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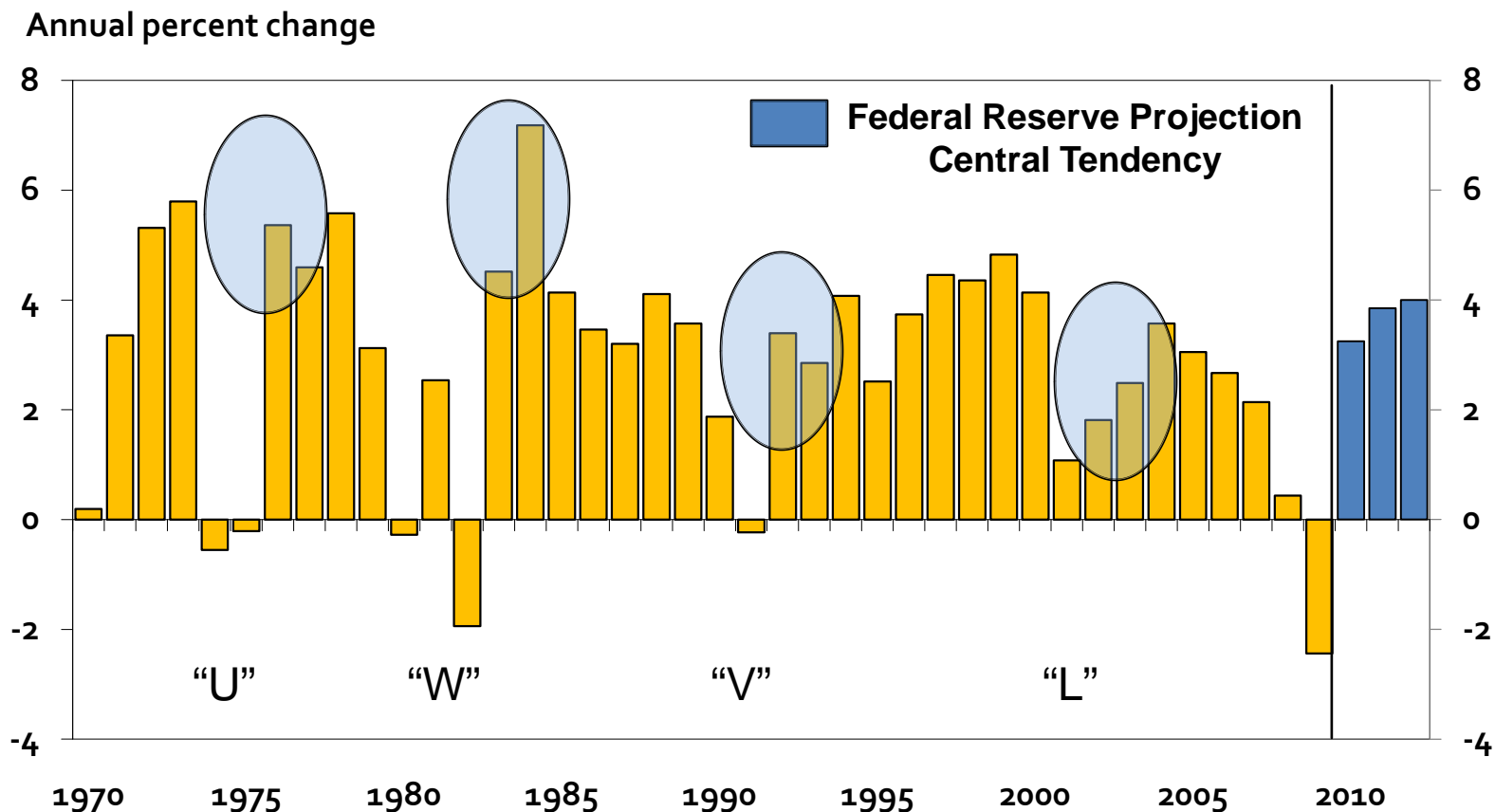
# Navigating Our Challenging Economy



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.

