

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



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History and Structure of the Federal Reserve System

- **Founded by Congress in 1913 as the nation's third central bank, the Fed consists of 3 main entities:**

- Board of Governors: 7 members appointed by U.S. President
- Federal Reserve Banks: 12 total; semi-independent by design
- Federal Open Market Committee (FOMC): 19 members; 12 voting

- **As with most central banks around the world, the Fed's responsibilities fall within four general areas:**

- Monetary policy – control money supply to affect growth and inflation
- Lender of last resort – provide liquidity in times of financial crisis
- Bank regulation – ensure safety and soundness, consumer rights
- Financial services – bank for banks, bank for federal government

Federal Reserve Districts and Office Locations

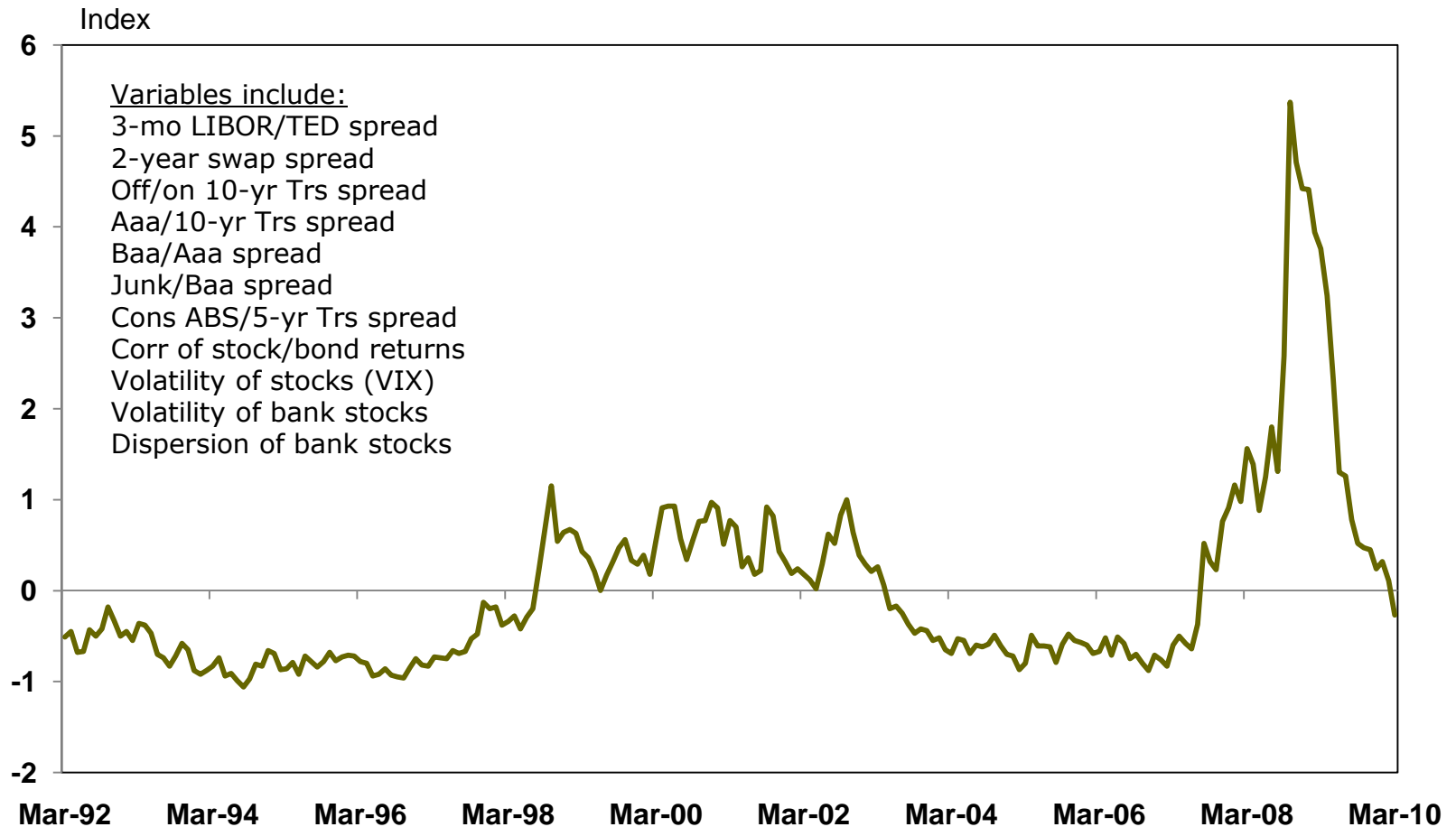


The U.S. Economy

- Credit market conditions have improved, and the U.S. economy is growing again
- But recovery is expected to be moderate, as debt and uncertainty remain high
- Inflation is expected to remain tame in the near term, but longer-run risks exist

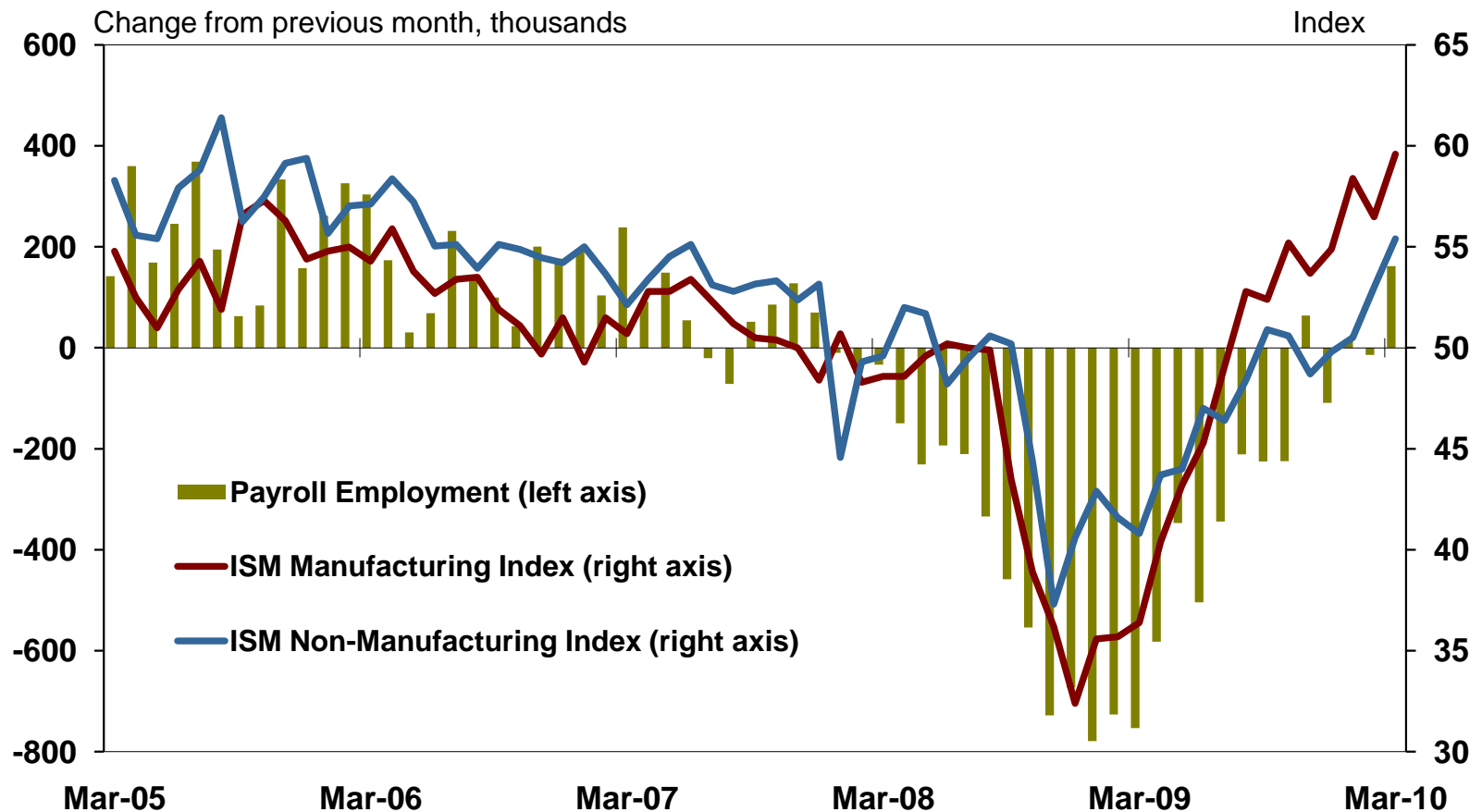
Broad measures of financial stress have moved back to normal levels

Kansas City Financial Stress Index



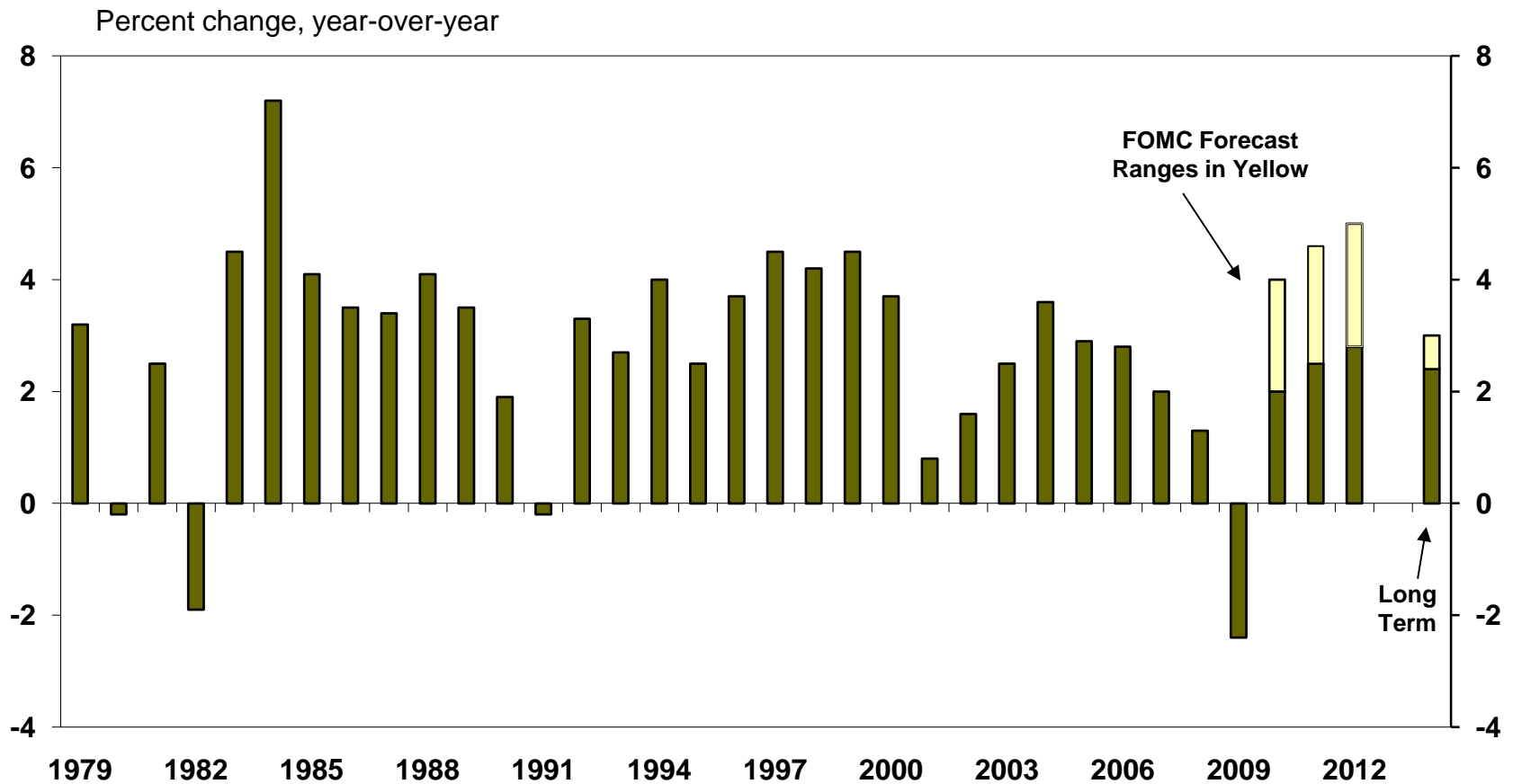
And early 2010 data show continued improvement in the U.S. economy

