

# Economic Trends

June 2008

(Covering May 9, 2008, to June 12, 2008)

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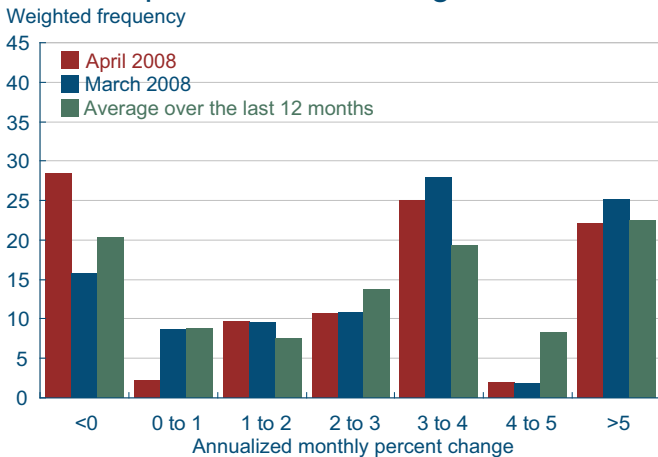
# April Price Statistics

## April Price Statistics

	Percent change, last					2007 avg.
	1mo. <sup>a</sup>	3mo. <sup>a</sup>	6mo. <sup>a</sup>	12mo.	5yr. <sup>a</sup>	
<b>Consumer Price Index</b>						
All items	2.5	2.3	4.5	3.9	3.2	4.2
Less food and energy	1.3	1.2	2.2	2.3	2.2	2.4
Median <sup>b</sup>	2.9	2.4	3.1	3.1	2.7	3.1
16% trimmed mean <sup>b</sup>	2.7	2.5	3.0	2.8	2.5	2.8
<b>Import Price Index</b>						
All commodities	23.9	21.3	20.4	15.4	7.2	11.5
Nonpetroleum imports	13.7	11.8	9.7	6.2	3.0	3.1
<b>Export Price Index</b>						
All commodities	4.0	11.8	11.4	7.7	4.5	6.1

a. Annualized.  
 b. Calculated by the Federal Reserve Bank of Cleveland.  
 Sources: U.S. Department of Labor, Bureau of Labor Statistics; and Federal Reserve Bank of Cleveland.

## CPI Component Price Change Distributions



Sources: U.S. Department of Labor, Bureau of Labor Statistics.

05.21.08

Michael F. Bryan and Brent Meyer

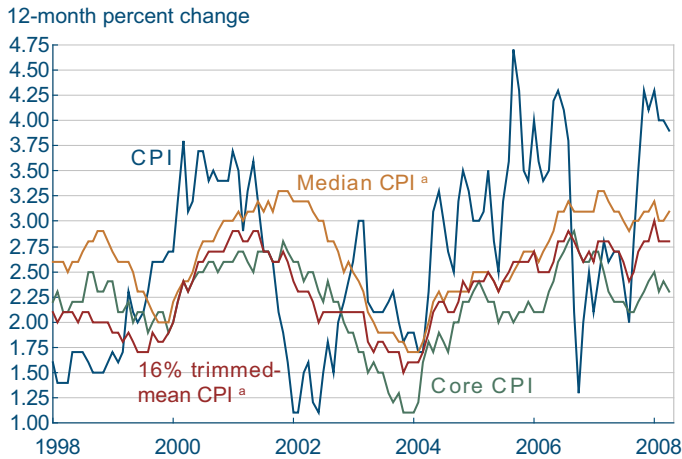
The Consumer Price Index (CPI) rose at an annualized rate of 2.5 percent in April, following a 4.2 percent increase in March. The CPI was pushed up by an 11.9 percent jump in food prices that was tempered by a curious 20.8 percent fall in motor fuel prices and a 20.1 percent decrease in the price of lodging away from home. Over the past six months, the CPI has risen 4.5 percent (annualized rate). Consumer prices excluding food and energy increased slightly in April, rising only 1.3 percent after an increase of 1.8 percent in March. In contrast to the rather well-behaved headline and core price indexes, the median and 16 percent trimmed-mean CPI measures rose 2.9 percent and 2.7 percent, respectively.

Digging deeper into the components that comprise the CPI, we can see that nearly 50 percent of the market basket rose at rates exceeding 3.0 percent in April, down slightly from 55 percent last month, but in line with price changes over the past 12 months. Also, 28 percent of the CPI components posted a decrease in price during the month, compared to 16 percent in March and an average of 20 percent over the past 12 months.

Longer-term trends in both headline and core CPI have been falling since the first of the year, but remain elevated. The 12-month growth rate in the CPI fell from 4.3 percent in January to 3.9 percent in April, while the core CPI ticked down 0.2 percentage point to 2.3 percent. However, the longer-term trends in both of the trimmed-mean measures have lingered near their January values.

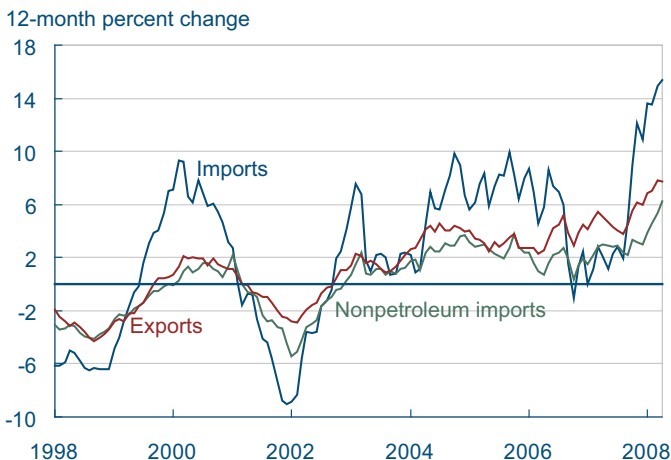
Import prices continued to surge ahead in April, rising 23.9 percent (annualized rate), following an upwardly revised 40.9 percent jump in March. Over the past three months, import prices are up 21.3 percent. Petroleum import prices are continuing to soar—up 66.9 percent in April and 187.9 percent in March—though the rise in import prices

## CPI, Core CPI, and Trimmed-Mean CPI Measures



a. Calculated by the Federal Reserve Bank of Cleveland.  
Sources: U.S. Department of Labor, Bureau of Labor Statistics, and Federal Reserve Bank of Cleveland.

## Import and Export Price Indexes

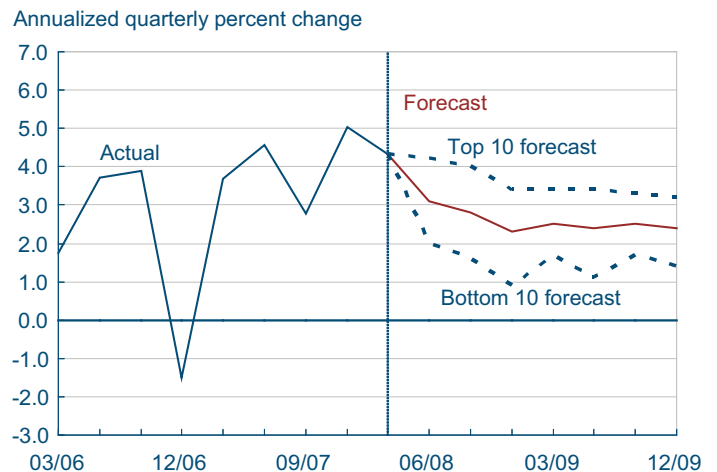


Source: Bureau of Labor Statistics.

appears to be relatively broad-based. Nonpetroleum imports rose 13.7 percent, a month after posting their largest increase on record (13.9 percent). Nonpetroleum import prices have shot up 6.2 percent over the past 12 months. Export prices increased 4.0 percent in April, following double-digit monthly gains over the past three months, and are up 7.7 percent over April of last year.

Looking forward, the Blue Chip Consensus forecast has consumer prices falling to 2.4 percent by the end of 2009, although these projections were made before the April price reports. Thirty of the fifty forecasters surveyed revised their 2008 inflation forecasts upward in May from last month, as commodity and energy prices continued to rise.

## CPI and Forecasts



Sources: Blue Chip panel of economists, May 10, 2008.

