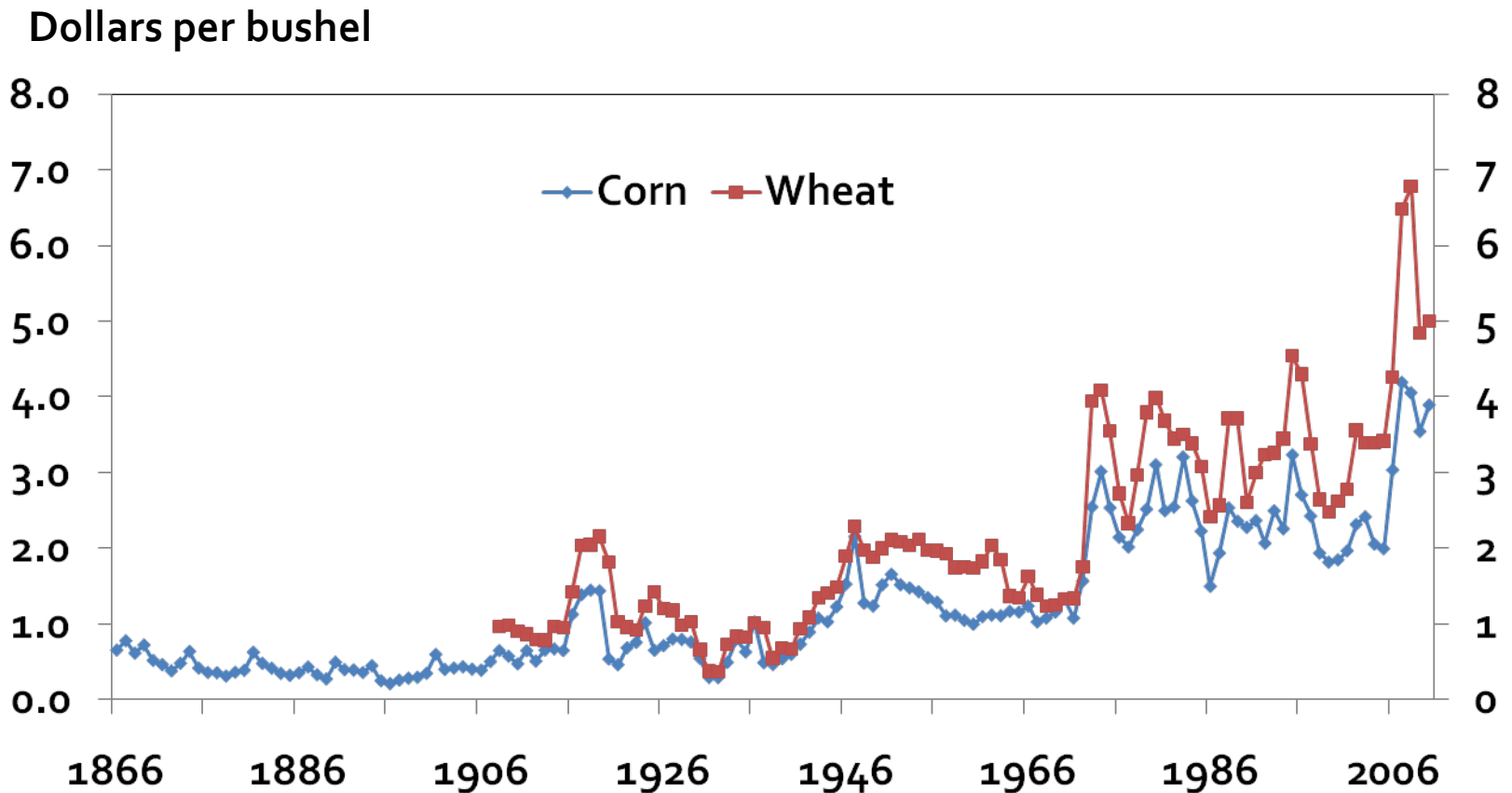
Source: USDA

Variable costs exclude costs for labor and management, depreciation, land, taxes, insurance, and farm overhead.



Volatility in commodity prices remains high.

U.S. Annual Farm Prices



Source: USDA



3) U.S. Ag: High Hopes, Uncertain Profits

- If we can get \$4 corn with weak demand, what happens when demand rebounds?
- \$4 corn presents a challenge to U.S. livestock.