National Business Indexes and Payroll Employment



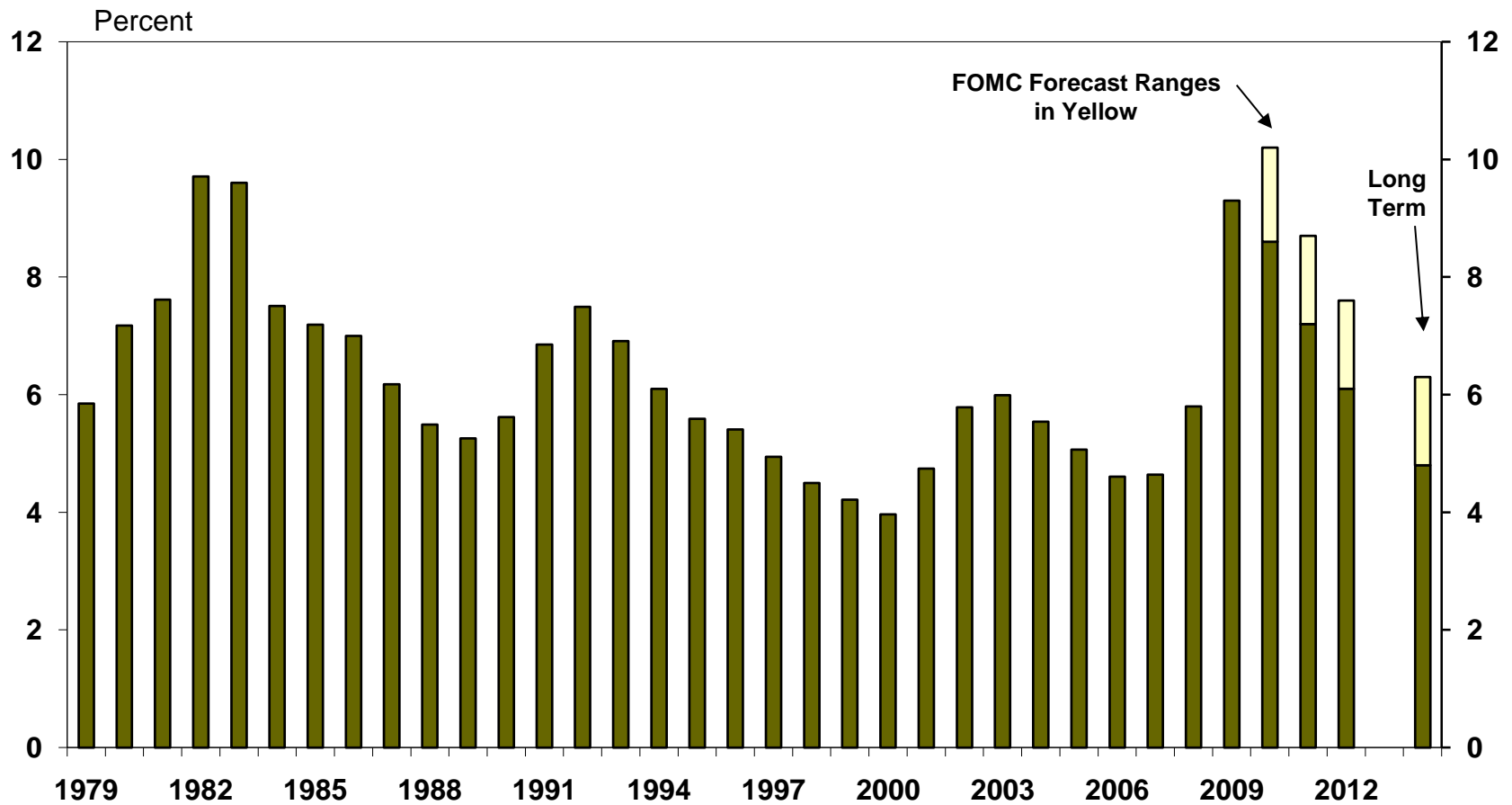
Heading forward, Fed policymakers generally expect a moderate recovery

Gross Domestic Product



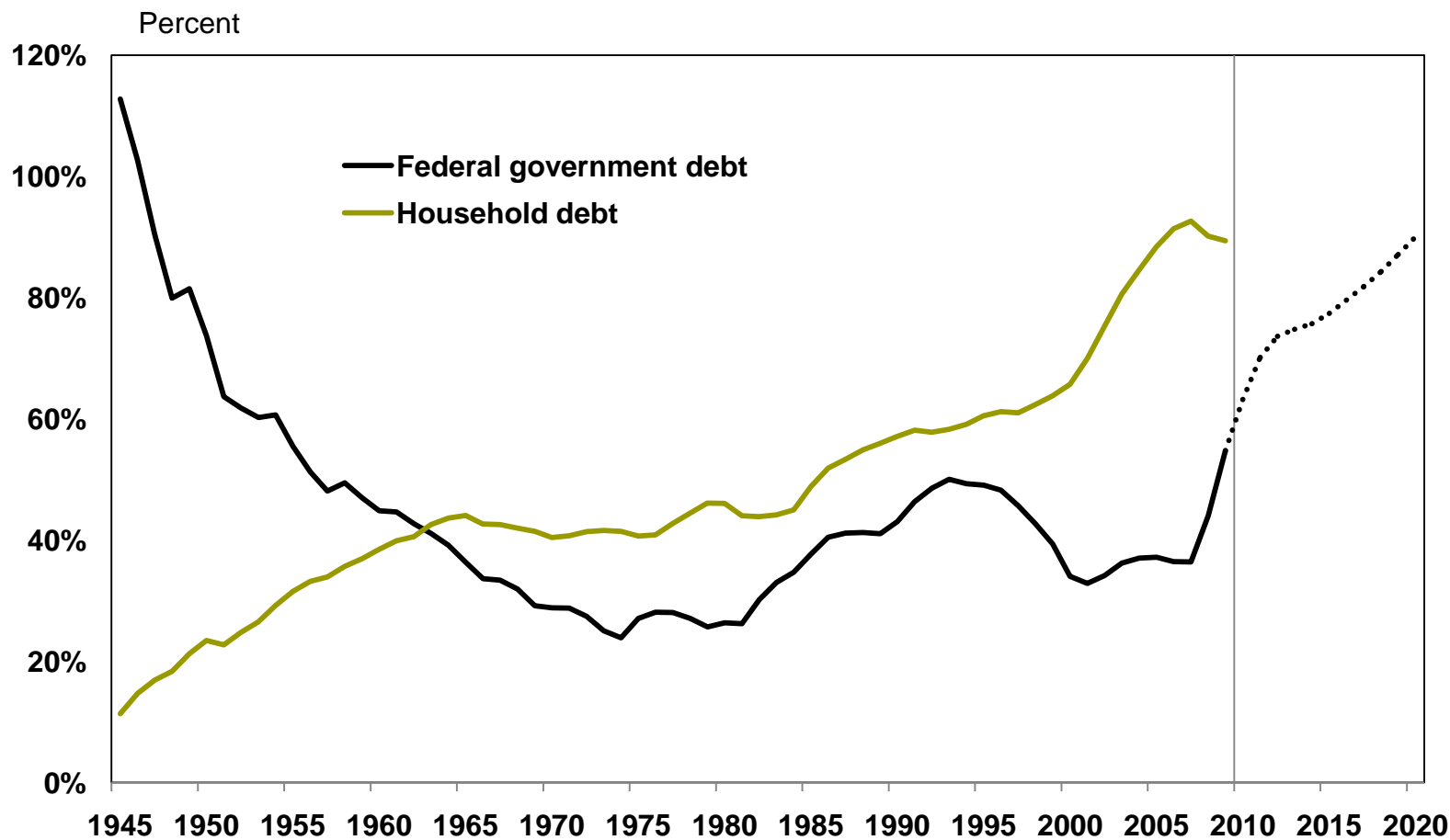
With unemployment remaining high for some time