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

## Real GDP Growth

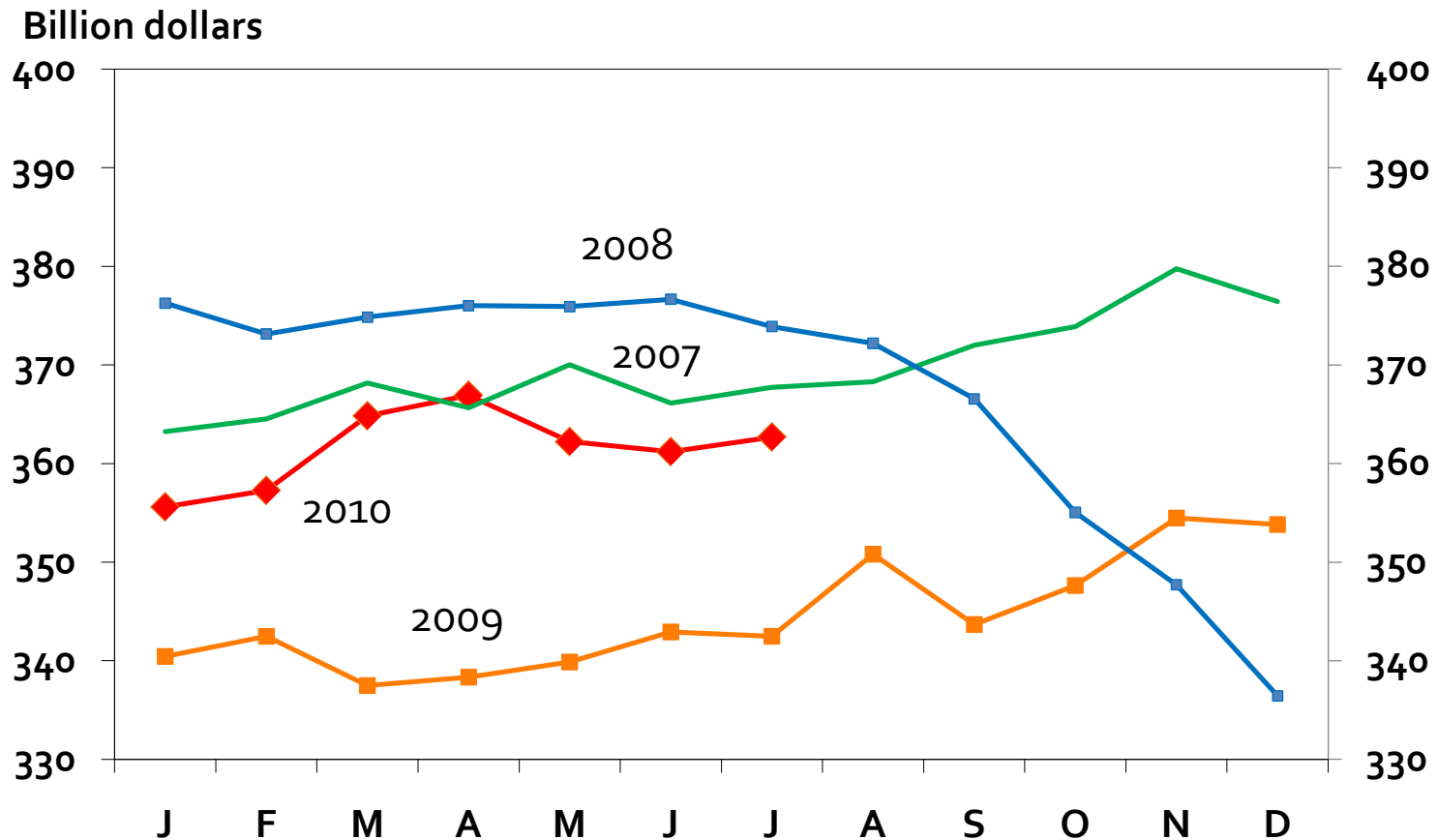


Source: Bureau of Economic Analysis Federal Reserve Board of Governors



# U.S. consumers are spending money.

## U.S. Monthly Retail and Food Sales

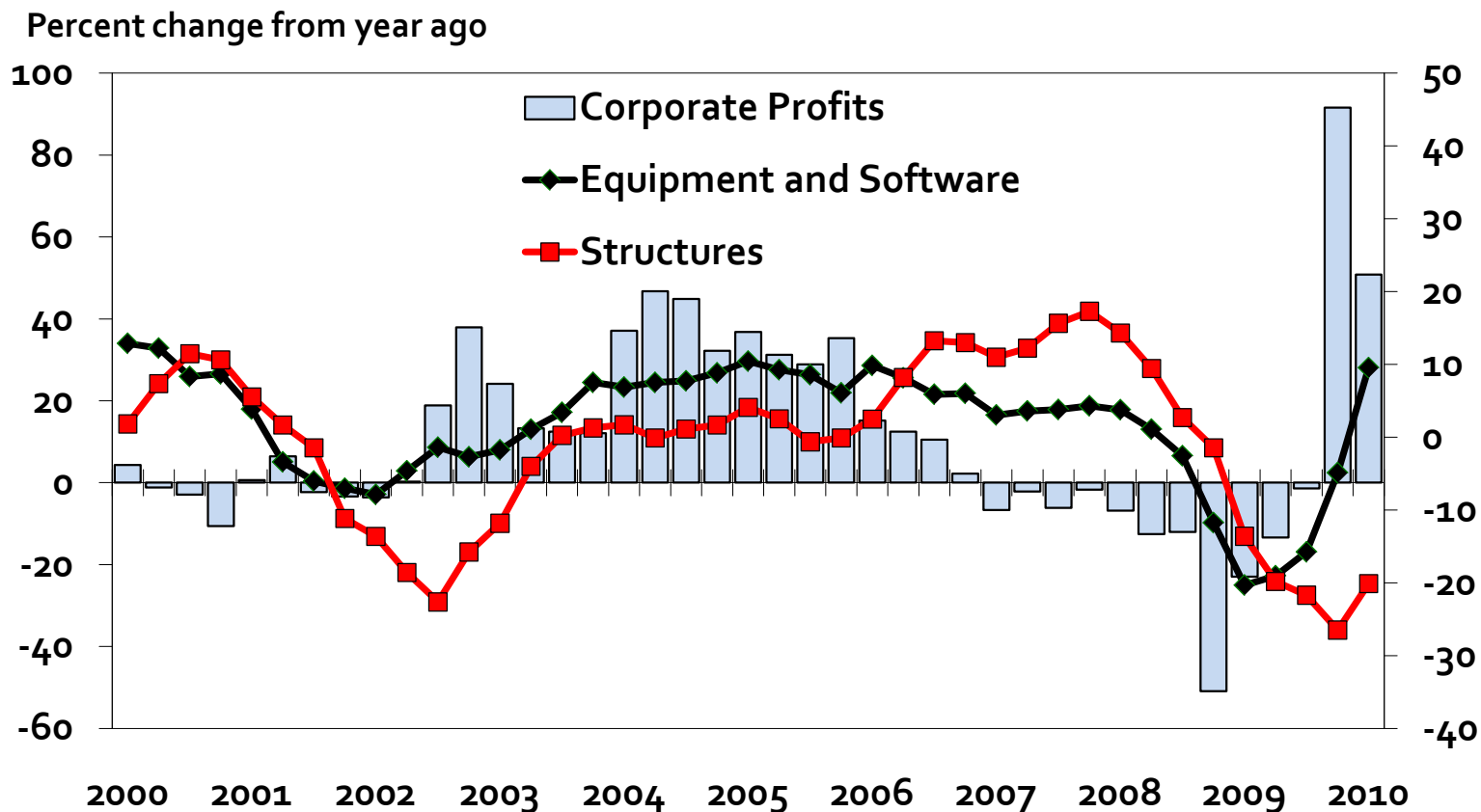


Source: U.S. Census Bureau



# Corporate profits and business investment are beginning to rebound.