## Money, Financial Markets, and Monetary Policy

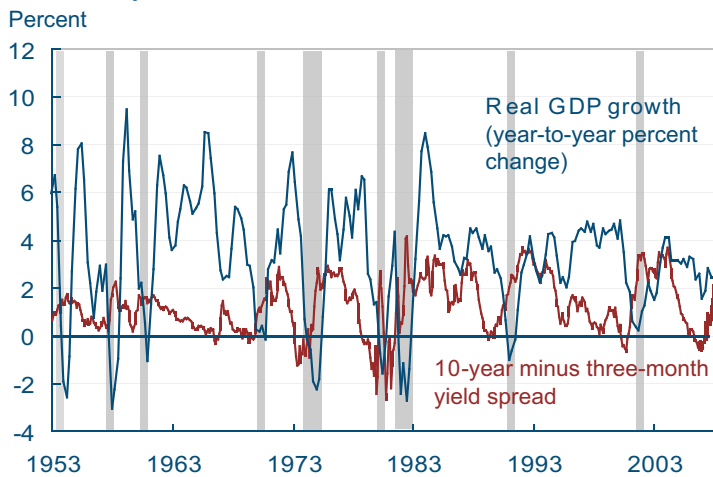
### The Yield Curve

05.13.08

by Joseph G. Haubrich

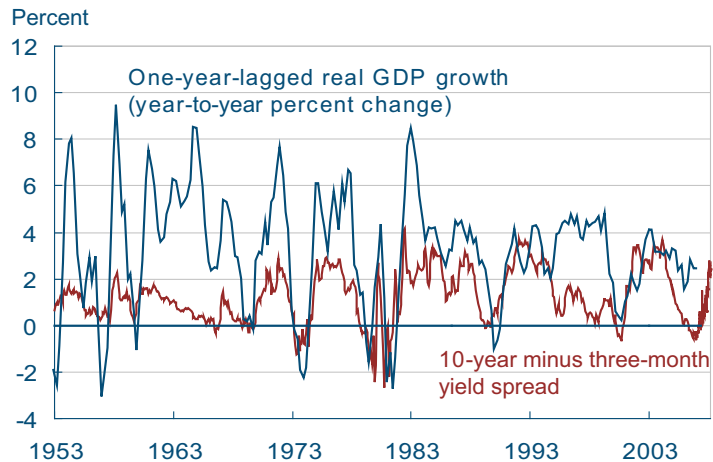
Since last month, the yield curve has witnessed a parallel upward shift, with both short-term and long-term interest rates rising. One reason for noting this is that the slope of the yield curve has achieved some notoriety as a simple forecaster of economic growth. The rule of thumb is that an inverted yield curve (short rates above long rates) indicates a recession in about a year, and yield curve inversions have preceded each of the last six recessions (as defined by the NBER). Very flat yield

## Yield Spread versus Real GDP Growth



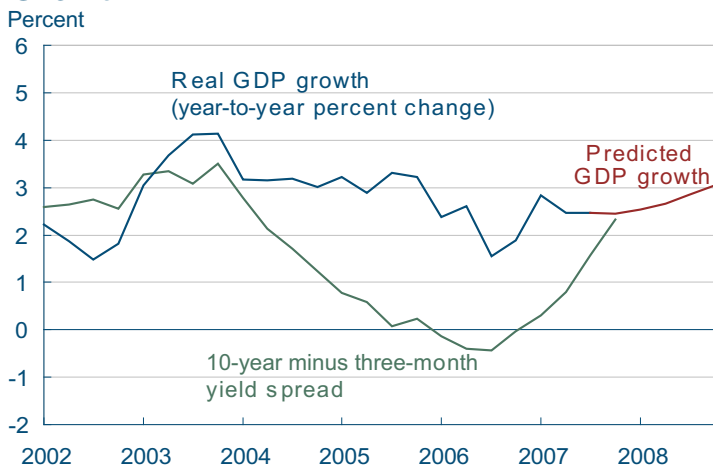
Note: Shaded bars represent recessions.  
Sources: Bureau of Economic Activity; Federal Reserve Board.

## Yield Spread versus One-Year-Lagged Real GDP Growth



Sources: Bureau of Economic Analysis; Federal Reserve Board.

## Yield Spread versus Predicted GDP Growth



Sources: Bureau of Economic Analysis; Federal Reserve Board.

curves preceded the previous two, and there have been two notable false positives: an inversion in late 1966 and a very flat curve in late 1998. More generally, though, a flat curve indicates weak growth, and conversely, a steep curve indicates strong growth. One measure of slope, the spread between 10-year bonds and 3-month T-bills, bears out this relation, particularly when real GDP growth is lagged a year to line up growth with the spread that predicts it.

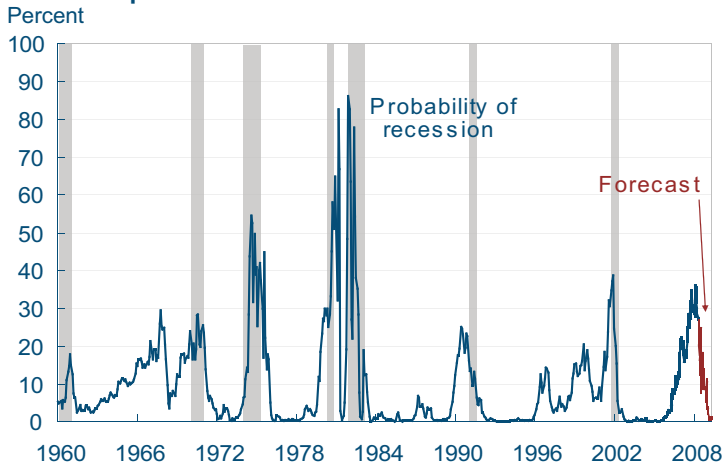
The yield curve slope stayed the same, with both long and short rates edging up. The spread remains positive, with the 10-year rate moving up 31 basis points to 3.85 percent, and the 3-month rate up the same to 1.64 percent (both for the week ending May 9). Standing at 221 basis points, the same as April's 221, the spread is above March's 214 basis points. Projecting forward using past values of the spread and GDP growth suggests that real GDP will grow at about a 3.0 percent rate over the next year. This is on the high side of other forecasts.

While such an approach predicts when growth is above or below average, it does not do so well in predicting the actual number, especially in the case of recessions. Thus, it is sometimes preferable to focus on using the yield curve to predict a discrete event: whether or not the economy is in recession. Looking at that relationship, the expected chance of the economy being in a recession next May stands at 0.9 percent, just below April's 1 percent, and March's 2.7 percent.

The probability of recession is below several recent estimates, and perhaps seems strange in the midst of recent financial concerns. But one aspect of those concerns has been a flight to quality, which lowers Treasury yields. Also related is the reduction of the federal funds target rate and the discount rate by the Federal Reserve, which tends to steepen the yield curve. Furthermore, the forecast is for where the economy will be next May, not earlier in the year.

On the other hand, a year ago, the yield curve was predicting a 35 percent chance that the US economy would be in a recession in May 2008, a number that seemed unreasonably high at the time. To compare the 0.9 percent chance of a recession to

## Probability of Recession Based on the Yield Spread\*



\*Estimated using probit model.  
Note: Shaded bars indicate recessions.  
Sources: Bureau of Economic Analysis; Federal Reserve Board; author's calculations

some other probabilities and learn more about different techniques of predicting recessions, head on over to the Econbrowser blog.

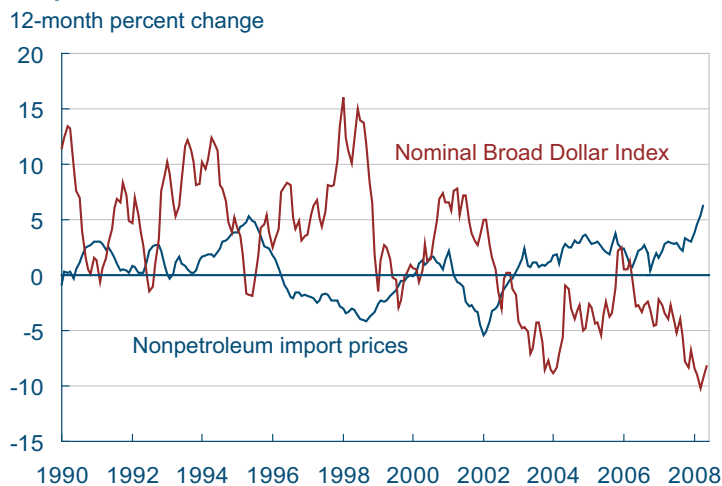
Of course, it might not be advisable to take this number quite so literally, for two reasons. First, this probability is itself subject to error, as is the case with all statistical estimates. Second, other researchers have postulated that the underlying determinants of the yield spread today are materially different from the determinants that generated yield spreads during prior decades. Differences could arise from changes in international capital flows and inflation expectations, for example. The bottom line is that yield curves contain important information for business cycle analysis, but, like other indicators, should be interpreted with caution.