4) *Changing Government Policies*

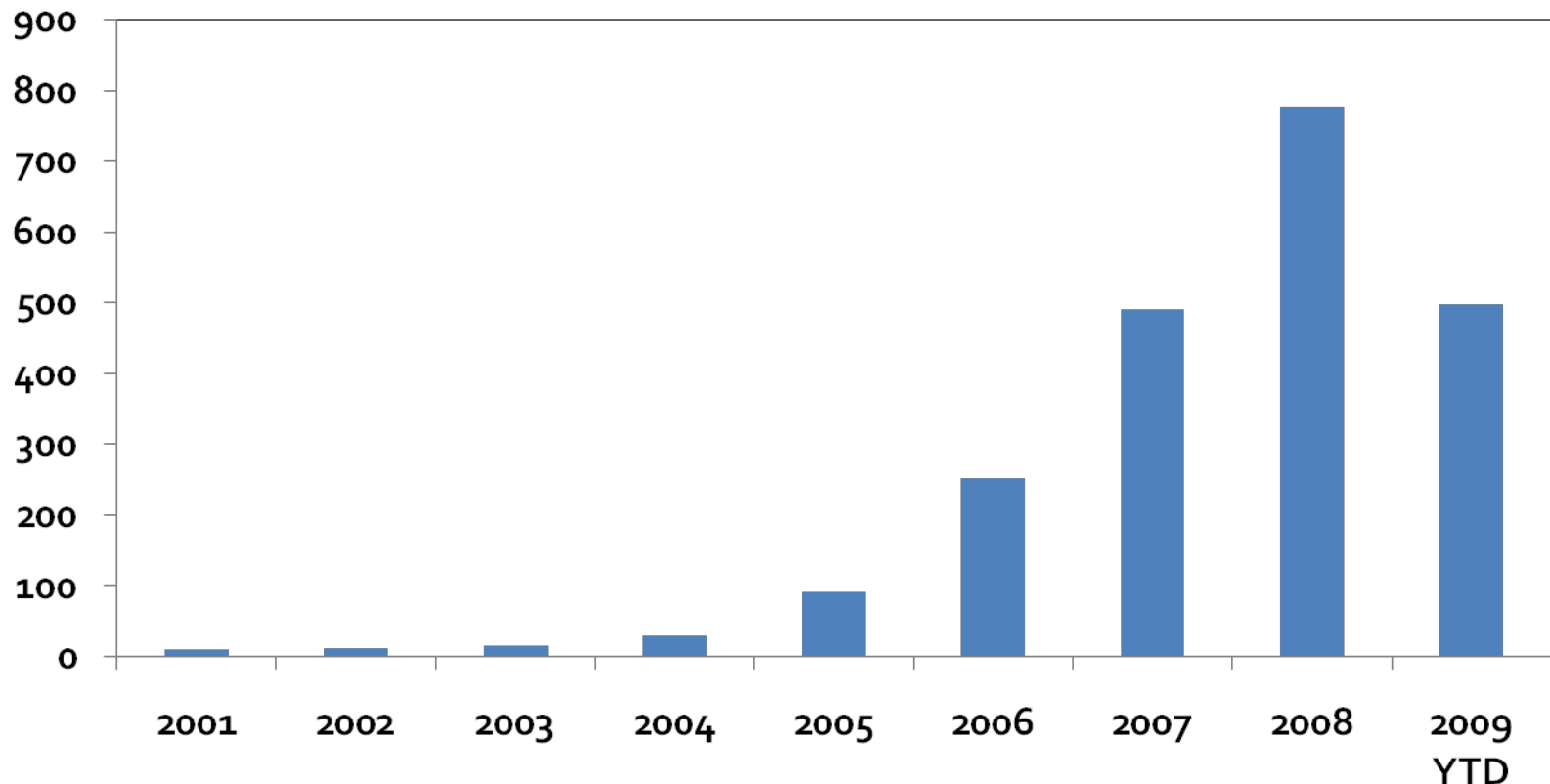
- Financial markets and regulation
- Environmental policy
- Energy policy
- Health care policy
- Agricultural policy
- Rural development
- ???



What happened to biodiesel production in Jan. 2010? Do you want to base your profits on government policy?

U.S. Biodiesel Production

Million gallons



Source: Dept. of Energy



5) Another Wave of Consolidation.

- Potential consolidation in banking, agriculture, and rural communities.
- Shaped by the following ...
 - Business and bank failures open opportunities for survivors.
 - Higher fixed costs of production.
 - Regulatory costs also boost fixed costs.
 - With tighter standards, equity/collateral needs rise.
- Economies of scale and scope will tend to dominate in rural America.