## Corporate Profits and Nonresidential Fixed Investment

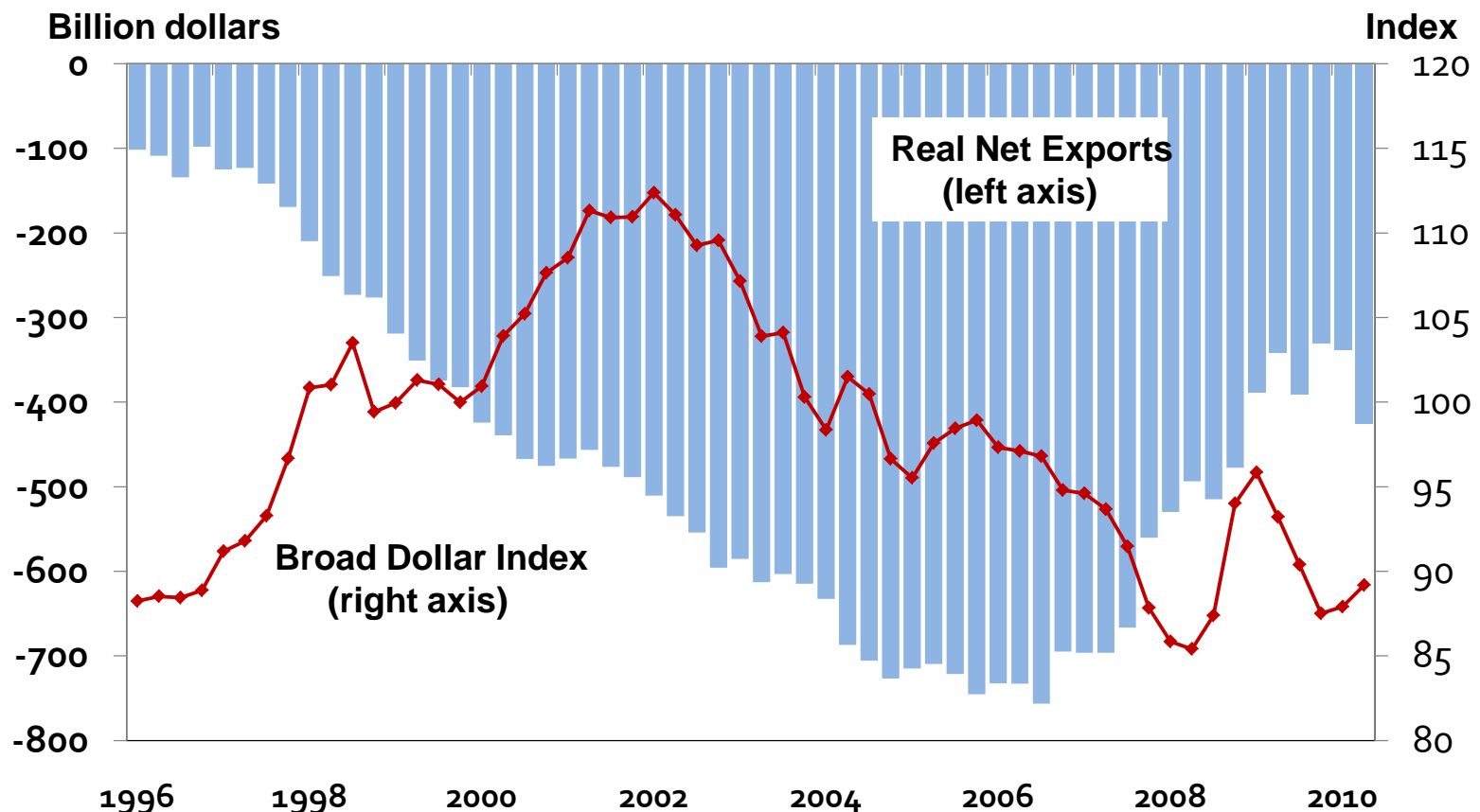


Source: Bureau of Economic Analysis



# 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

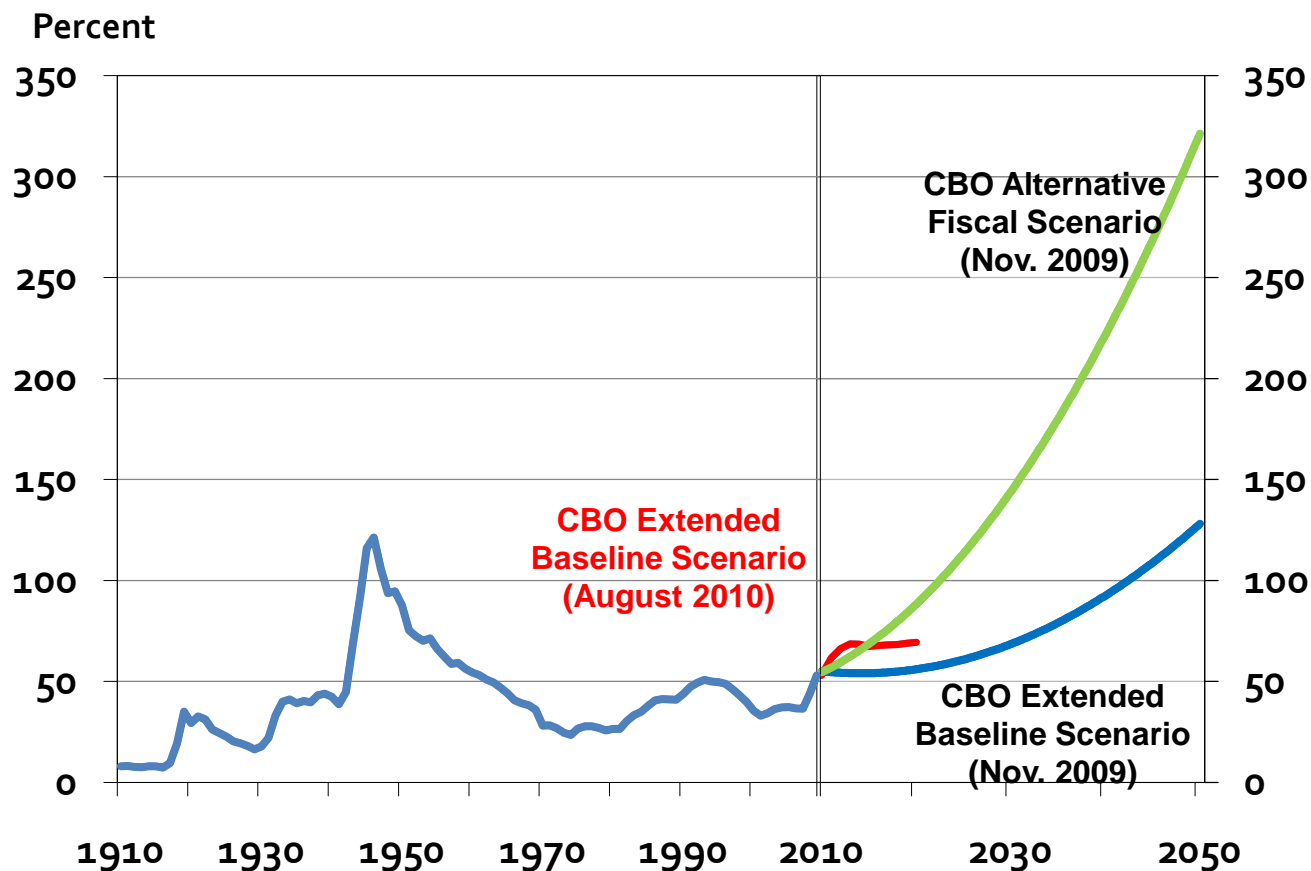


Source: Bureau of Economic Analysis and Federal Reserve Board of Governors



# How will surging federal debt levels affect economic conditions long-term?

## U.S. Debt as a Percent of GDP



Source: Congressional Budget Office



# Navigating Our Challenging Economy

- Today's Roadmap
  - Our challenging economy
  - What does this mean for real estate?
    - Residential markets: will the bottom hold?
    - Commercial markets: will signs of improvement emerge?
    - Agricultural markets: up, up, and ...



# *Real Estate 101*

- What was the real estate lesson of the 1980s farm crisis?