For more detail on these and other issues related to using the yield curve to predict recessions, see the Commentary “Does the Yield Curve Signal Recession?”

## International Markets

### Exchange-Rate Pass-Through to Import Prices

#### Import Prices and the Value of the Dollar



Source: Board of Governors of the Federal Reserve System; Bureau of Labor Statistics

06.11.08

by Owen F. Humpage and Michael Shenk

A dollar depreciation—like the broad-based, 26 percent one that we have experienced since February 2002—tends to raise the dollar price of all goods and services imported into the United States. Typically, however, less than the full amount of a dollar depreciation gets passed through to the dollar prices of imports. Interestingly, the amount of pass-through, both in the United States and other industrial countries, seems to have declined along with the level and volatility of worldwide inflation.

Most firms engaged in international trade do not conform closely with the economists' ideal of being perfectly competitive. Firms exporting to the United States typically can mark up their home-currency prices above their marginal costs and earn significant economic profits. Such firms can—and most likely will—react to a dollar depreciation by cutting their profit margins, at least temporarily, to protect their U.S. market share. As a consequence,

U.S. consumers often will not see the full percentage of a dollar depreciation reflected in dollar-denominated import prices.

How much of the exchange-rate depreciation eventually gets passed through to dollar import prices depends on myriad industry-specific things that influence the responsiveness of demand and production costs to price and output changes. In addition, the size and expected duration of an exchange-rate change, as well as its direction, seem important. As one might then expect, estimates of pass-through at the industry level show a great deal of variation.

Likewise, estimates of pass-through for the overall economy show wide variation, so much so that we find it hard to specify their central tendency. Going out of a limb—and it's a slim one at that—pass-through in the United States seems to have been less than 60 percent on average since the inception of floating exchange rates in 1973. Moreover, pass-through in the United States seems low relative to other industrialized countries.

While specifying a central tendency for pass-through in the United States is difficult, the evidence seems to indicate more clearly that U.S. pass-through has fallen by roughly one-half during the 1990s. Researchers note a similar pattern in many other industrialized countries.

In part, this might just reflect changes in the composition of U.S. imports, away from industries that traditionally have had a high rate of pass-through to industries that traditionally have had a low rate of pass-through. In part, the declining rate of pass-through might reflect growing facilities for hedging exposures to unanticipated exchange-rate changes.

Yet, two other explanations seem to loom large. One is China's growing influence in world markets. Because China pegged the renminbi to the dollar until 2005 and has since managed the renminbi's movements, the dollar's depreciation since 2002 has had less of a negative effect on China's competitiveness than it has had on many other nation's trade positions. Foreign firms may cut their price mark-ups more readily when they face Chinese competition.

The other—the dominant—explanation for a declin-

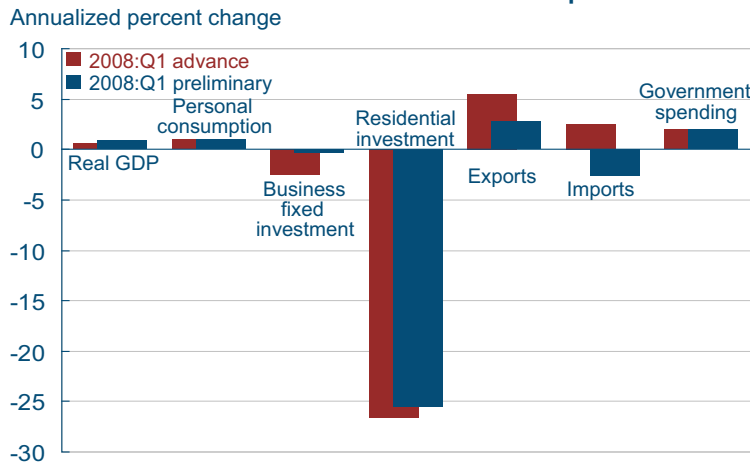
ing rate of pass-through contends that in an environment of low and stable inflation, foreign firms are more reluctant to pass through exchange-rate changes into dollar prices. International trading firms, despite having some pricing power, often face a cost to changing prices, in large part because price changes encourage customers to look elsewhere. Such firms will only change prices when the gains from doing so exceed the costs, so they will delay until they find that the exchange-rate change is substantial and permanent. In a high-inflation environment, permanent depreciations are more likely and the rising overall price level can quickly negate relative pricing errors. Real GDP First-Quarter 2008 Preliminary Estimate

## Economic Activity and Labor Markets

# Real GDP First-Quarter 2008 Preliminary Estimate

06.03.08  
by Brent Meyer

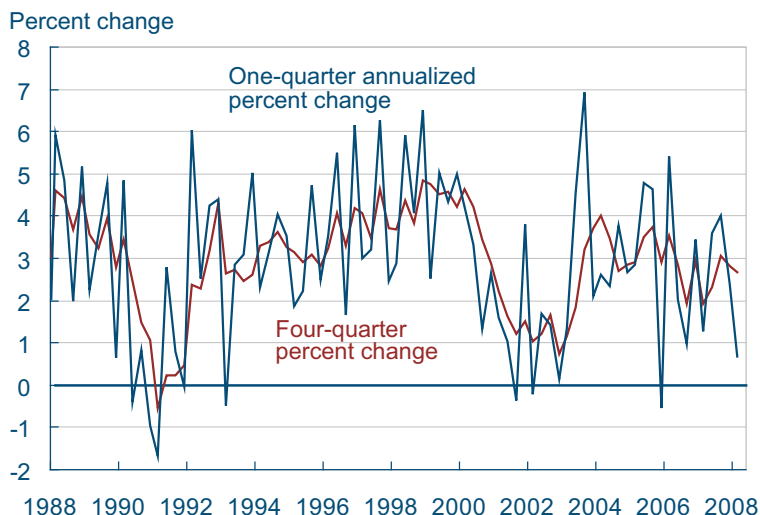
## Revisions to Real GDP and Components



Source: Bureau of Economic Analysis.

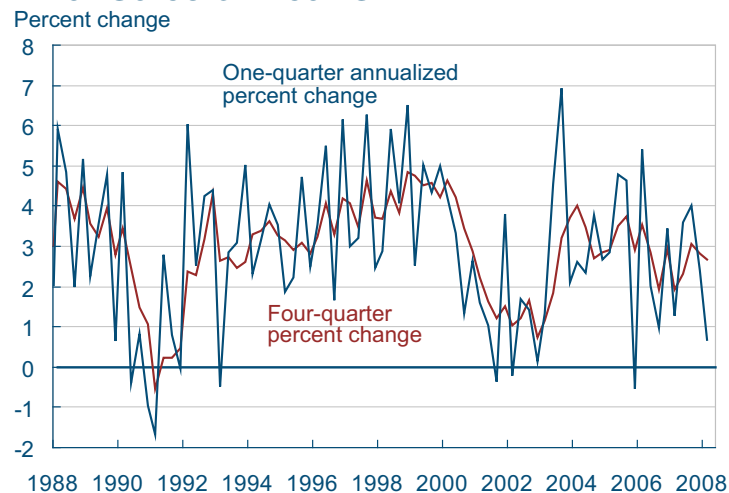
Real (inflation-adjusted) GDP increased at an annualized rate of 0.9 percent in the first quarter, according to the preliminary estimate from the Bureau of Economic Analysis (BEA), up 0.3 percentage point from the advance estimate. The magnitude of this revision is consistent with the long-term trend for revisions from the advance to preliminary release: From 1983 to 2004, the average revision has been 0.2 percentage point (the absolute average was 0.5 percentage point and the standard deviation was 0.4 percentage point). The latest revision was primarily due to upward adjustments to nondurable consumer spending, nonresidential fixed investment, and net exports, which were tempered by downward corrections to private inventory investment and consumer spending on services. Nondurable consumer spending was revised up from -1.3 percent to -0.3 percent in the first quarter, while 0.4 percentage point were trimmed off consumer spending on services, negating any effect on overall consumption. Nonresidential investment in structures was adjusted up from -6.2 percent to 1.1 percent. While export growth was revised down from 5.5 percent to 2.8 percent in the first quarter, import growth fell further, from