Unemployment Rate
Seasonally Adjusted



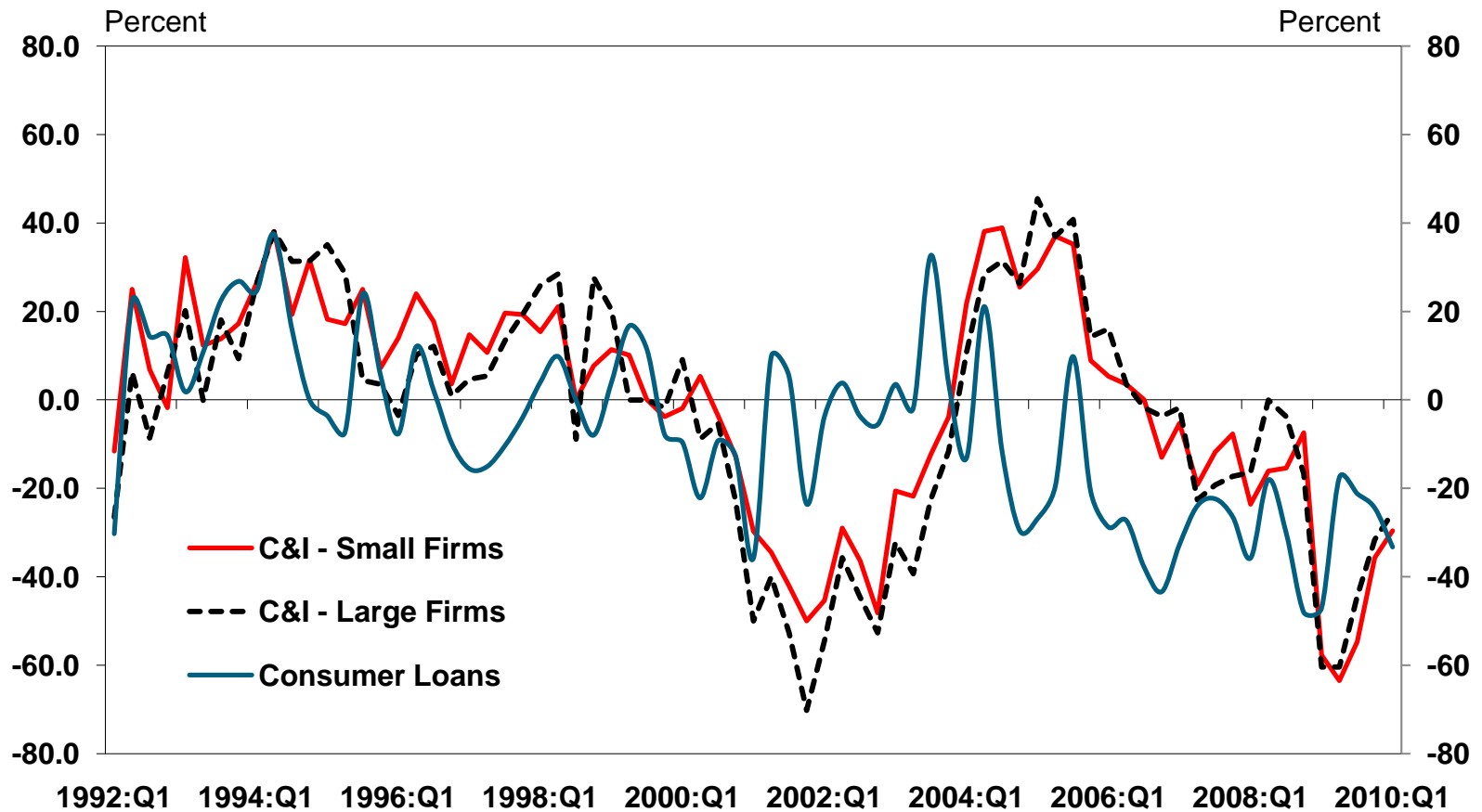
Consumer debt could constrain short-run growth and federal debt projections are a concern

U.S. Debt as a Share of GDP



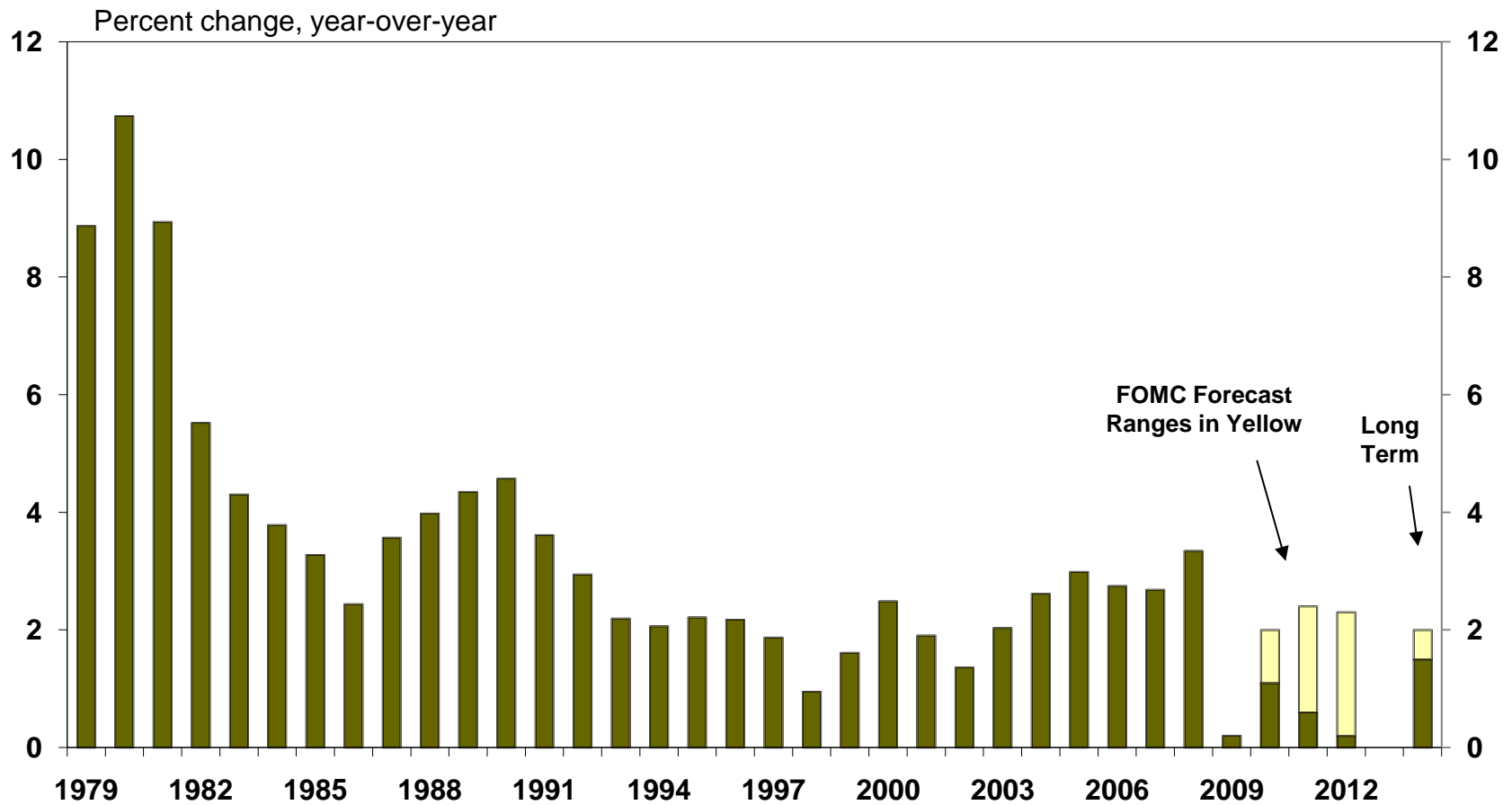
Both business and consumer loan demand remain sluggish

Net Percentage of Banks Reporting Increased Loan Demand



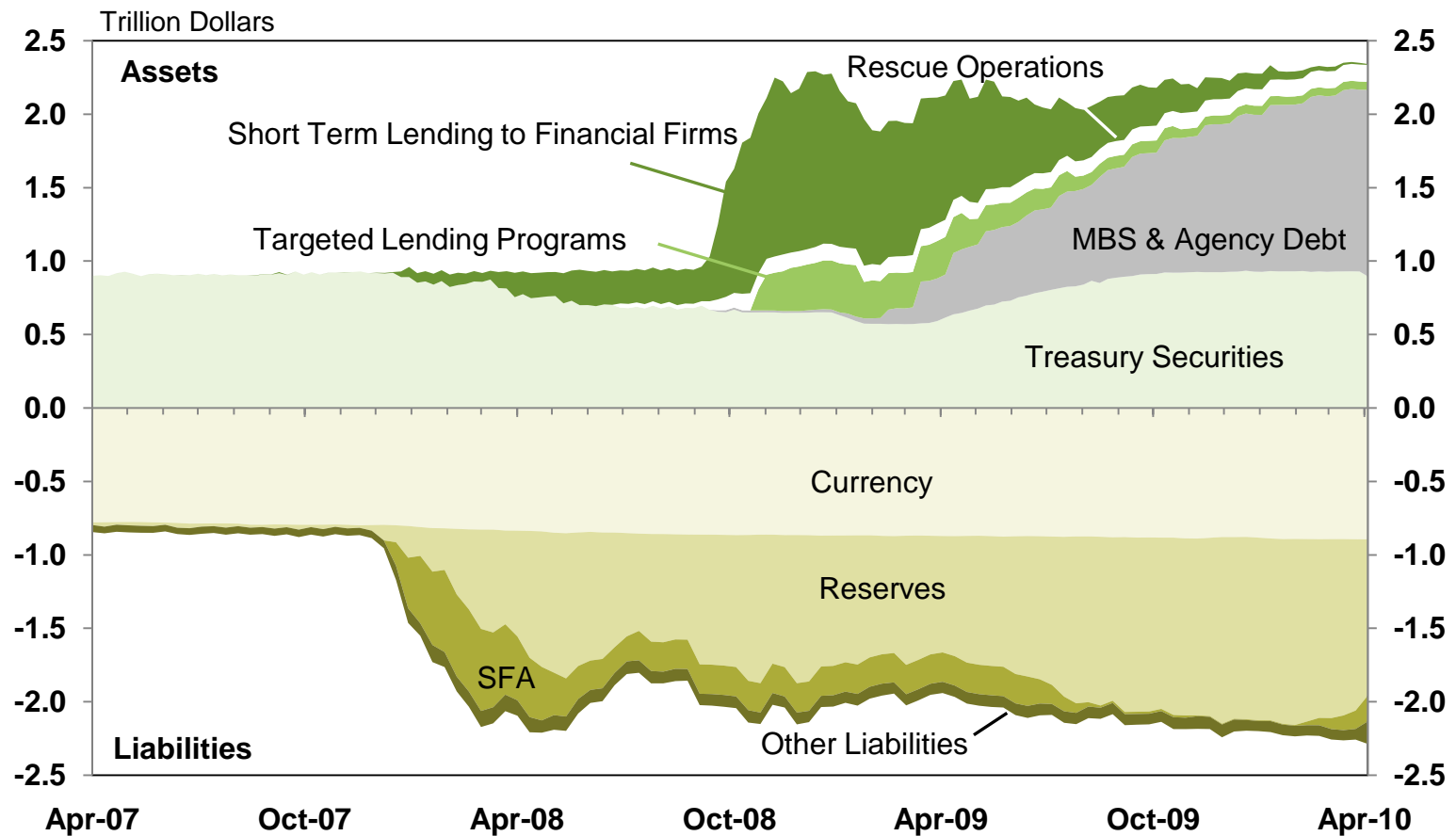
Inflation is expected to remain tame in the near term, but will require careful oversight