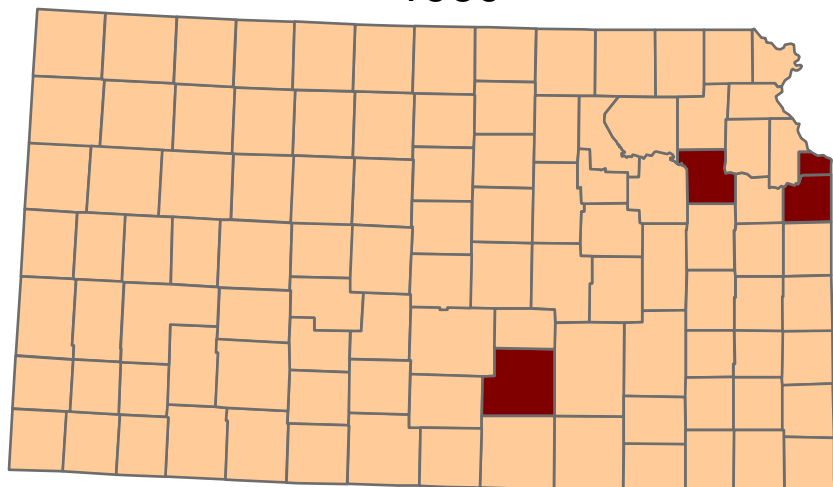
Don't be surprised if Rural America Can Compete.

- The strongest economic regions are formerly rural communities.

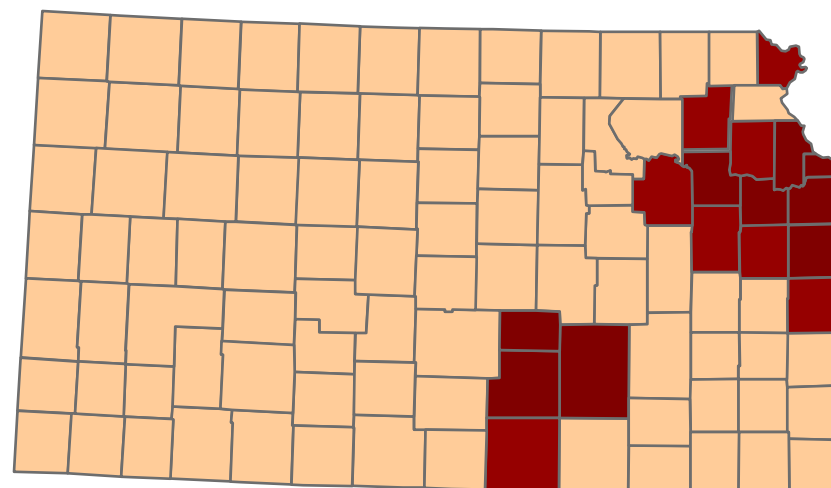
"If you can't beat them, annex them."

Kansas Metropolitan Counties

1960

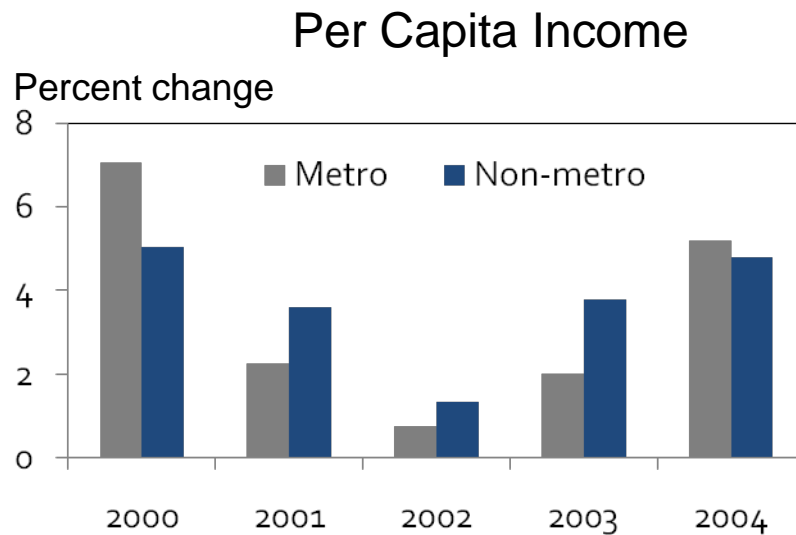
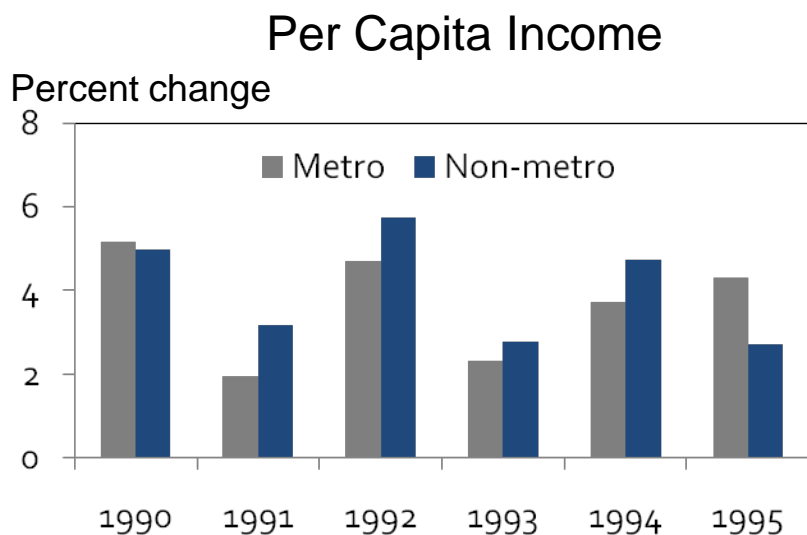


2006



Don't be surprised if Rural America Can Compete.