**Real estate values  
should be based  
on cash flows.**

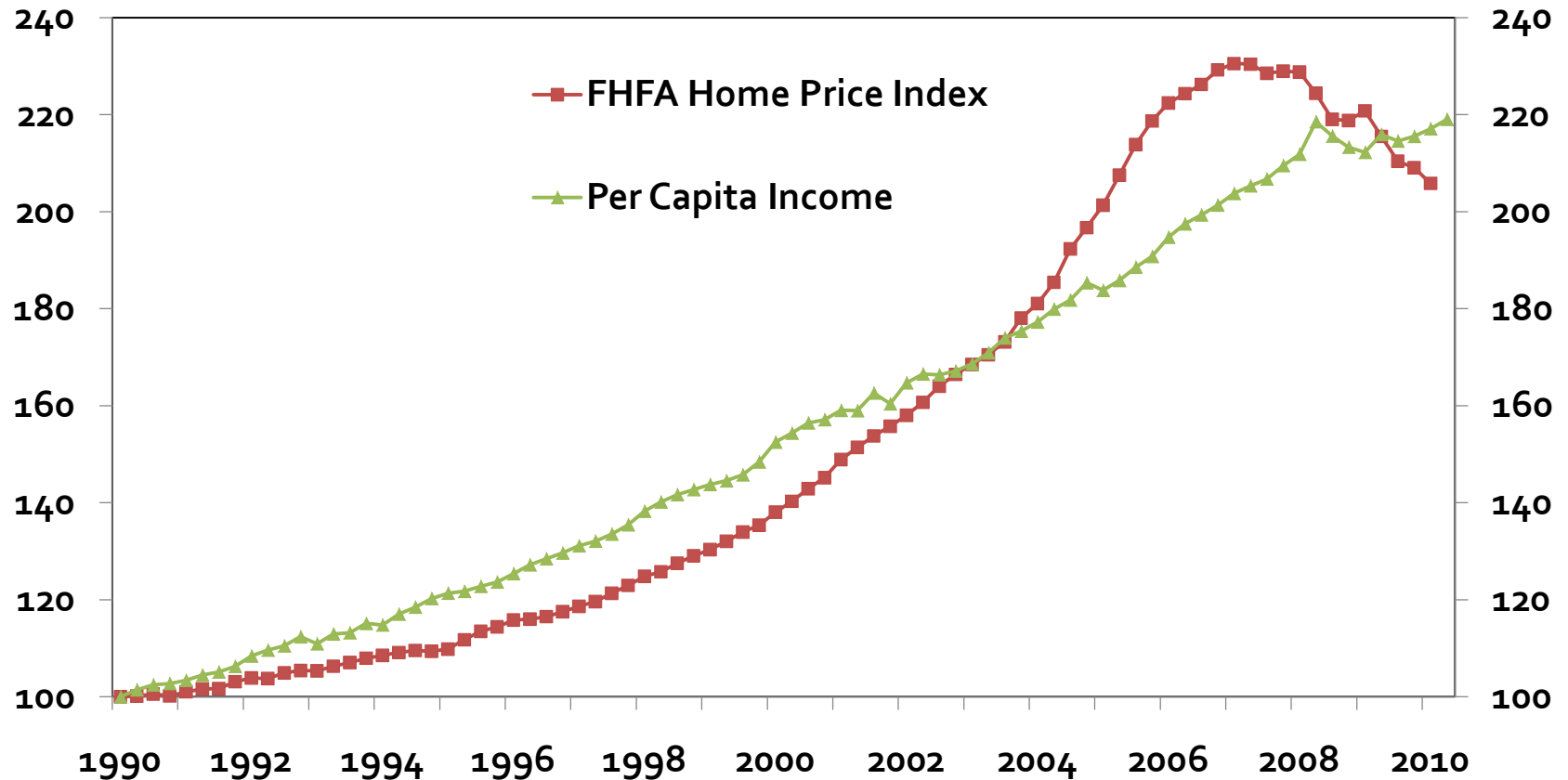




# Home prices outpaced personal incomes.

## U.S. Home Prices and Personal Incomes

Index (1990 = 100)