PCE Inflation Index



The Fed's balance sheet is still large, with extra assets now largely MBS

Federal Reserve Balance Sheet

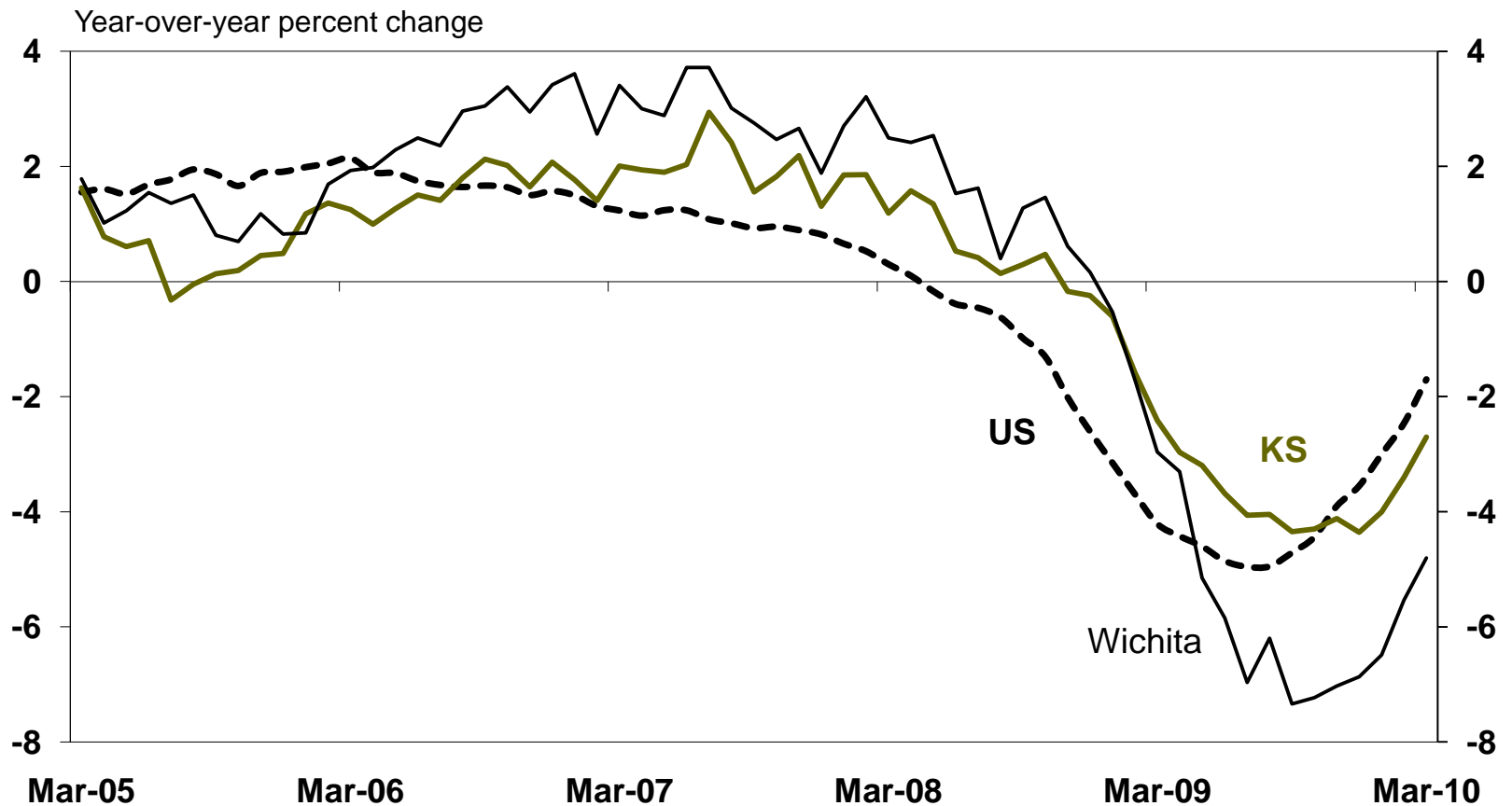


The Kansas Economy

- Like much of the Tenth Fed District, Kansas entered late into the recent recession
- But the state then shed jobs rapidly in 2009, especially in Wichita
- Signs of stabilization are emerging, and conditions remain better than in the nation

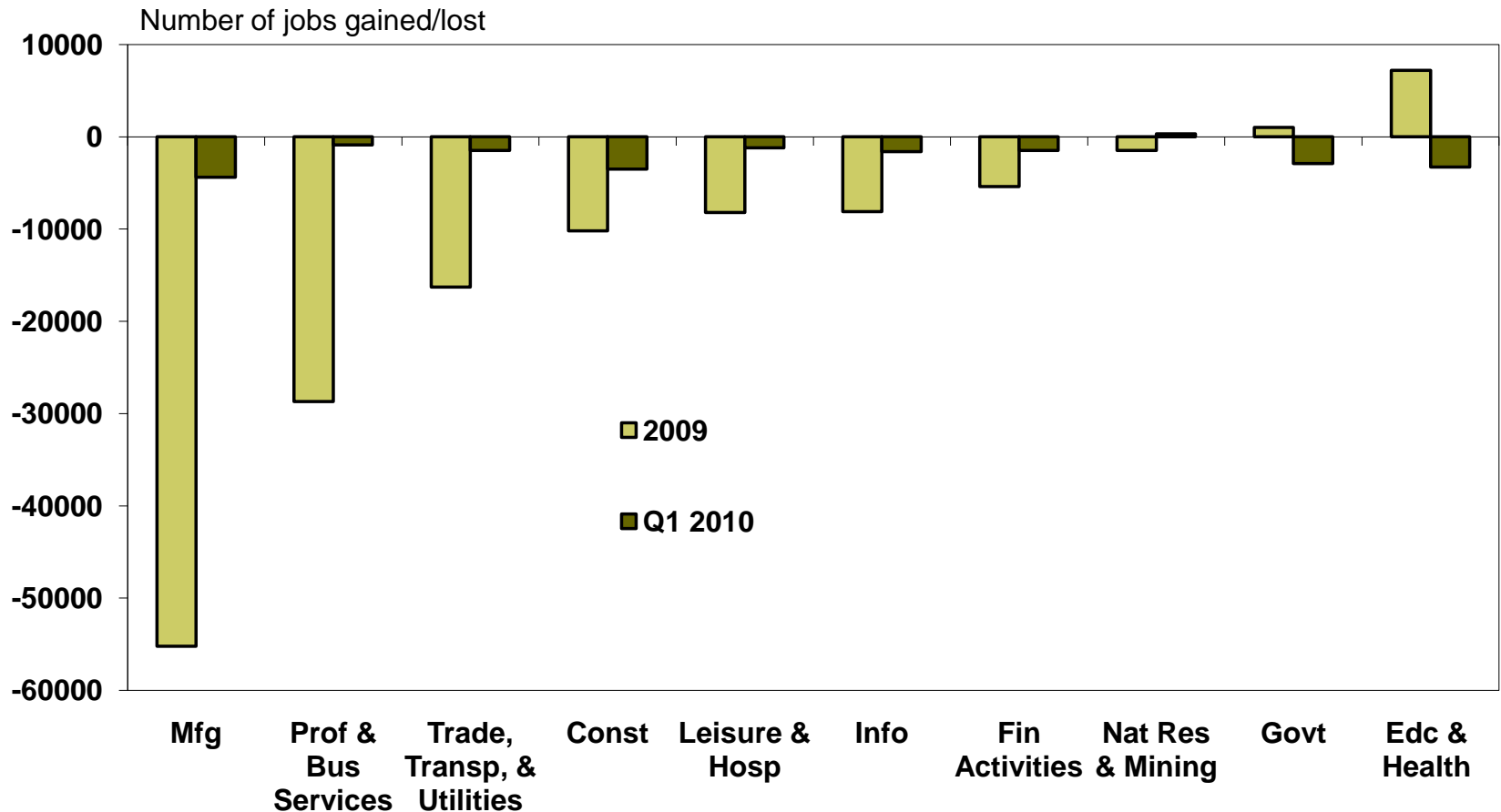
After steep declines in 2009, Kansas employment appears to have bottomed