## Final Sales of Real GDP



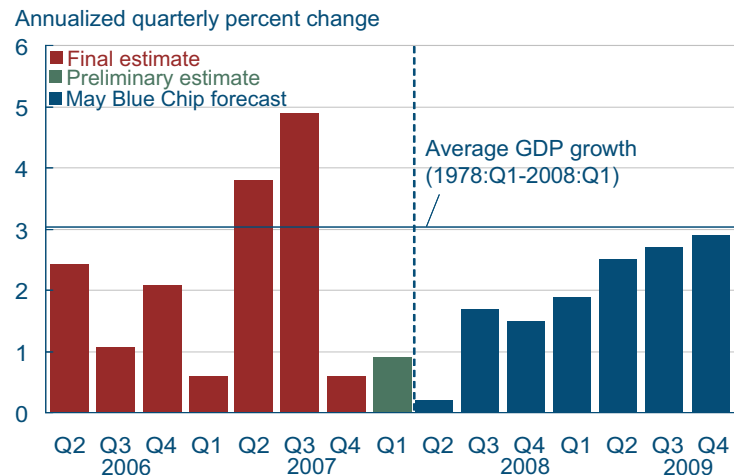
Source: Bureau of Economic Analysis.

## Final Sales of Real GDP



Source: Bureau of Economic Analysis.

## Real GDP Growth



Sources: Blue Chip Economic Indicators, May 2008; Bureau of Economic Analysis.

of 2.5 percent to -2.6 percent.

An investigation into each component's contribution to the percent change in real GDP yields some interesting results. Most notably, a downward revision to private inventories—from an accumulation of \$20.1 billion to just \$3.9 billion—subtracted 0.6 percentage point from growth. The advanced estimate for the first quarter had private inventories adding 0.8 percentage point to growth, keeping GDP out of the red. Changes in private inventories can have muddling effects on the interpretation of GDP, which is why it may be useful to look at final sales of GDP.

The final-sales-of-real-GDP statistic is basically real GDP excluding inventories. It gives us a clearer picture of demand by adding together consumer, business, and government spending. It also may provide an early warning sign of turning points in the economy. The story is that if final sales growth is less than overall GDP growth (for some period of time), inventories will begin to accumulate and that will cause businesses to slow or halt production. This results in an impending slowdown or recession. According to the advance estimate, final sales of real GDP for the first quarter dipped below zero for the first time since the fourth quarter of 2005, falling 0.2 percent (at an annualized rate). However, after the first revision, final sales grew 0.7 percent in the first quarter, taking some wind out of the recession argument (for the moment). On a year-over-year basis, final sales of real GDP ticked down from 2.8 percent last quarter, to 2.7 percent currently.

The Blue Chip consensus economic forecast is predicting that the economy will grow a shade above zero next quarter, before snapping back in the third quarter and rising to near trend growth by the end of 2009. Of the 50 forecasters surveyed, nearly half revised up their 2008 GDP forecast from the April survey. On the other hand, 30 forecasters revised their 2009 GDP outlook down.



## Labor Turnover and Employment in Different U.S. Regions

### Job Openings and Turnover, Regional Monthly Averages (thousands)

	Midwest	Northeast	South	West	U.S.
Hires	1,020	745	1,753	1,047	4,565
Separations	990	718	1,669	1,016	4,392
Job openings	731	617	1,362	821	3,530
Net hires	30	28	85	30	173

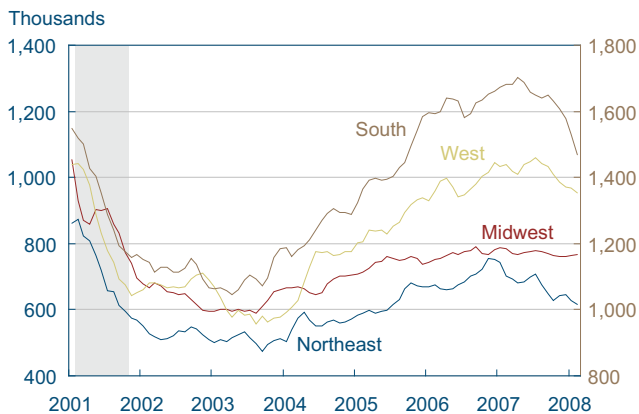
Note: The averages represent monthly JOLTS data since December 2000, when the series began.  
Source: Bureau of Labor Statistics.

### Job Openings and Turnover, Regional Shares of U.S. Total

	Midwest	Northeast	South	West	U.S.
Hires	.223	.163	.384	.229	1.00
Separations	.225	.163	.380	.231	1.00
Job openings	.207	.175	.386	.232	1.00
Net hires	.175	.161	.489	.176	1.00
Employment	.236	.190	.355	.219	1.00

Note: The averages represent monthly JOLTS data since December 2000, when the series began.  
Source: Bureau of Labor Statistics.

### Job Openings



Notes: Seasonally-adjusted, 3-month moving averages. The shaded bar represents a recession.  
Source: Bureau of Labor Statistics.

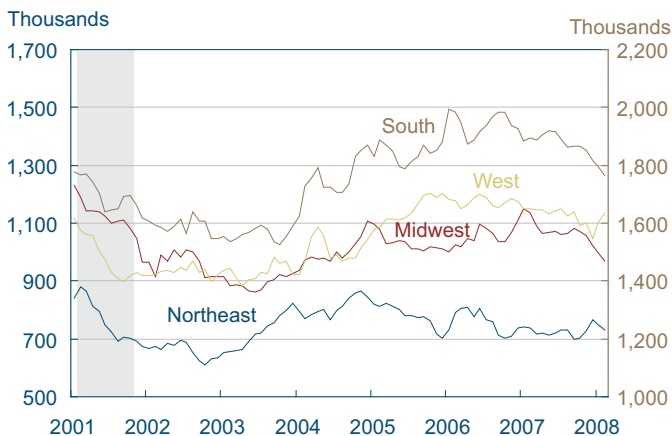
06.03.08

by Murat Tasci and Beth Mowry

The Bureau of Labor Statistics (BLS) provides labor turnover and vacancy data for four broad census regions (the Midwest, Northeast, South, and West) and the entire nation as part of its Job Openings and Labor Turnover Survey (JOLTS). According to these data, which begin in December 2000, there is significant variation in the way labor turnover behaves in the different regions. In the Northeast, for instance, employers hired an average of 745,000 workers a month, while in the South it was more than 1.7 million. Similarly, the South has accounted for most of the job openings and separations over the past eight years, whereas the Northeast lagged behind other regions.

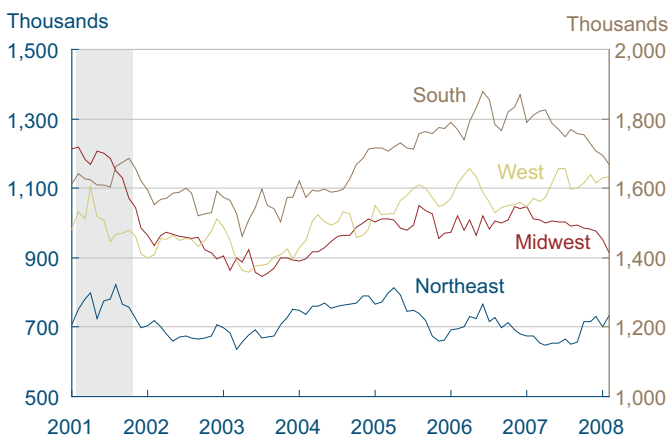
These figures should not be surprising given the South's greater employment numbers: Since 2001, average total employment in the South has accounted for about 35.5 percent of U.S. nonfarm payroll employment, compared to 23.6 percent for the Midwest, 21.9 percent for the West, and 19 percent for the Northeast. But the curious behavior emerges when we look at each region's share of various categories of labor turnover. The contribution of the South is greater than its employment share in virtually every category. Its share of hires, separations, and job openings are all about 38 percent of the U.S. total. The West shows a similar pattern, although much less pronounced. The Northeast, on the other hand, seems to have contributed less than its employment share in all measures of labor turnover and job openings. The Midwest presents a balanced picture in terms of hires and separations. Its share of job openings, however, has been lagging significantly behind its employment share. As a result, the South's employment share has grown over this period (from 35 percent to 36 percent), more rapidly than the West (from 21.5 percent to 22.2 percent), whereas that of Northeast and Midwest have been shrinking somewhat (from 19.2 percent to 18.5 percent and from 24 percent to 23 percent, respectively).