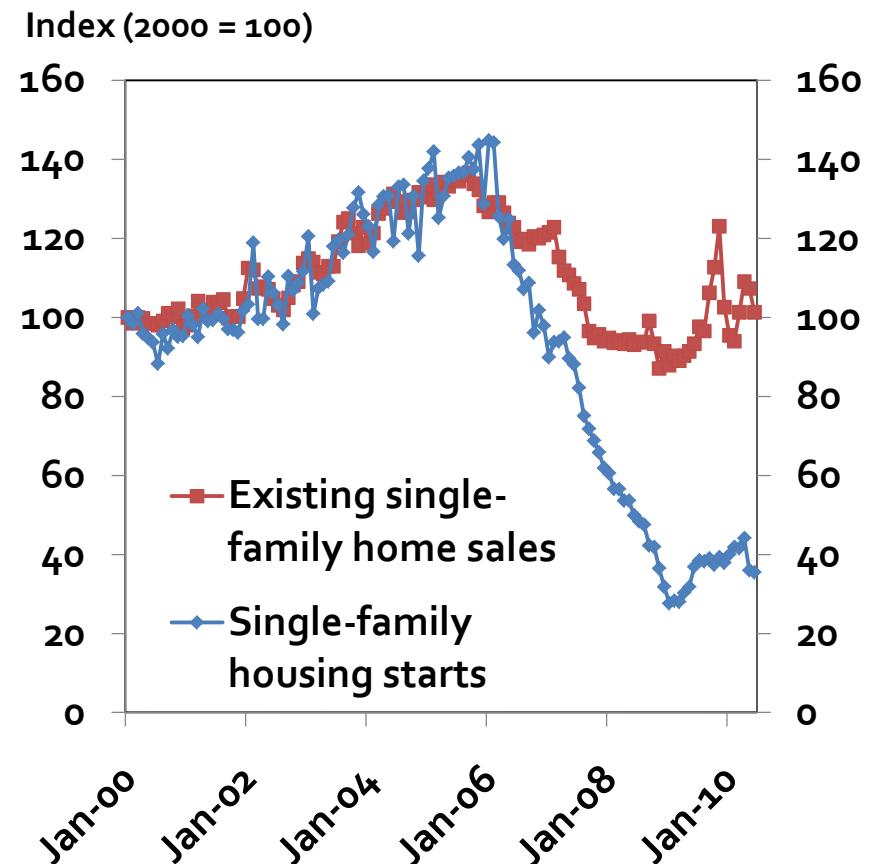
Source: USDA



# Have housing markets hit bottom?

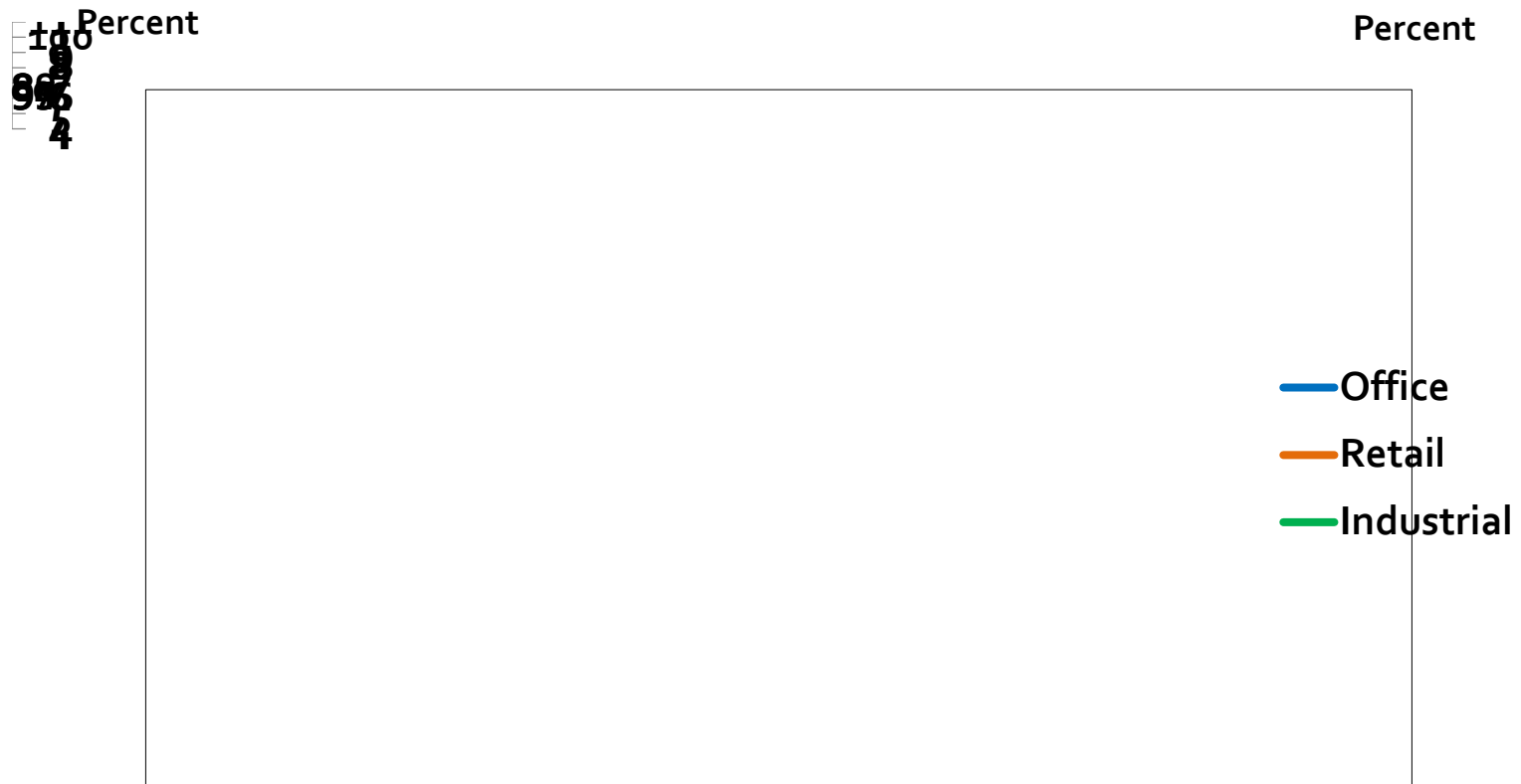
- Foreclosure rates have declined, but remain high.
- Housing starts have stabilized at low levels.
- Home sales have increased, primarily for low-priced homes.
- What happens after the end of the first-time home buyers tax credit?

Existing Home Sales and Housing Starts



*Prices have fallen faster than rents,  
leading to higher cap rates.*

## U.S. Commercial Real Estate Capitalization Rates



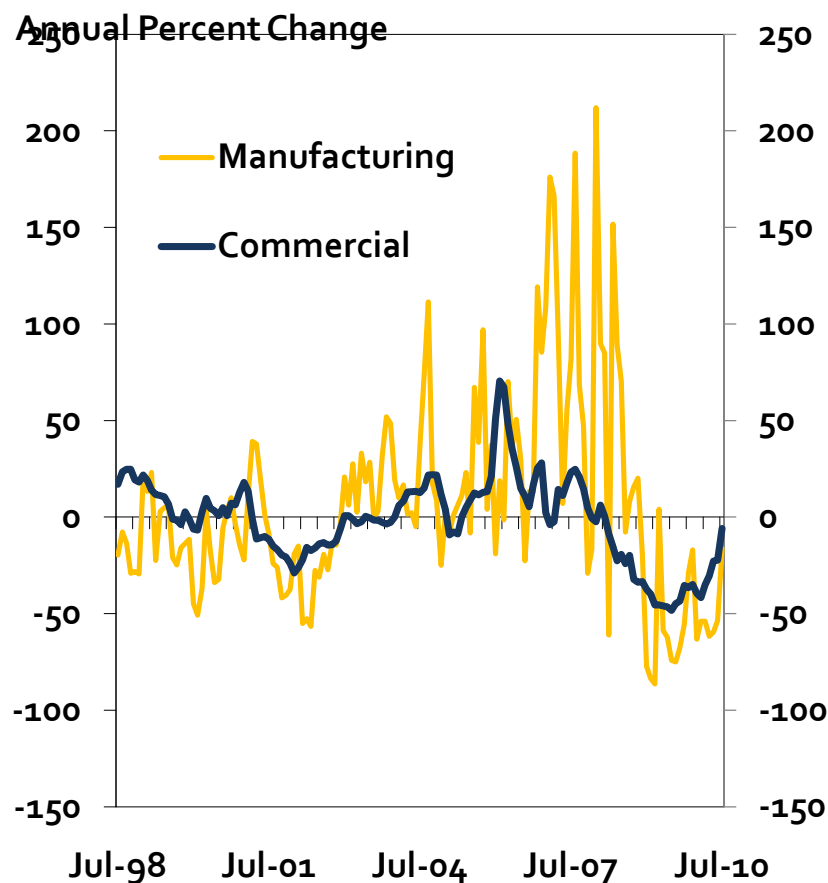
Source: Torto-Wheaton Research



# Commercial construction is beginning to stabilize at low levels.

- Commercial construction remains weak, with a few signs of improvement.
- In second quarter, vacancy rates declines in Denver, Kansas City, and Omaha. Will this trend continue?
- Industrial production and capacity utilization in manufacturing are edging up.
- Corporate profits have jumped, when will they invest in infrastructure?