Nonfarm Payroll Employment Growth



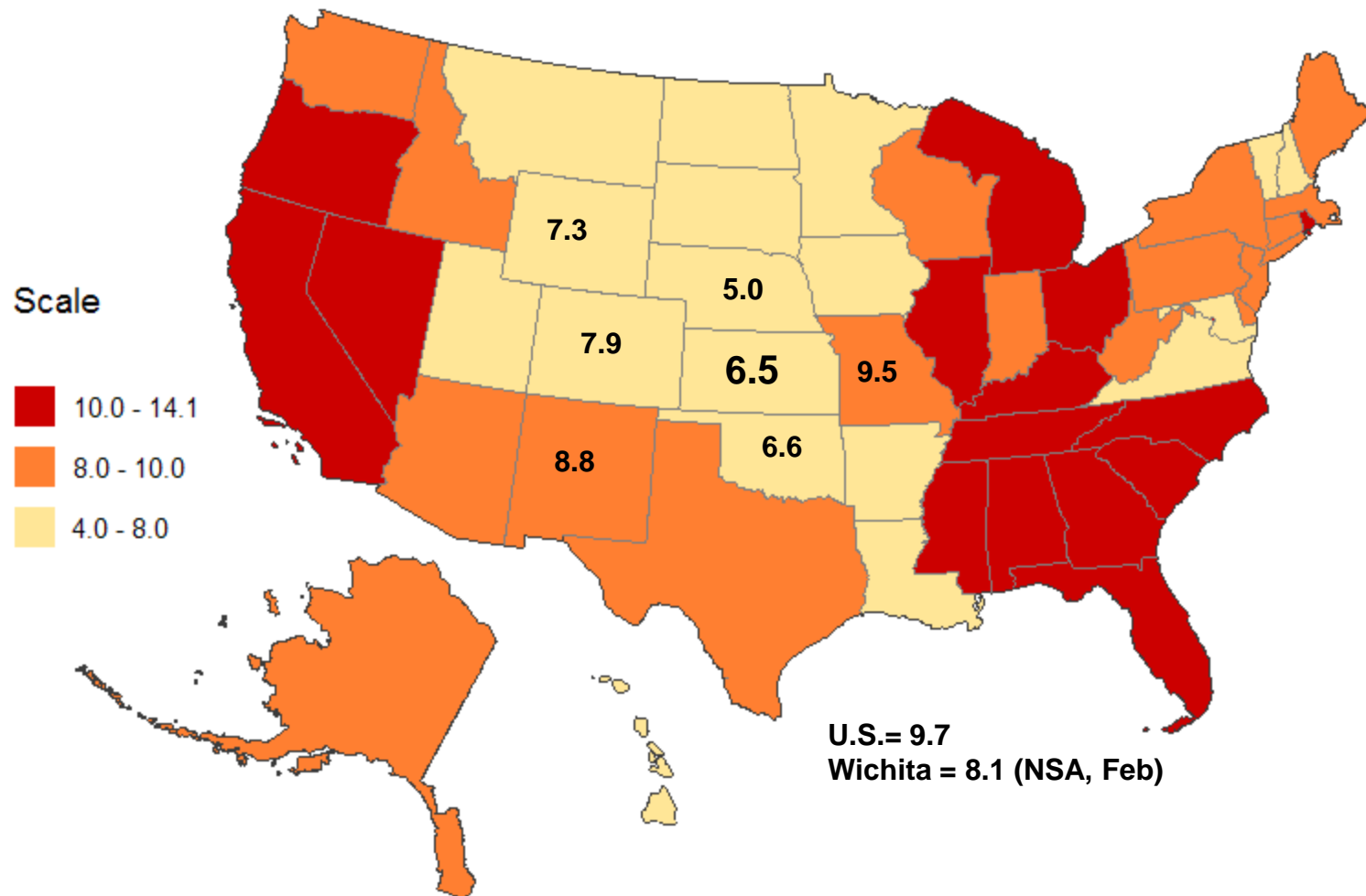
Employment stabilized across industries in Q1 2010, following a rough year in 2009

Kansas Employment Change by Industry



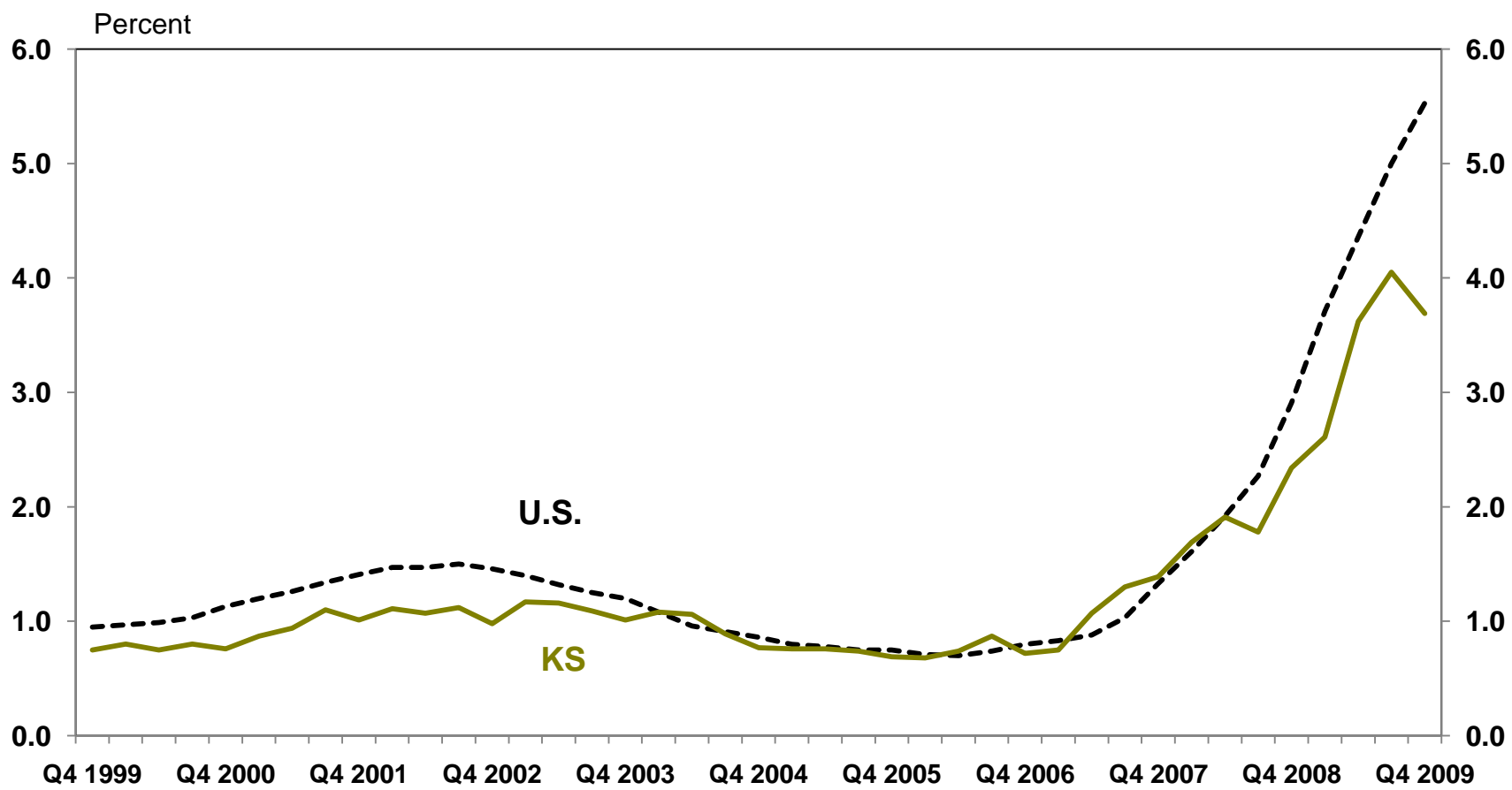
With the shorter recession, unemployment in the region is much lower than the nation

Unemployment Rate, March 2010



Banks in the state also remain in somewhat better shape than in the nation

Noncurrent Loans as a Share of Total Loans
Commercial Banks



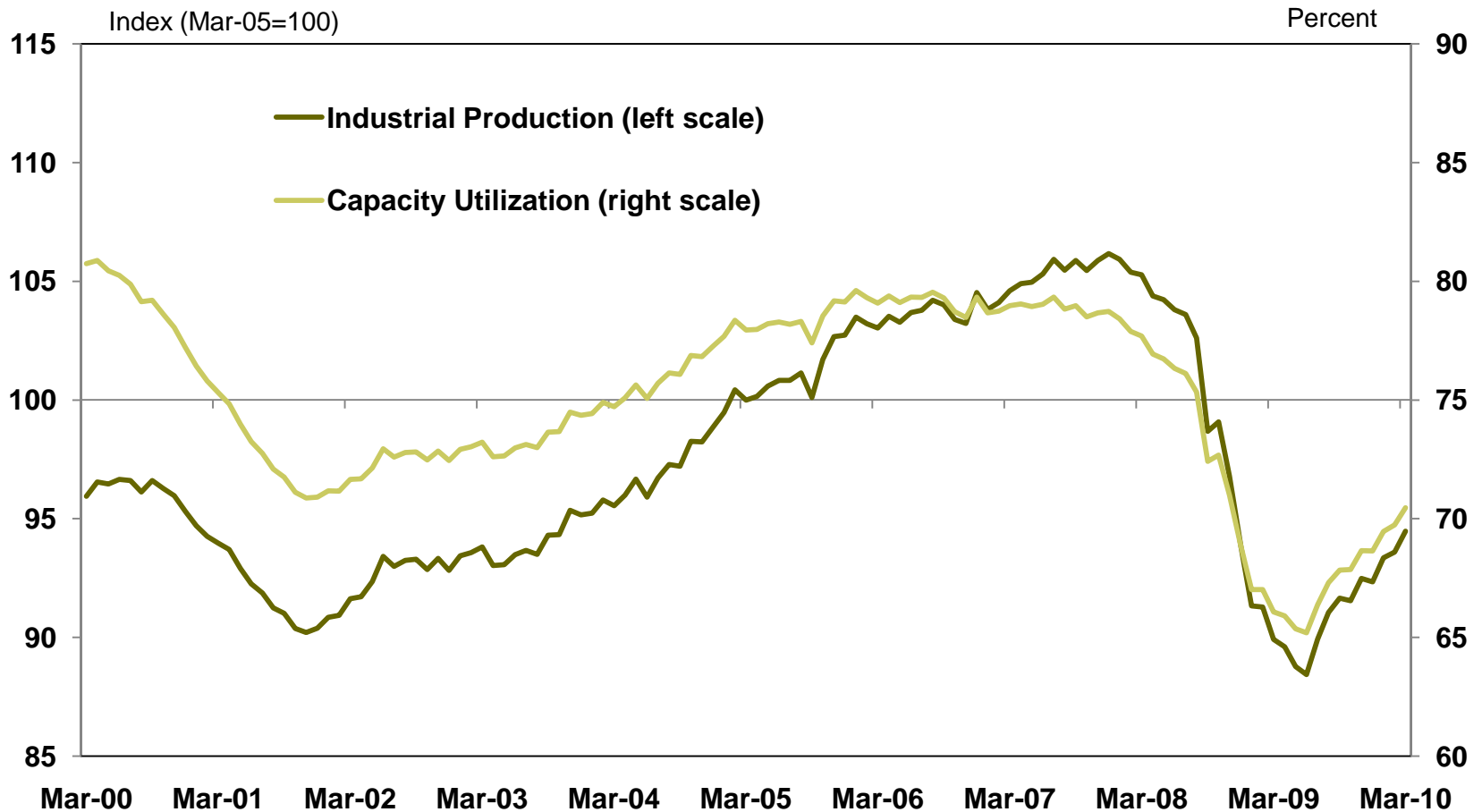
Source: FDIC

The Manufacturing Sector

- National and state factory activity is rising solidly and is expected to rise further
- But excess capacity and uncertainty remain, keeping a damper on capital spending
- Exports could provide future opportunities