## Hires



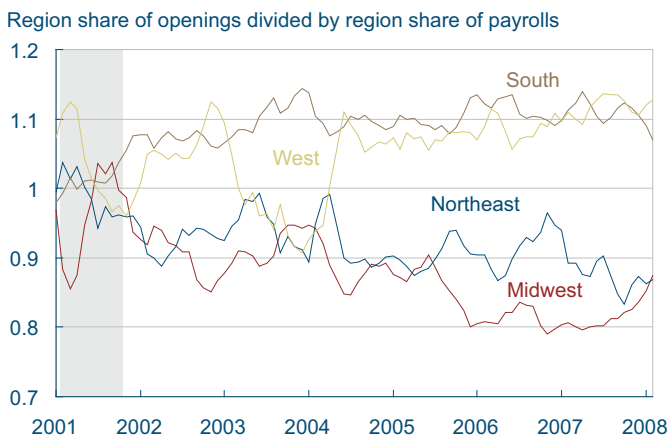
Notes: Seasonally-adjusted, 3-month moving averages. The shaded bar represents a recession.  
Source: Bureau of Labor Statistics.

## Separations



Note: Seasonally-adjusted, 3-month moving averages.  
Source: Bureau of Labor Statistics.

## Proportion of U.S. Job Openings



Notes: Seasonally-adjusted data. The shaded bar represents a recession. Proportions represent regional shares of openings divided by regional shares of payrolls. Proportions greater than 1.0 imply that a region has a disproportionately higher share of openings compared to the United States as a whole.  
Source: Bureau of Labor Statistics.

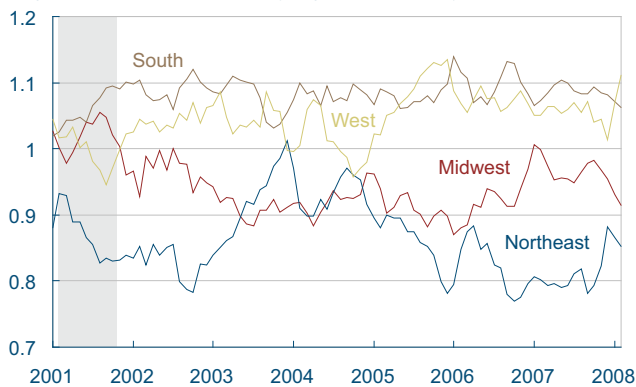
Time series data on turnover and job openings reveal some interesting similarities and differences across regions as well. During the last recession, for example, all four regions experienced sharp declines in job openings. Even though each region started to recover later, only in the South and West had job openings reached their pre-recession levels by 2007. Interestingly, in the Midwest, job openings have been virtually flat for the past three years.

Hiring activity also declined in all four regions during the last recession. Once again, although each region had begun to recover by the end of 2003, hiring remained below pre-recession levels in the Midwest and Northeast. This picture, in conjunction with the separations data, implies that job reallocation has declined in the Northeast and Midwest over time. While high levels of separations and hiring could be inefficient if resources are being spent unnecessarily to reallocate workers across different firms, regions, and states, they could also indicate an active search by both workers and firms to find their best matches in the labor market.

Each region's relative shares could give further interesting details about regional labor markets. To this end, we construct relative shares of labor turnover and job openings for all four regions, adjusting each for the region's employment share. This is basically a ratio of two shares: the share of a region's job openings, hires, or separations over the share of a region's employment. So, for example, a ratio for hires greater than 1 for a particular region means it is hiring a higher number of workers than the U.S. average. Several features of the data stand out when interpreted in this way: First, the South leads U.S. averages in all dimensions. Second, regional job openings in the Midwest relative to the U.S. have been the lowest among the four regions. Its job openings rate has been around 20 percent below the average for the past two years. Interestingly, the Midwest looks like an average region when it comes to hiring and separations. In particular, separations are not disproportionately higher than the US average in the Midwest. Finally, the West stands out as a region that has a separation rate at least 30 percent below average during our sample period. Even though both the South and the West have the highest average hiring for the United States, the

## Proportion of U.S. Hires

Region share of hires divided by region share of payrolls

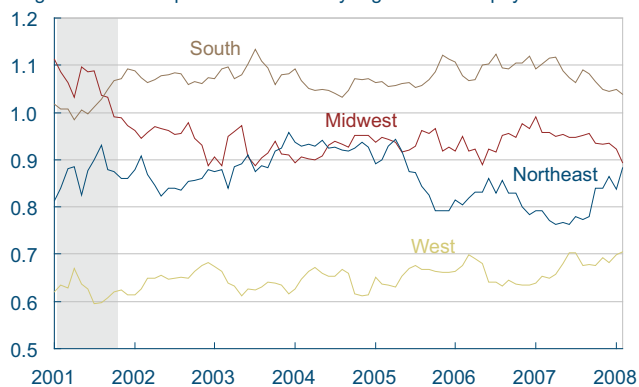


Notes: Seasonally-adjusted data. The shaded bar represents a recession. Proportions represent regional shares of hires divided by regional shares of payrolls. Proportions greater than 1.0 imply that a region has a disproportionately higher share of hires compared to the United States as a whole.

Source: Bureau of Labor Statistics.

## Proportion of U.S. Separations

Region share of separations divided by region share of payrolls



Notes: Seasonally-adjusted data. The shaded bar represents a recession. Proportions represent regional shares of separations divided by regional shares of payrolls. Proportions greater than 1.0 imply that a region has a disproportionately higher share of separations compared to the United States as a whole.

Source: Bureau of Labor Statistics.

## Job Openings and Turnover, Regional Shares of U.S. Total

	U.S.	Midwest	Northeast	West	West
U.S.	1	.58	.77	.81	.75
Midwest		1	.24	.29	.29
Northeast			1	.55	.47
South				1	.42
West					1

Note: The averages represent monthly JOLTS data since December 2000, when the series began.

Source: Bureau of Labor Statistics.

West is distinguished by lower reallocation due to lower separations than the South.

Each region's net employment creation (hires minus separations) is significantly positively correlated with the U.S. total. This means that growth in total payrolls is associated with an increase in payrolls in the different regions. The correlation is highest for the South, another sign that is consistent with this region's leading role in employment creation. However, the correlations between the different regions are not very strong. Net employment creation in the Midwest has the lowest correlation with the other regions. This low correlation seems to stem from the low correlation of separations with other regions, not hires. This might indicate a structural change that is affecting only the Midwest, resulting in a regional labor market that does not follow the rest of the country.

## JOLTS Regions

The states of the Midwest region are: ND, SD, NE, MN, KS, IA, MO, WI, IL, IN, MI, and OH.

The states of the Northeast region are: ME, NH, MA, VT, RI, CT, NJ, NY, and PA.

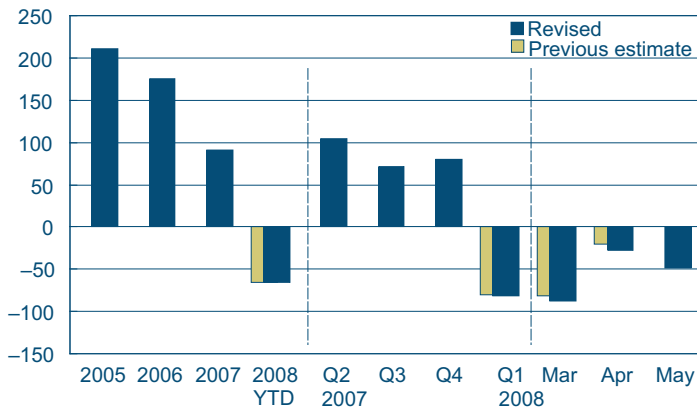
The states of the South region are: TX, OK, AR, LA, MS, AL, TN, KY, WV, VA, DE, MD, DC, NC, SC, GA, and FL.

The states of the West region are: WA, OR, CA, MT, ID, WY, NV, UT, CO, AZ, NM, HI, and AK.

# The Employment Situation

## Average Nonfarm Employment Change

Change, thousands of jobs



Source: Bureau of Labor Statistics.