## U.S. Value of Construction Put in Place

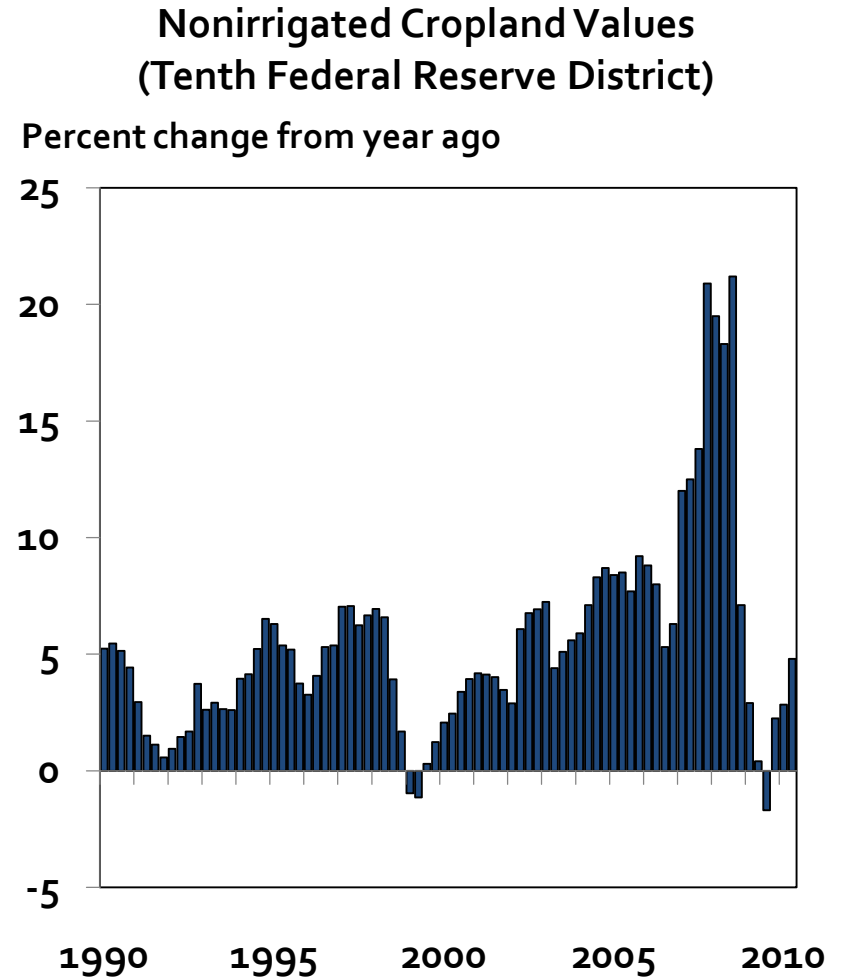


Source: F.W. Dodge



# Farmland values are rising again.

- After pausing in 2009, farmland values are rising.
- Robust farm demand with stronger incomes.
- Investor demand is rising.
  - Hedge against inflation
  - Limited returns on other assets.
- Fewer farms for sale.

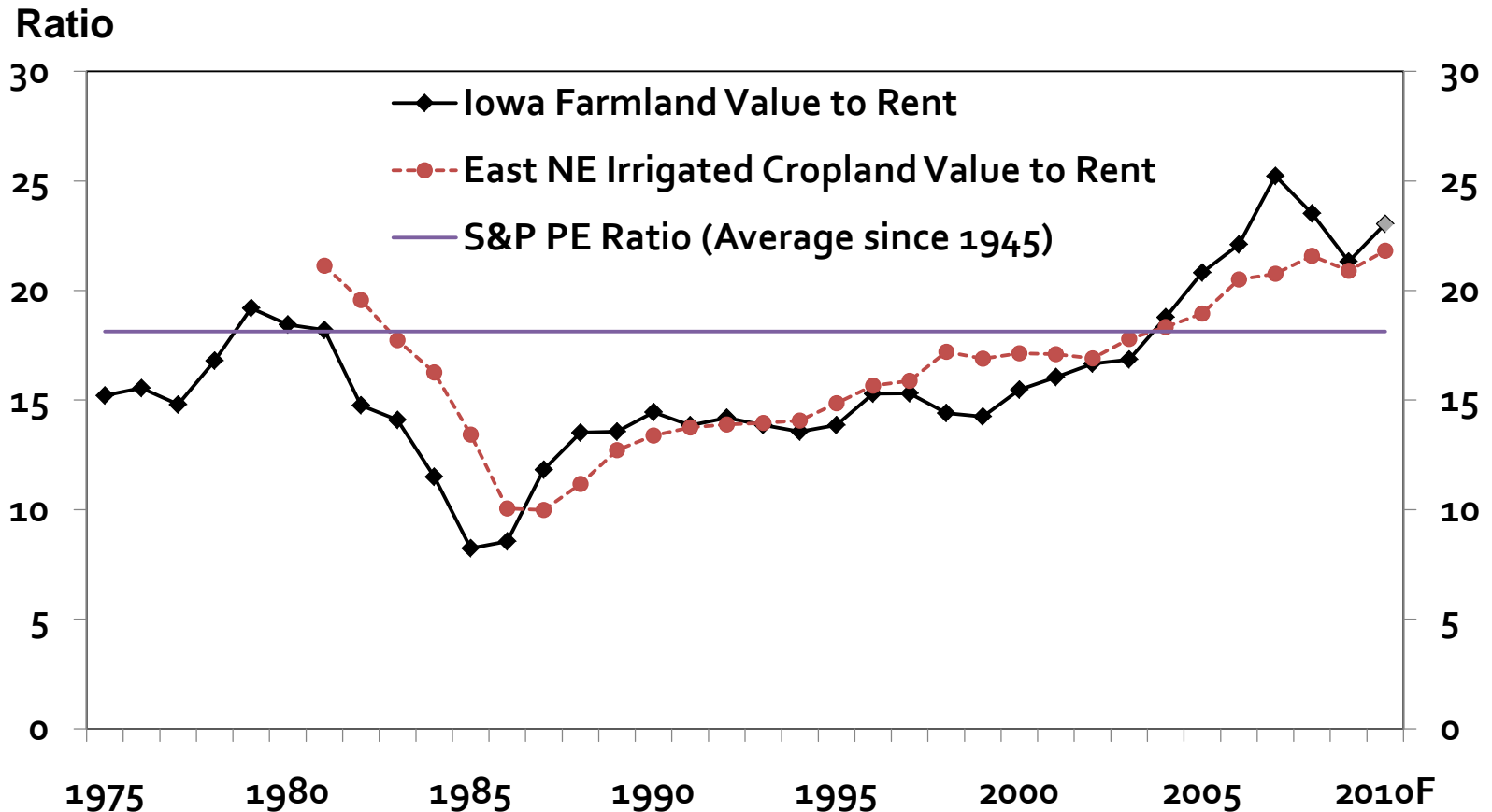


Source: Federal Reserve Bank of Kansas City



# Is a farmland bubble brewing?

## Farmland Values to Rent Ratio



Calculations based on Iowa State University and University of Nebraska data



# Navigating Our Challenging Economy

- Today's Roadmap
  - Our challenging economy
  - What does this mean for real estate?
  - Dealing with financial imbalances