- The strongest economic regions are formerly rural communities.
- Rural places have had stronger growth in past “jobless recoveries”



Calculations based on BEA wage and salary employment and per capita income data.

Note: The 1990-91 recession ending in March 1991 and the 2001 recession ending in November 2001.



The Competitiveness of Rural Places

- Technology: Rural America adopts technology
 - 1850: 85 hours of labor needed to produce 100 bushels of corn.
 - 2000's: less than 2 hours of labor needed to produce 100 bushels of corn.

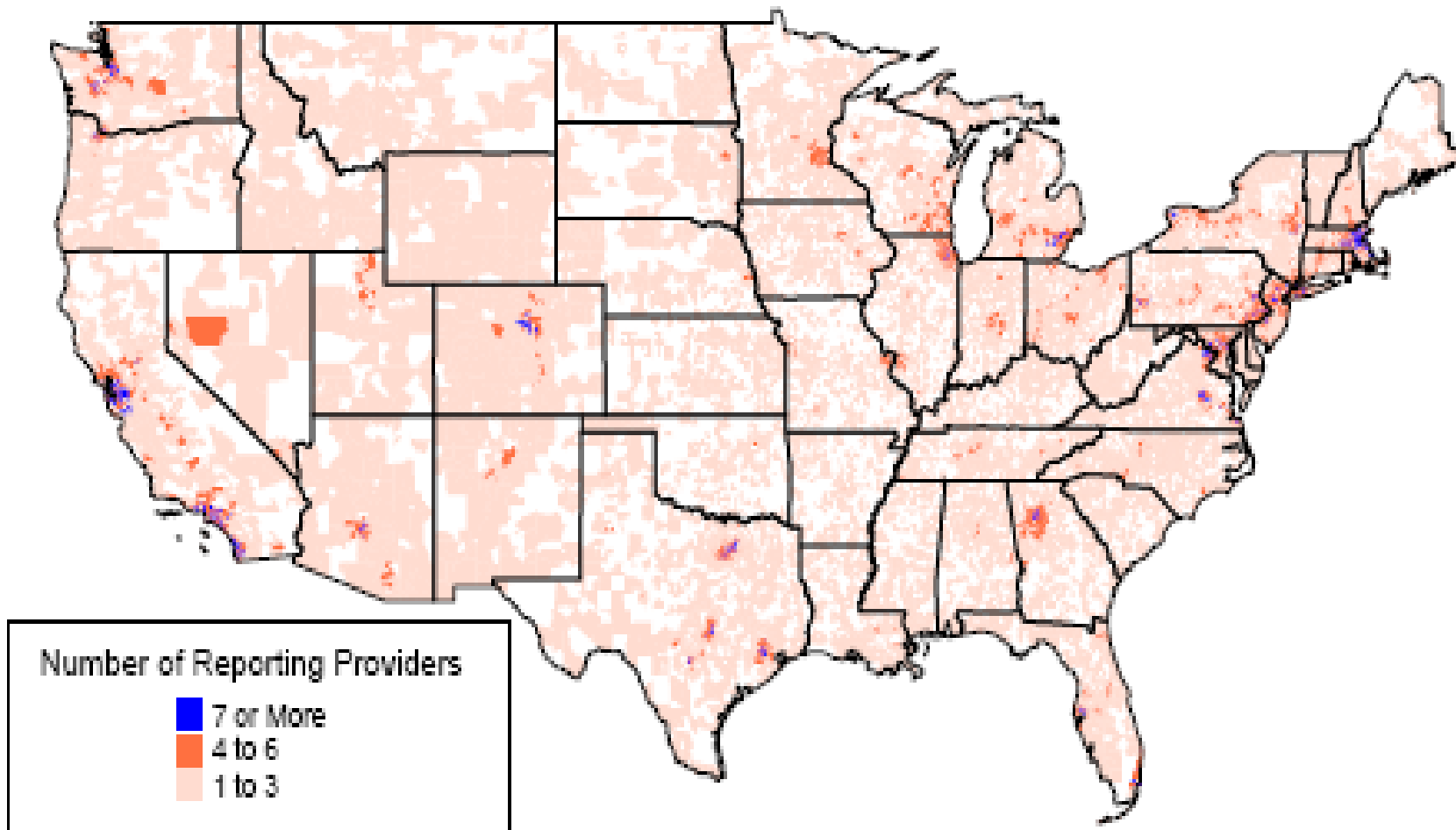


The Competitiveness of Rural Places

- Technology: Rural America adopts technology
- Infrastructure: a focus on broadband and communication, but what about traditional infrastructure (roads, rail, and water)?