06.06.08

by Murat Tasci and Beth Mowry

Nonfarm payrolls fell for the fifth consecutive month in May, coming in at a slightly smaller-than-expected loss of 49,000. Along with the downward revisions for March and April (a total of 15,000), this figure brings the year-to-date monthly average loss in payroll employment to 65,000. The last time payrolls shrank for five consecutive months was in mid-2003. The Bureau of Labor Statistics (BLS) also reported today that the unemployment rate shot up from 5.0 percent to 5.5 percent, its sharpest increase in 22 years.

The job declines were broad-based, spreading beyond the usual housing-related sectors that have exhibited consistently poor performance in recent months. The only major sectors to add jobs last month were education and health services (54,000), leisure and hospitality (12,000), and the government (17,000). The goods-producing sector lost a total of 57,000 jobs, continuing along its 14-month path of decline. Service-providing industries added a very modest 8,000 jobs, much lower than April's addition of 72,000.

Within the goods-producing sector, manufacturing lost 34,000 jobs and construction lost 26,000. Durable goods manufacturing as a whole shed 19,000 jobs, largely due to losses in wood products (8,400) and computer and electronic products (7,500). The most positive contribution came from transportation equipment, which added 7,200 jobs, largely because of jobs added in the motor vehicles and parts subsector. The only small positives within nondurable goods came from paper and paper products (500) and chemicals (900).

## Labor Market Conditions

	Average monthly change (thousands of employees, NAICS)				
	2005	2006	2007	2008 YTD	May 2008
Payroll employment	211	175	91	-65	45
Goods-producing	32	3	-38	-79	-57
Construction	35	13	-19	-42	-34
Heavy and civil engineering	4	3	-1	-6	-3
Residential <sup>a</sup>	11	-2	-10	-28	-25.1
Nonresidential <sup>b</sup>	4	7	1	-7	-5.2
Manufacturing	-7	-14	-22	-41	-26
Durable goods	2	-4	-16	-30	-19
Service-providing	179	172	130	14	8
Retail trade	19	5	6	-30	-27.1
Financial activities <sup>c</sup>	14	9	-9	-4	-1
PBS <sup>d</sup>	56	46	26	-25	29
Temporary help svcs.	17	1	-7	-23	-29.6
Education and health svcs.	36	39	44	51	54
Leisure and hospitality	23	32	29	13	12
Government	14	16	21	15	17
Local educational svcs.	6	6	5	6	14.1
	Average for period (percent)				
Civilian unemployment rate	5.1	4.6	4.6	5.1	5.5

a. Includes construction of residential buildings and residential specialty trade contractors.

b. Includes construction of nonresidential buildings and nonresidential specialty trade contractors.

c. Includes the finance, insurance, and real estate sector and the rental and leasing sector.

d. PBS is professional business services (professional, scientific, and technical services, management of companies and enterprises, administrative and support, and waste management and remediation services).

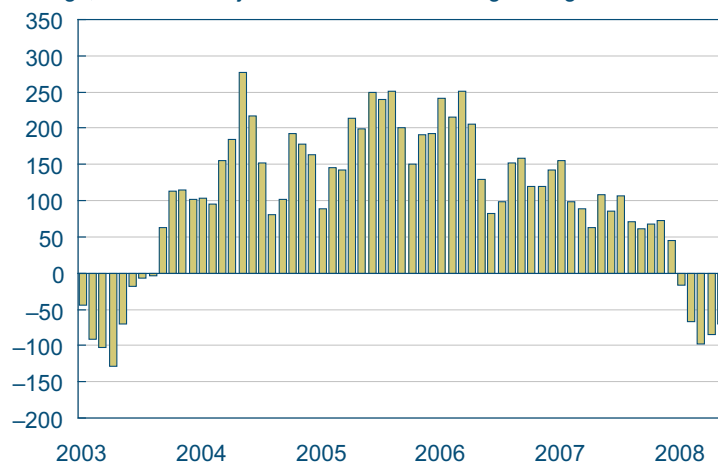
Source: Bureau of Labor Statistics.

### The Unemployment Rate

U.S. labor markets have not experienced an increase in the unemployment rate of 0.5 percentage point since February 1986. The decline in 1986 in fact did not happen during a recession, but most such sharp increases have been historically associated with an overall economic downturn. The primary reason behind the latest large uptick in the unemployment rate is labor force entry. The total number of workers in the labor force increased in May by 577,000. An additional 285,000 workers lost their jobs, which gave rise to an increase of more than 861,000 in the number of unemployed. However, one needs to be cautious when interpreting these monthly changes in household data, which are very volatile. One interesting feature of the household employment data in May was the unusually high

### Private Sector Employment Growth

Change, thousands of jobs: Three-month moving average



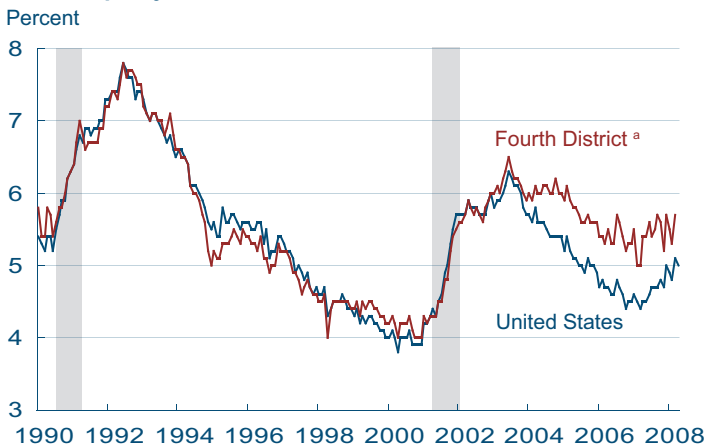
Source: Bureau of Labor Statistics.

increase in teenage unemployment. The unemployment rate of workers aged 16 to 19 increased from 15.4 percent in April to 18.7 percent in May. This increase of 3.3 percentage points has been the largest change observed since January 1948, when the series begins. Hence, this latest unusual uptick in the unemployment rate is partly due to an unusually high level of teenagers entering the labor force.

## Regional Activity

### Fourth District Employment Conditions, March

#### Unemployment Rates



Notes: Seasonally adjusted using the Census Bureau's X-11 procedure; Shaded bars represent recessions; Some data reflect revised inputs, reestimation, and new statewide controls. For more information, see <http://www.bls.gov/lau/launews1.htm>. Source: U.S. Department of Labor, Bureau of Labor Statistics.

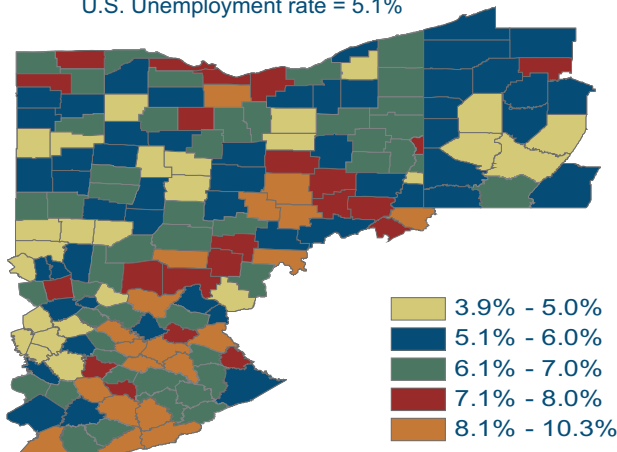
05.23.08

Tim Dunne and Kyle Fee

The district's unemployment rate jumped 0.4 percent to 5.7 percent for the month of March. The increase in the unemployment rate can be attributed to increases in the number of people unemployed (6.6 percent) and the labor force (0.1 percent), along with a decrease in the number of people employed (-0.3 percent). The district's unemployment rate was higher than the national rate in March (by 0.6 percent), as it has been since early 2004. Since this time last year, both the Fourth District and the national unemployment rates have increased by 0.7 percentage point.

#### County Unemployment Rates

U.S. Unemployment rate = 5.1%



Note: Data are seasonally adjusted using the Census Bureau's X-11 procedure. Source: U.S. Department of Labor, Bureau of Labor Statistics.