# Two Perspectives on Monetary Policy and Resource Allocation

- The Issue: long periods of low interest rates lead to financial imbalances.
- Two Perspectives:
  - "... My preference at this time is to use prudential regulation and supervision to strengthen the financial system and lean against developing financial imbalances."  
Donald Kohn, Vice Chairman, Federal Reserve Board of Governors, May 13, 2010.
  - "It was after a period of too-low interest rates, too much credit, too much leverage that the collapse of the housing bubble, the rapid deleveraging and the ensuing financial crisis occurred." ...

"Monetary policy is a powerful tool. Certainly lowering interest rates is the appropriate monetary policy response to the onset of an economic recession and rising unemployment. But it is also a blunt instrument that has a wide set of unintended consequences that can and have worsened economic outcomes including misallocation of precious resources, inflation and long-term unemployment."

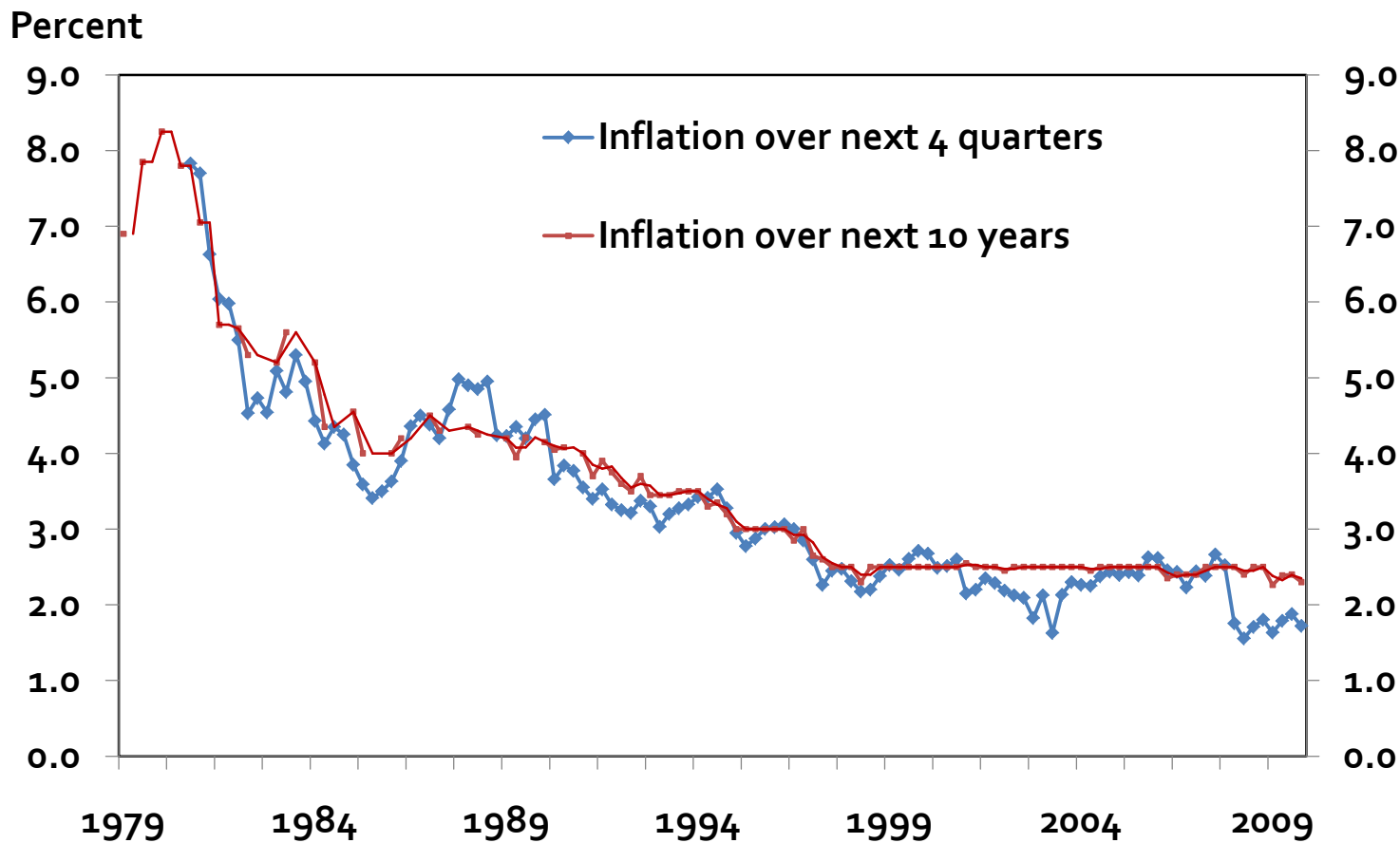
Thomas Hoenig, President and CEO, Federal Reserve Bank of Kansas City, June 3, 2010





# Deflation or Inflation: What does the future hold?

## Consumer Price Inflation Expectations



Source: Survey of Professional Forecasters



**For More Information**

**Federal Reserve Bank of Kansas City  
Omaha Branch**

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