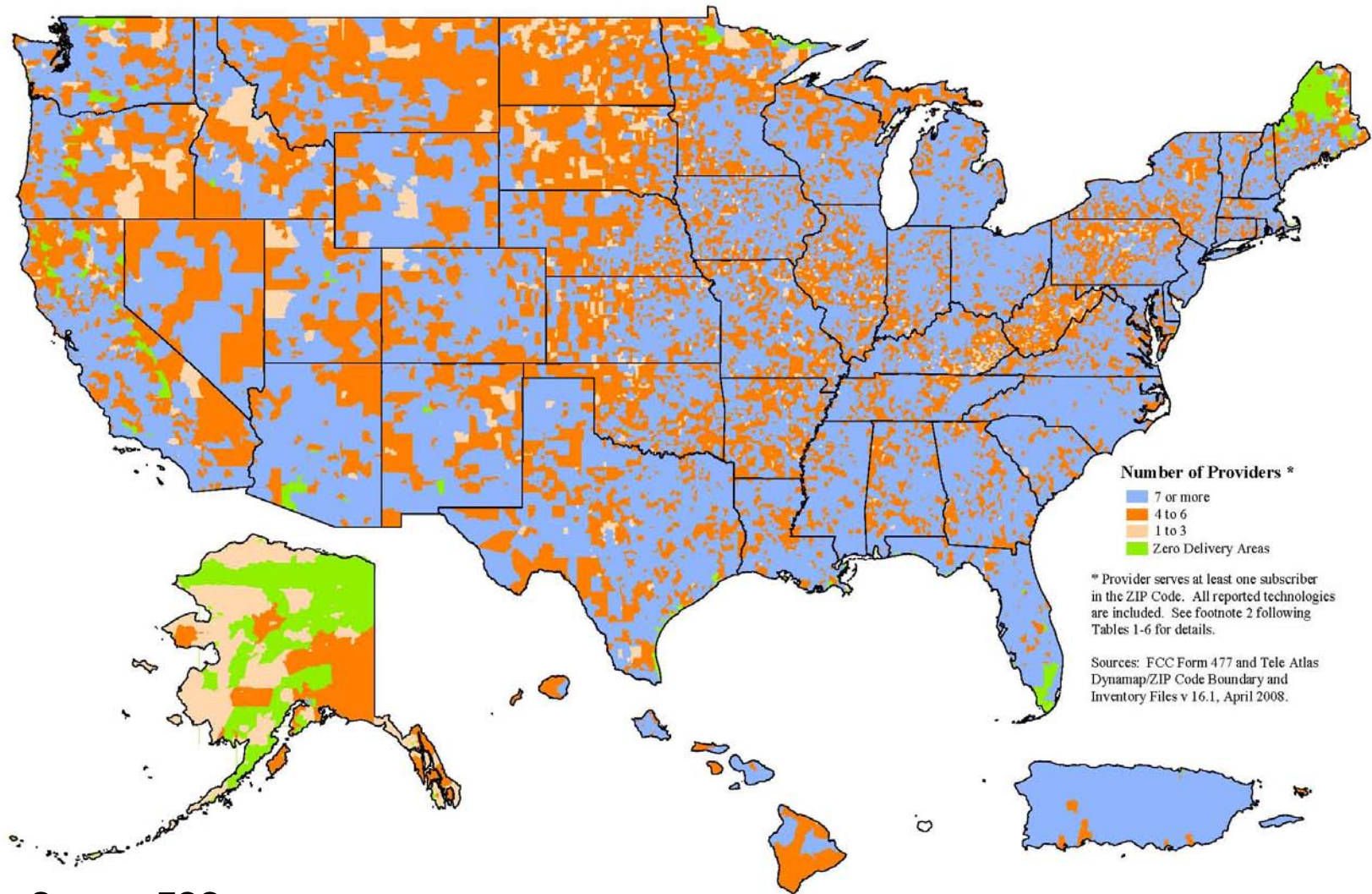
High Speed Internet Coverage June 2000



Source: FCC



High Speed Internet Coverage 2008

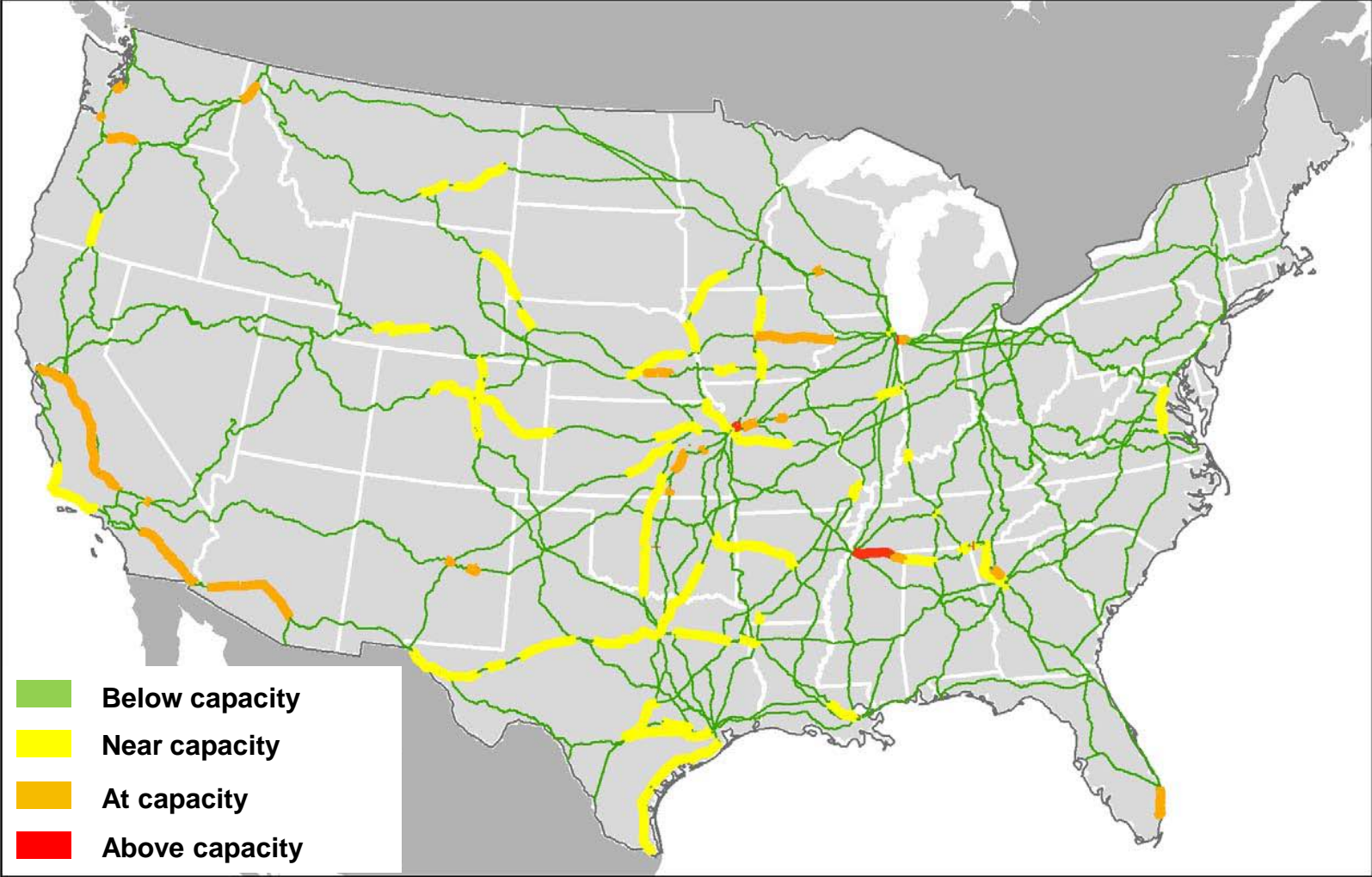


Source: FCC



Railroad Capacity

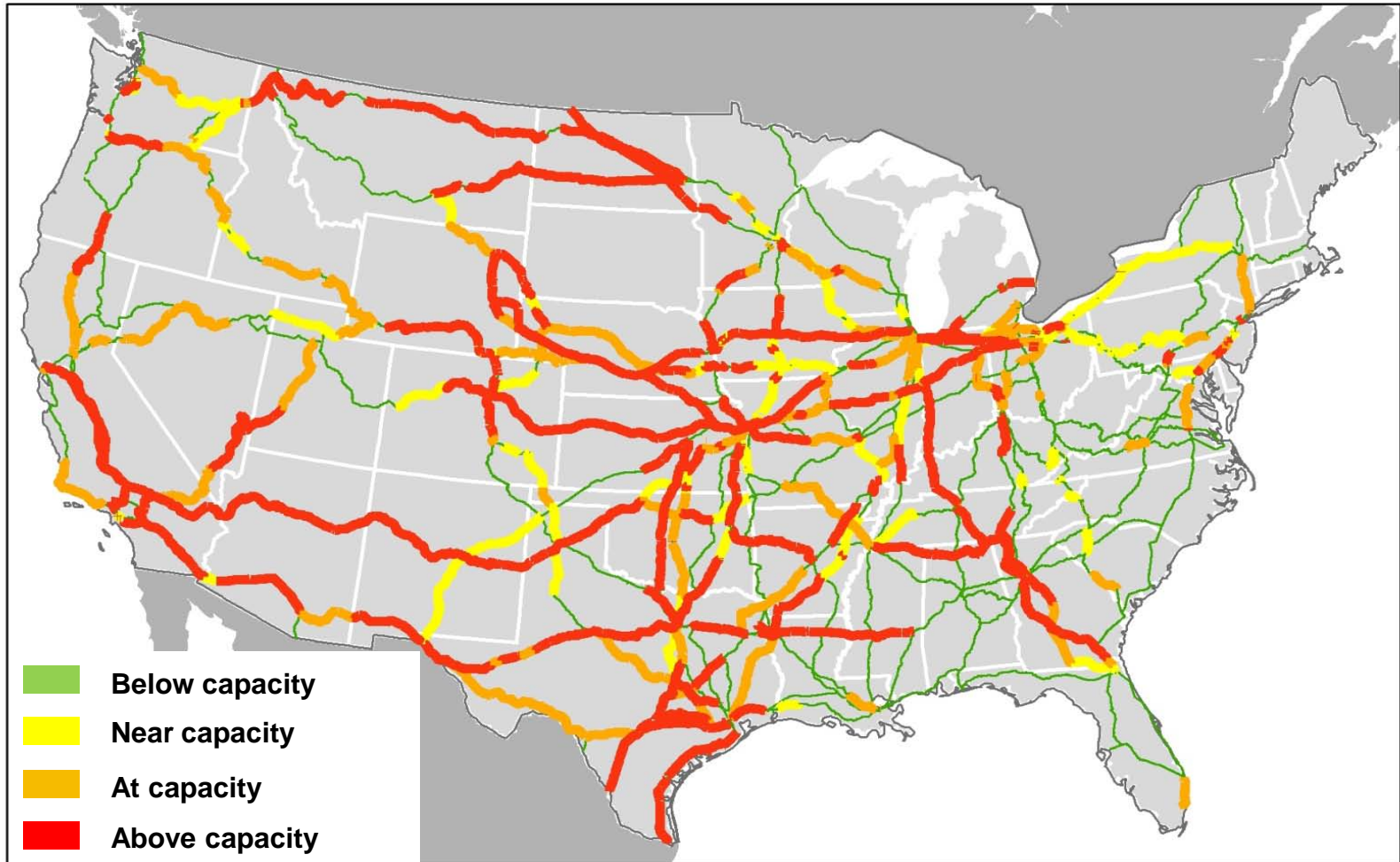
2007



Source: Dept. of Transportation



Projected Railroad Capacity 2035 without improvements



Source: Dept. of Transportation



What has Brazil been doing over the past decade?

Soybean Production Costs in U.S., Brazil and Argentina, 1998 (Dollars per bushel)

	U.S. Heartland	Mato Grasso , Brazil	Argentina
Variable costs	\$1.71	\$3.17	\$1.90
Fixed costs	\$3.40	\$0.72	\$2.02
Total production costs	\$5.11	\$3.89	\$3.92
Internal transportation and marketing	\$0.43	\$1.34	\$0.81
Freight Cost	\$0.38	\$0.57	\$0.49
Total costs	\$5.92	\$5.80	\$5.22

Source: USDA



The Competitiveness of Rural Places

- Technology: Rural America adopts technology
- Infrastructure: a focus on broadband and communication, but what about traditional infrastructure (roads, rail, and water)?
- Capital: Despite current situation, U.S. capital markets are the envy of the world.
 - Who is the “safe haven” financial market?
 - Debt capital flows to rural America.
 - A better flow of equity capital to rural communities is needed.