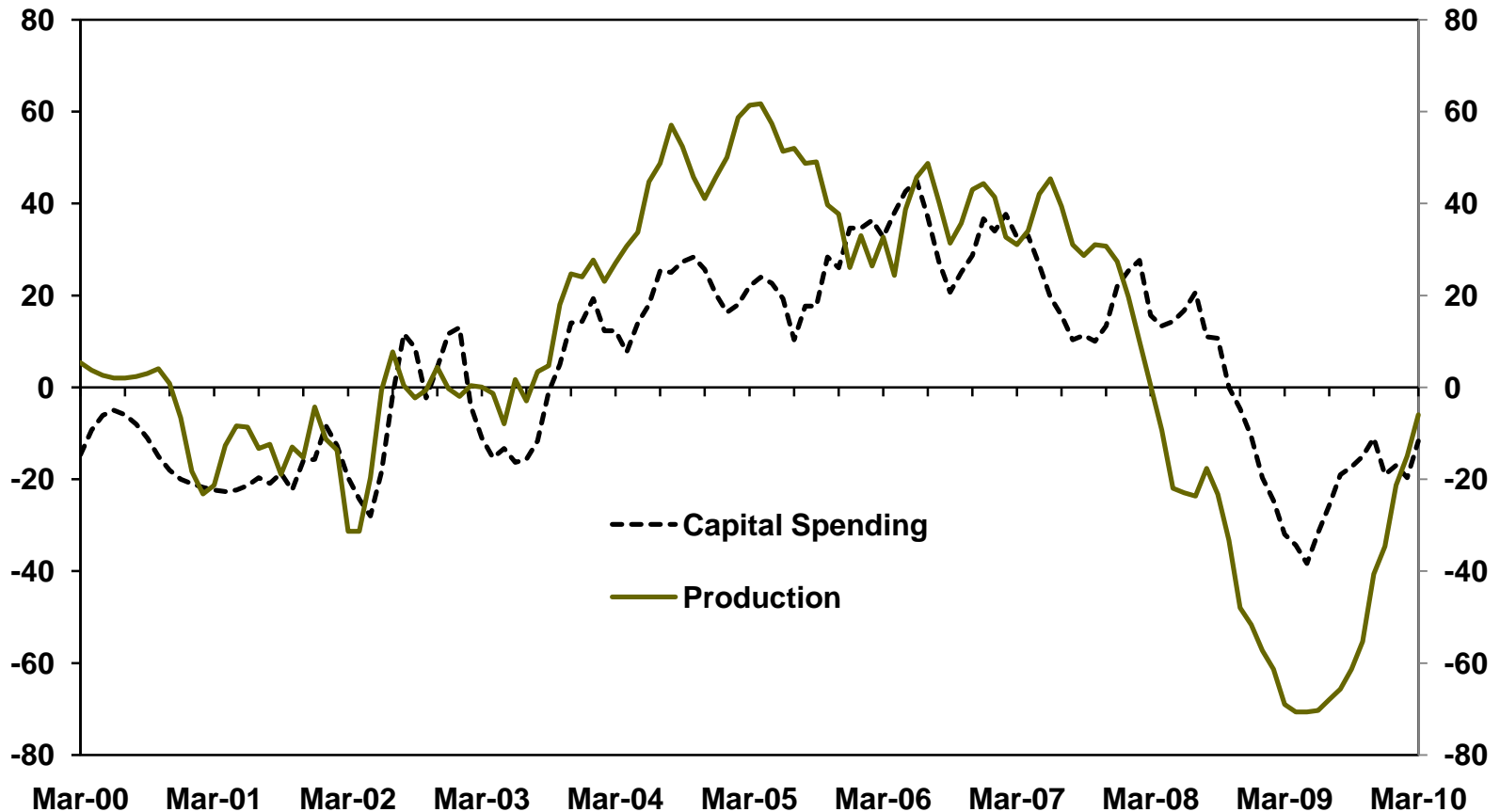
U.S. industrial production is rising, but much excess capacity remains

U.S. Industrial Production Index
Seasonally Adjusted



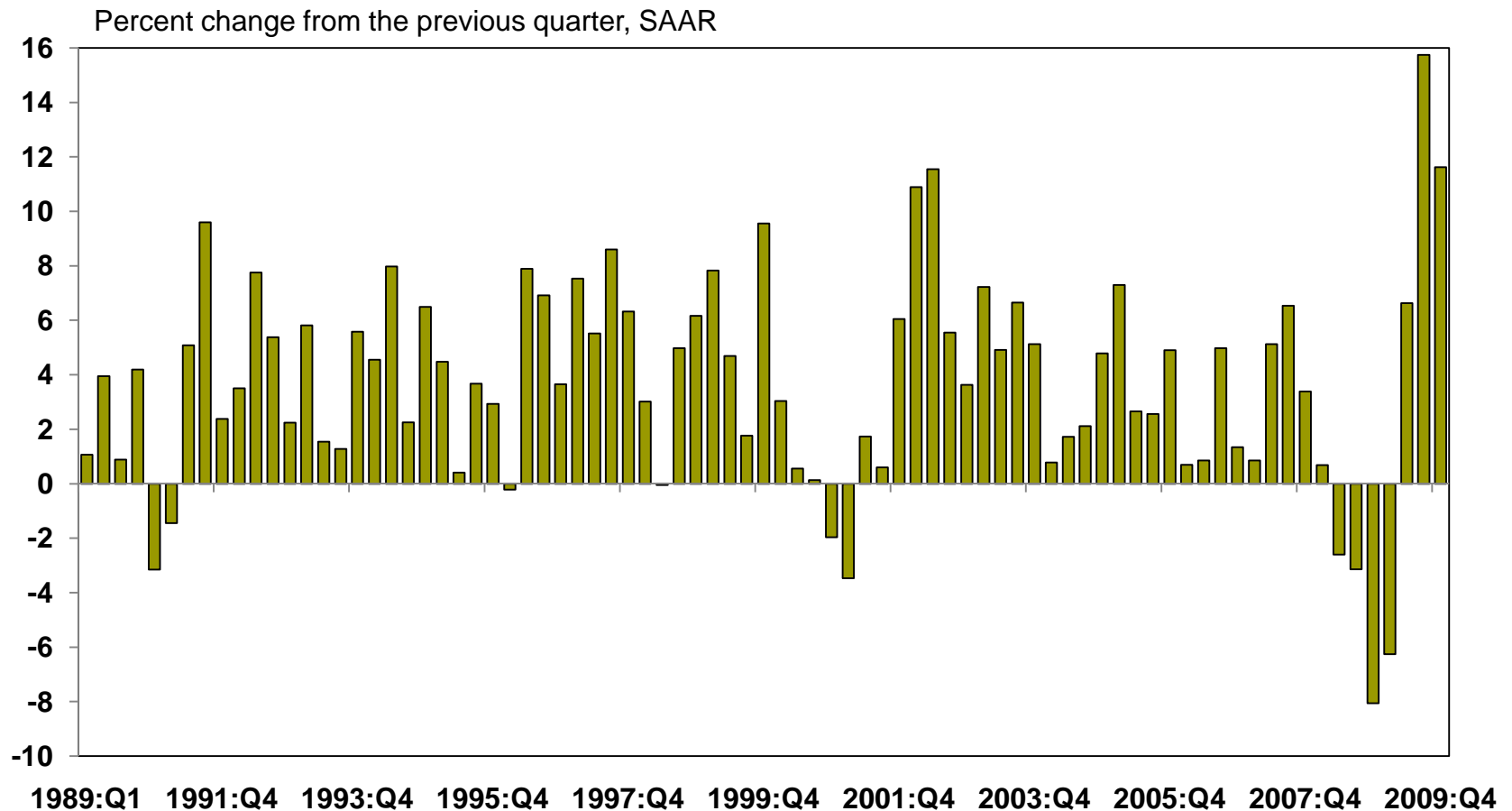
Factory activity in Kansas has also resumed growth, but remains below year-ago levels

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



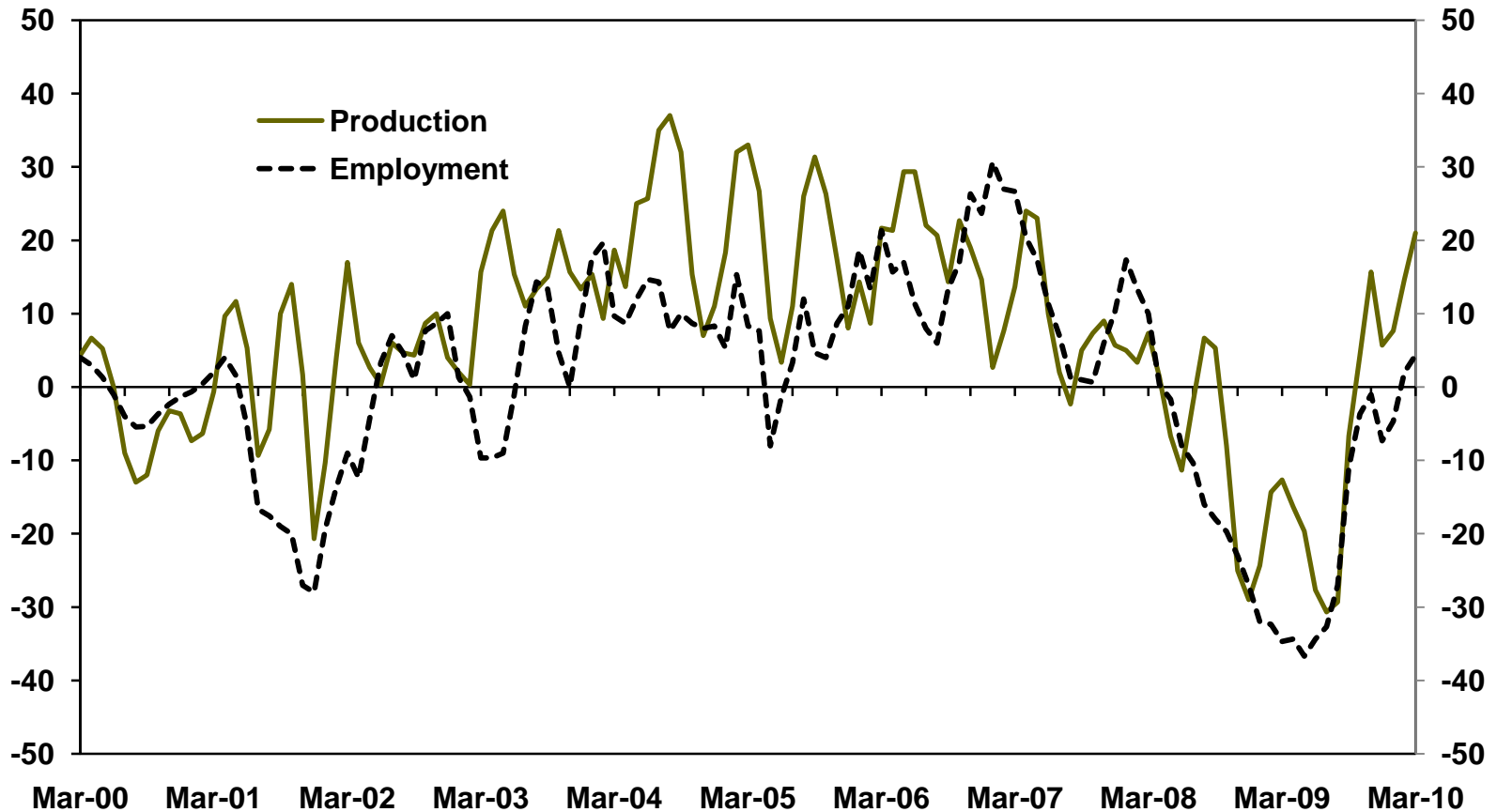
Recent U.S. productivity growth has been sizable, suggesting hiring could begin soon