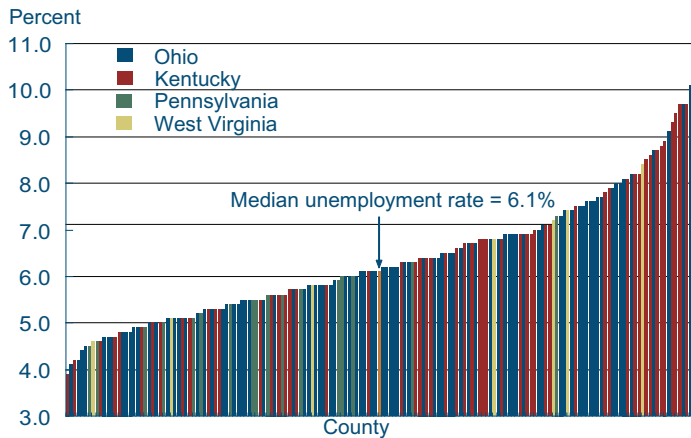
There are considerable differences in unemployment rates across counties in the Fourth District. Of the 169 counties that make up the Fourth District, 24 had an unemployment rate below the national average in March, and 145 had a higher unemployment rate than the national average. Rural Appalachian counties continue to experience higher levels of unemployment than others in the district.

The distribution of unemployment rates among Fourth District counties ranges from 3.9 percent to 10.3 percent, with a median county unemployment rate of 6.1 percent. Pennsylvania counties tend to populate the middle to lower half of the distribution, with roughly two-thirds of Kentucky's Fourth District counties in the upper half of the distribution.

The distribution of monthly changes in unemployment rates shows that the median county's unemployment rate increased 0.37 percentage

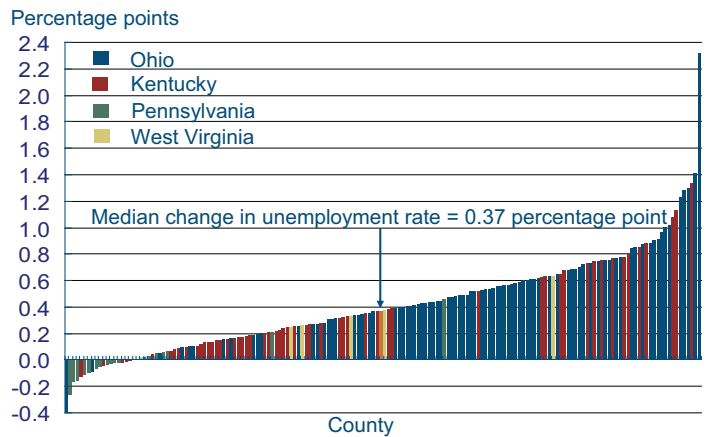
point from February to March. The county-level changes indicate that 69 percent of Ohio counties experienced an increase in unemployment rates that exceeded 0.4 percentage point. Alternatively, Pennsylvania counties averaged no change in unemployment rates, with 11 out of the 19 Fourth District Pennsylvania counties actually showing declines in unemployment rates.

## County Unemployment Rates



Note: Data are seasonally adjusted using the Census Bureau's X-11 procedure.  
Source: U.S. Department of Labor, Bureau of Labor Statistics.

## Change in County Unemployment Rates: February 2008 to March 2008



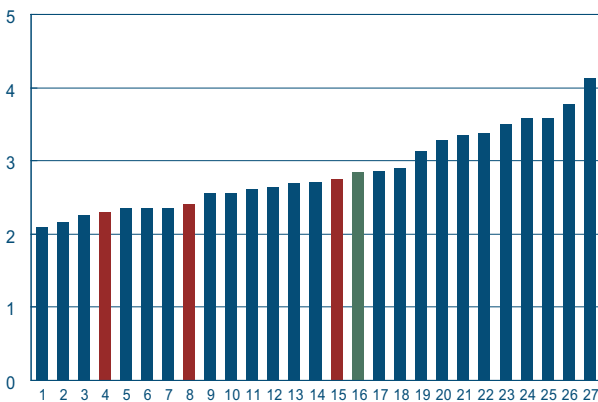
Note: Data are seasonally adjusted using the Census Bureau's X-11 procedure.  
Source: U.S. Department of Labor, Bureau of Labor Statistics.

## Regional Activity

### Real Income Growth across Metropolitan Areas

#### CPI Growth, 2000–2006

Average annual percent change



1. Milwaukee-Racine, WI
2. Portland-Salem, OR-UH
3. Atlanta, GA
4. Cleveland-Akron, OH
5. Denver-Boulder-Greeley, CO
6. Kansas City, MO-KS
7. Chicago-Gary-Kenosha, IL-IN-WI
8. Cincinnati-Hamilton, OH
9. Minneapolis-St. Paul
10. Dallas-Fort Worth, TX
11. Detroit-Ann Arbor-Flint, MI
12. Seattle-Tacoma-Bremerton
13. San Francisco-Oakland-San Jose
14. St. Louis, MO-IL
15. Pittsburgh, PA
16. USAAVG
17. Houston-Galveston-Brazoria, TX
18. Anchorage, AK
19. Honolulu, HI
20. Washington-Baltimore, DC-MD-VA-WV
21. Philadelphia-Wilmington-Atlanta City
22. Tampa-St. Pete-Clearwater, FL
23. New York-Newark-Li, NY-NY-CT-PA
24. Boston-Brockton-Nashua
25. Miami-Fort Lauderdale, FL
26. Los Angeles-Riverside-Orange
27. San Diego, CA

Source: Bureau of Labor Statistics.

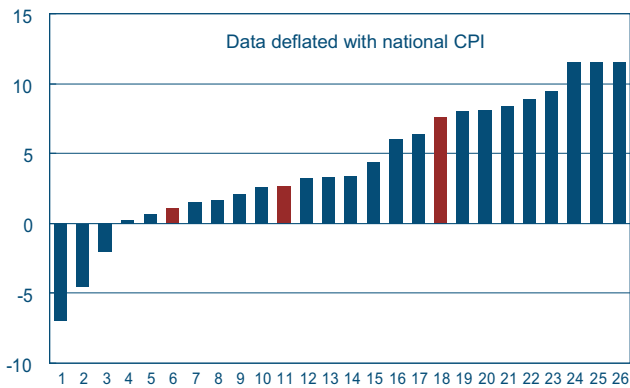
06.06.08

by Timothy Dunne and Kyle Fee

A standard measure of regional economic performance is per capita income growth. Typically, analysts try to remove the effects of inflation on the raw data for income growth by converting nominal per capita income for an area into real or constant-dollar income. The Consumer Price Index (CPI) is often used to make such adjustments. The chart below shows the real per capita income growth rates for a number of metropolitan areas from 2000 to 2006. (Note that the Bureau of Economic Analysis releases an adjusted income growth series, but it uses the PCE price index to deflate the raw data. We use the CPI here because of some comparisons we make below. Using the CPI instead of the PCE doesn't affect the rankings of cities with respect to their growth, although it does affect the magnitude of the real growth rates.)

## Real per Capita Income Growth, 2000-2006

Percent



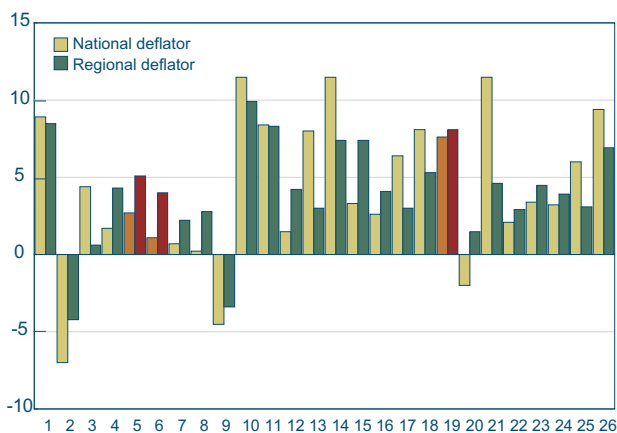
- |                                   |                                       |
|-----------------------------------|---------------------------------------|
| 1. Atlanta, GA                    | 14. Seattle-Tacoma-Bremerton          |
| 2. Detroit-Ann Arbor-Flint, MI    | 15. Boston-Brockton-Nashua            |
| 3. Portland-Salem, OR-UH          | 16. Tampa-St. Pete-Clearwater, FL     |
| 4. Denver-Boulder-Greeley, CO     | 17. NY-No. NJ-LI, NY-NY-CT-PA         |
| 5. Dallas-Forth Worth, TX         | 18. Pittsburgh, PA                    |
| 6. Cleveland-Akron, OH            | 19. Los Angeles-Riverside-Orange      |
| 7. Kansas City, MO-KS             | 20. Phila-Wilmington-Atl City         |
| 8. Chicago-Gary-Kenosha, IL-IN-WI | 21. Houston-Galveston-Brazoria, TX    |
| 9. San Francisco-Oakl-San Jose    | 22. Anchorage, AK                     |
| 10. Minneapolis-St. Paul          | 23. Washington-Baltimore, DC-MD-VA-WV |
| 11. Cincinnati-Hamilton, OH       | 24. Honolulu, HI                      |
| 12. St. Louis, MO-IL              | 25. Miami-Fort Lauderdale, FL         |
| 13. Milwaukee-Racine, WI          | 26. San Diego, CA                     |

Sources: Bureau of Labor Statistics; Bureau of Economic Analysis.