The Competitiveness of Rural Places

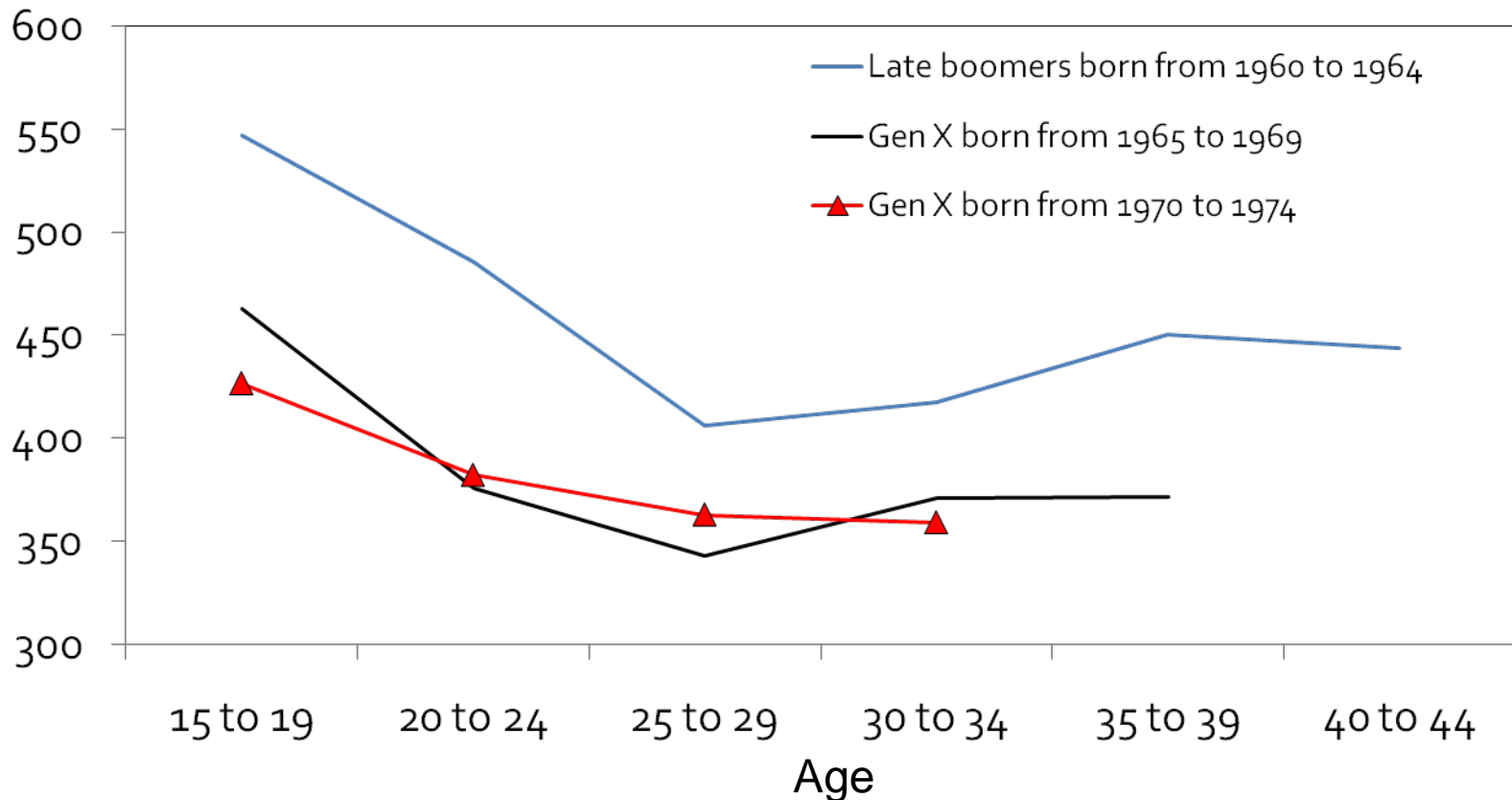
- Technology: Rural America adopts technology
- Infrastructure: a focus on broadband and communication, but what about traditional infrastructure (roads, rail, and water)?
- Capital: Despite current situation, U.S. capital markets are the envy of the world.
- Labor: a quantity of high-quality workers are needed.
 - Do jobs follow people, or do people follow jobs?
 - What entices people to return to rural America?



People do come home to rural America.

Rural Population by Birth Cohort (Tenth Federal Reserve District)

Thousands



The Competitiveness of Rural Places

- Technology: Rural America adopts technology
- Infrastructure: a focus on broadband and communication, but what about traditional infrastructure (roads, rail, and water)?
- Capital: Despite current situation, U.S. capital markets envy of the world.
- Labor: a quantity of high-quality workers are needed.
- Entrepreneurship: Necessity is the Mother of Invention.



How Does Knowing the Customer Affect What You Produce?



Japanese Watermelon

Cost:

**Square Watermelon:
\$82**

**Regular Watermelon
\$15 to \$25**

Source: BBC, 2001

Sold on a limited basis due to cost ... the Consumer is King



Conclusions


- *Recovery opens new horizons for rural America.*
- *High hopes for prosperity are not certain* in an environment of consolidation where money is not cheap, government action is high, and a fickle consumer is king.
- *Rural areas can compete* by tapping the pioneering spirit of our forefathers, where entrepreneurial investments in technology, infrastructure, capital, and labor are key.





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AND THE *Global Marketplace*

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