U.S. Manufacturing Sector Productivity Growth



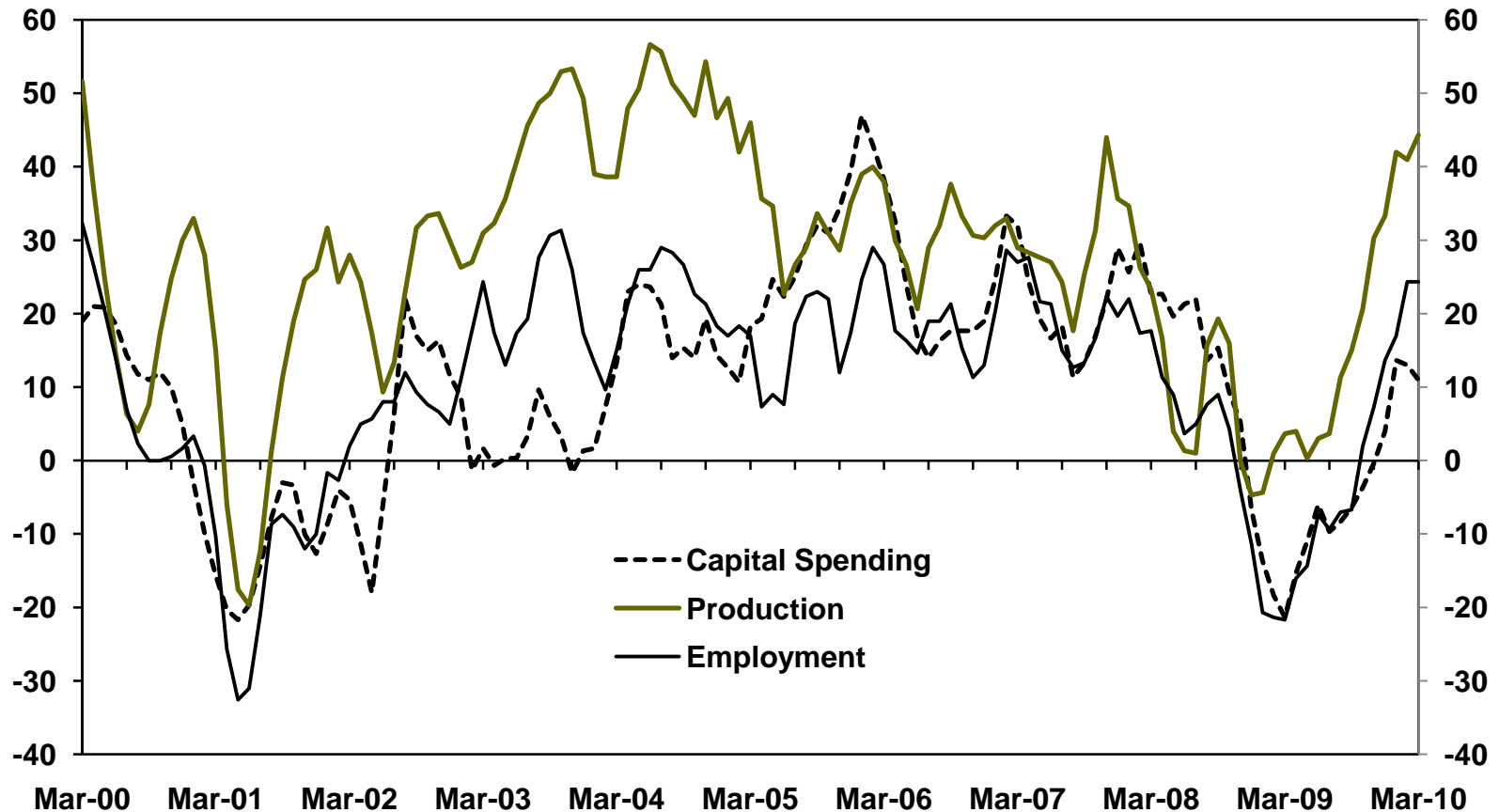
Rough measures of Kansas factory productivity have also risen in recent months

Kansas Manufacturing Indexes
Month-over-month, seasonally adjusted



Kansas production and hiring plans are increasing, but capex plans remain modest

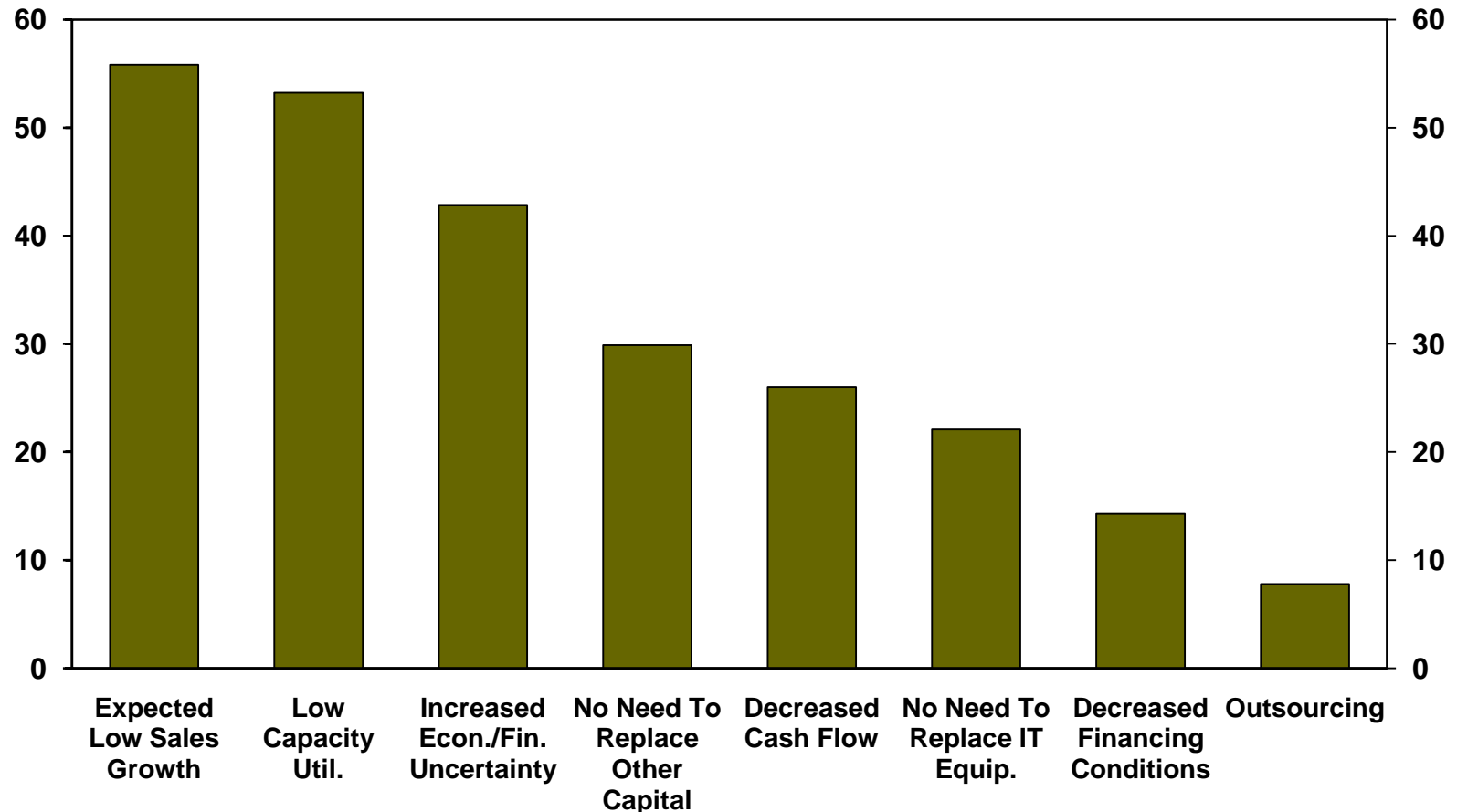
Kansas Manufacturing Indexes
Six-month ahead, 3-month moving avg.



Uncertainty about future conditions is a bigger reason than in the past for lower capex

Top Reasons for Not Increasing Capital Spending

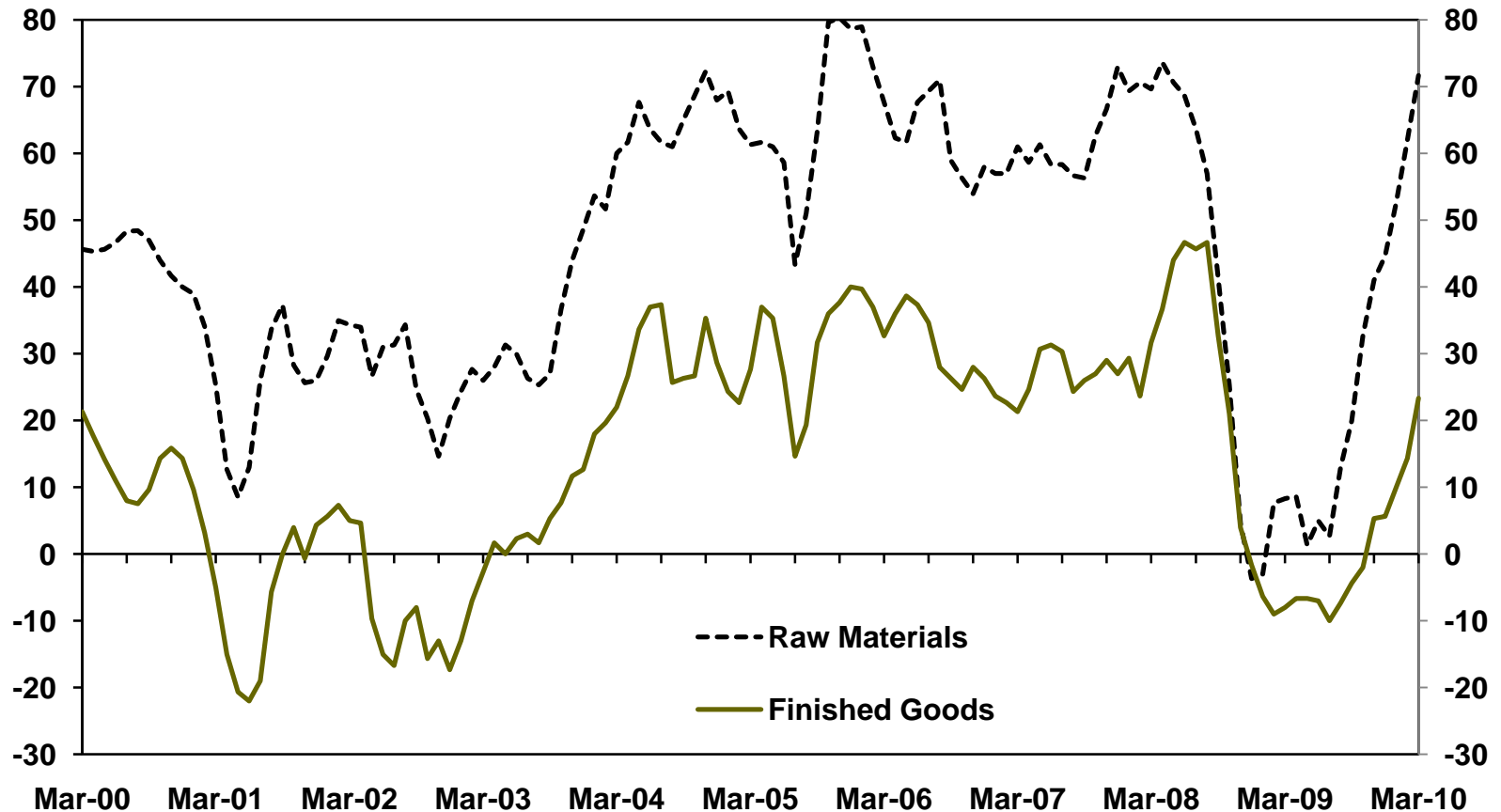
Share of firms choosing each reason, Jan. 2010



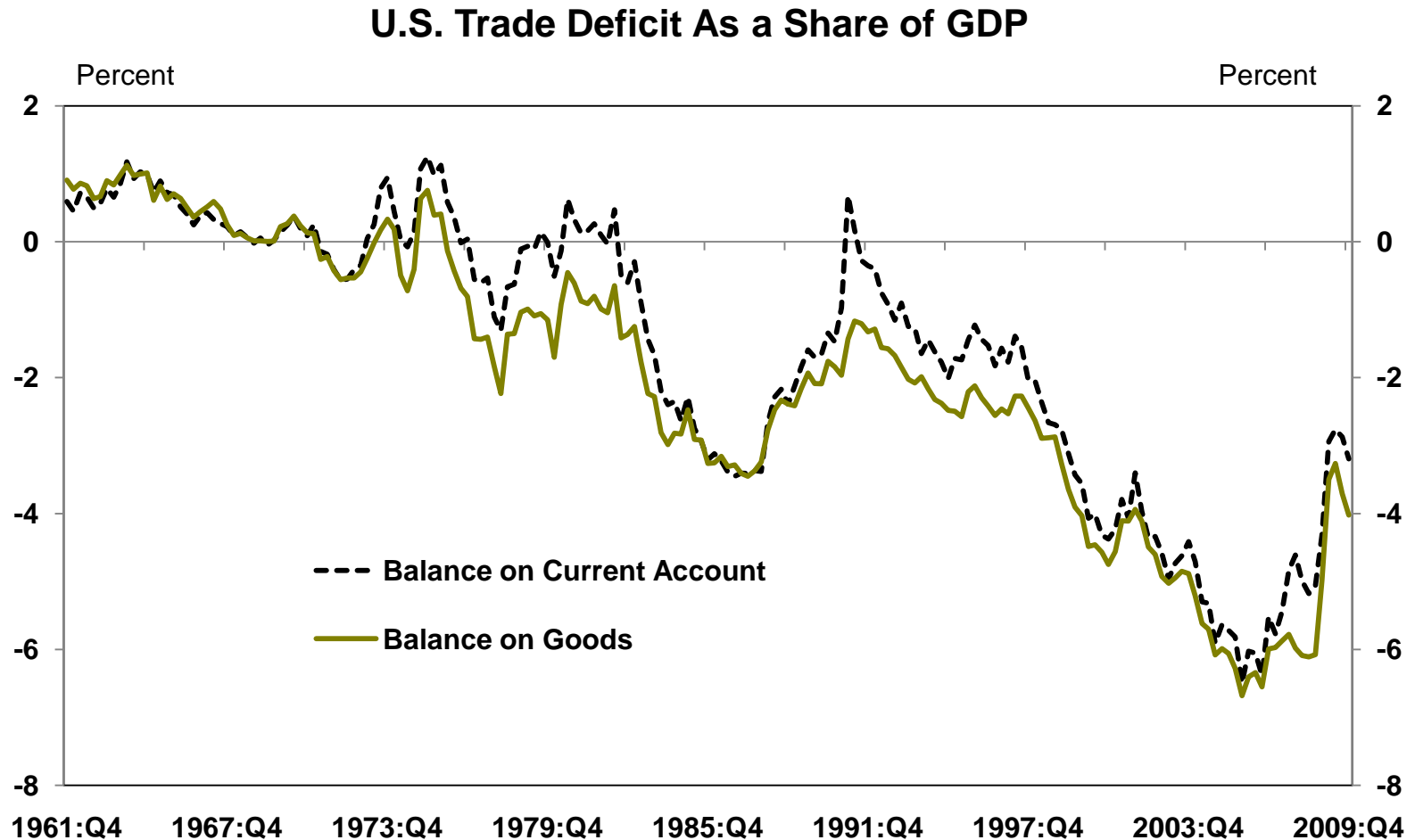
Pricing power may be another challenge, though some Kansas firms are raising prices

Kansas Manufacturing Price Indexes

Six-month ahead, 3-month moving avg.



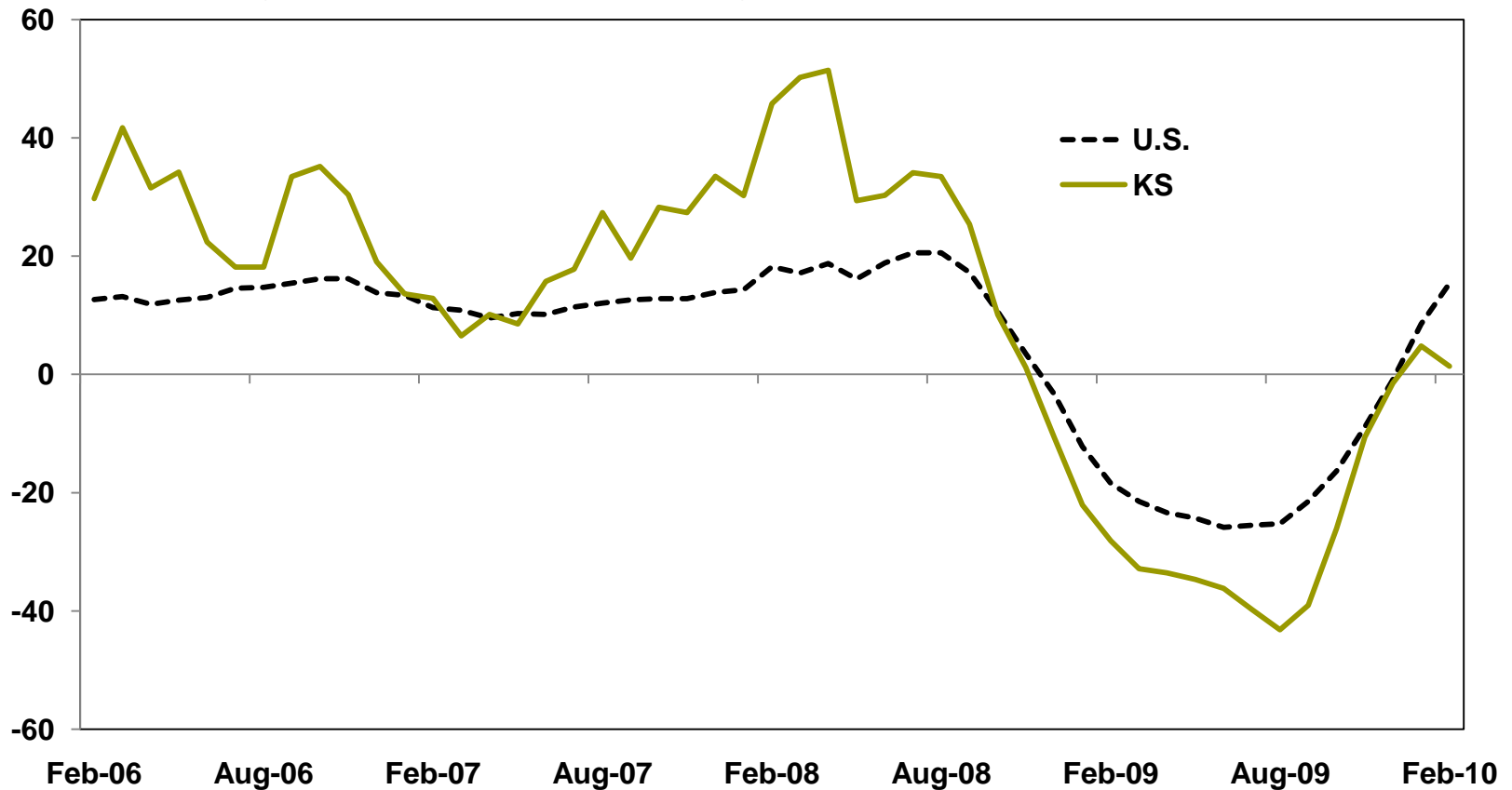
Longer-term, the U.S. trade imbalance provides opportunities for manufacturing



Kansas exports have edged higher in recent months following sharp declines in 2009

Merchandise Exports

Percent change year-over-year, 3-month mov. avg.



Summary

- The U.S. economy is growing again, but recovery speed is expected to be modest
- The Kansas economy is stabilizing, at a better level than in the nation
- Manufacturing activity is rising again in the nation and state, but some caution remains