In our adjusted series, real income growth was highest in San Diego, Miami-Fort Lauderdale, and Honolulu and lowest in Atlanta, Detroit-Ann Arbor-Flint, and Portland-Salem. With respect to Fourth District metropolitan areas, Cleveland-Akron experienced very modest growth of 1.1 percent over the period, ranking it sixth-lowest among the 26 metropolitan areas. Cincinnati had a growth rate of 2.7 percent, placing it in the middle of the distribution, and Pittsburgh's growth rate was 7.6 percent, the highest in the Fourth District.

This standard approach to measuring real income growth assumes that the changes in price levels experienced in metropolitan areas are similar to the change in price levels at the national level. No adjustments are made for differences in inflation rates across metropolitan areas. But inflation rates are not necessarily identical in different regions. For the areas in the figure above, the Bureau of Labor Statistics (BLS) produces region-specific CPI's, which provide estimates of how price levels have changed over time within a particular region. Comparing changes in regional price indexes across regions shows which region has experienced a more rapid change in prices—not which region has a higher price level or higher living costs. The distribution of metropolitan average CPI growth rates indicates considerable variation in inflation across regions. Metropolitan areas on the low end, like Milwaukee, Portland, and Atlanta, had average annual inflation rates of 2.1 to 2.3 percent, while metropolitan areas on the higher end, such as Miami, Los Angeles, and San Diego, had rates of 3.8 to 4.1 percent.

## Real per Capita Income Growth, Deflated with National CPI and Regional CPI

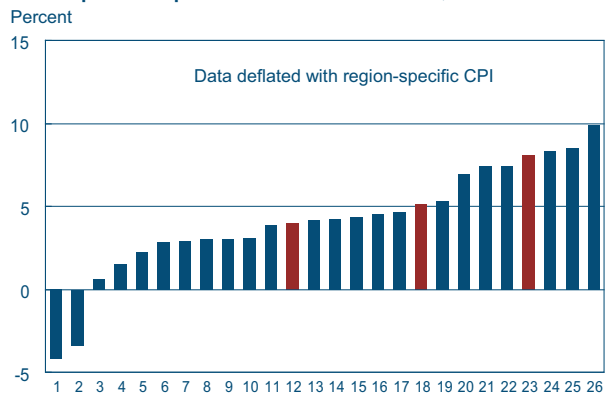


- |                                    |   |
|------------------------------------|---|
| 1. Anchorage, AK                   | 14. Miami-Fort Lauderdale, FL             |
| 2. Atlanta, GA                     | 15. Milwaukee-Racine, WI                  |
| 3. Boston-Brockton-Nashua          | 16. Minneapolis-St Paul                   |
| 4. Chicago-Gary-Kenosha, IL-IN-WI  | 17. NY-No. NJ-LI, NY-NY-CT-PA             |
| 5. Cincinnati-Hamilton, OH         | 18. Philadelphia-Wilmington-Atlantic City |
| 6. Cleveland-Akron, OH             | 19. Pittsburgh, PA                        |
| 7. Dallas-Fort Worth, TX           | 20. Portland-Salem, OR-UH                 |
| 8. Denver-Boulder-Greeley, CO      | 21. San Diego, CA                         |
| 9. Detroit-Ann Arbor-Flint, MI     | 22. San Francisco-Oakland-San Jose        |
| 10. Honolulu, HI                   | 23. Seattle-Tacoma-Bremerton              |
| 11. Houston-Galveston-Brazoria, TX | 24. St Louis, MO-IL                       |
| 12. Kansas City, MO-KS             | 25. Tampa-St. Pete-Clearwater, FL         |
| 13. Los Angeles-Riverside-Orange   | 26. Washington-Baltimore, DC-MD-VA-WV     |

These differences in regional CPI growth rates affect the calculation of real per capita income growth, as well. The figure below shows real per capita income growth of different metropolitan areas calculated with both the national and regional price indexes. Comparing the two measures of real income growth across areas, we note that the series deflated by the regional CPI shows less overall variation across regions than the series that uses the national CPI. Real income growth rates using the national CPI range from -7.0 to 11.5 percent over the period from 2000 to 2006. Using the regional CPIs as deflators, the range falls to -4.2 to 9.9 percent.



## Real per Capita Income Growth, 2000–2006



- |                                   |                                       |
|-----------------------------------|---------------------------------------|
| 1. Atlanta, GA                    | 14. Kansas City, MO-KS                |
| 2. Detroit-Ann Arbor-Flint, MI    | 15. Chicago-Gary-Kenosha, IL-IN-WI    |
| 3. Boston-Brockton-Nashua         | 16. Seattle-Tacoma-Bremerton          |
| 4. Portland-Salem, OR-UH          | 17. San Diego, CA                     |
| 5. Dallas-Fort Worth, TX          | 18. Cincinnati-Hamilton, OH           |
| 6. Denver-Boulder-Greeley, CO     | 19. Phila-Wilmington-Atl City         |
| 7. San Francisco-Oakl-San Jose    | 20. Washington-Baltimore, DC-MD-VA-WV |
| 8. NY-No. NJ-LI, NY-NY-CT-PA      | 21. Miami-Fort Lauderdale, FL         |
| 9. Los Angeles-Riverside-Orange   | 22. Milwaukee-Racine, WI              |
| 10. Tampa-St. Pete-Clearwater, FL | 23. Pittsburgh, PA                    |
| 11. St. Louis, MO-IL              | 24. Houston-Galveston-Brazoria, TX    |
| 12. Cleveland-Akron, OH           | 25. Anchorage, AK                     |
| 13. Minneapolis-St. Paul          | 26. Honolulu, HI                      |

Sources: Bureau of Labor Statistics; Bureau of Economic Analysis

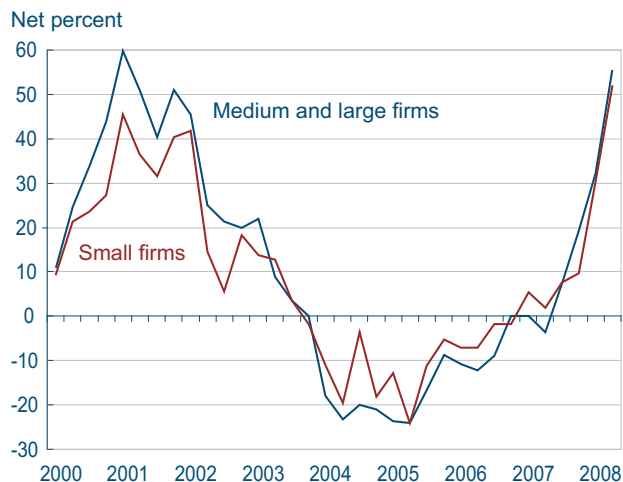
Moreover, there are significant differences in real per capita income across cities, depending on which deflator is used. For example, when we use the national CPI to adjust for changes in prices over time, New York has a real income growth rate of 6.4 percent compared to Cleveland's 1.1 percent for the 2000–2006 period. When we use the regional CPIs, Cleveland's real income grows at 4.0 percent, while New York's grows at 3.0 percent. A key difference between Cleveland and New York in changes in underlying prices is that New York experienced much higher growth in the housing component of its regional CPI than did Cleveland.

Comparing the relative rankings of Fourth District cities in income growth across the two series using the different CPIs, we see that Fourth District cities move up in the rankings when the regional CPI is used to adjust for growth in prices. With the regional CPI, Cleveland is near the center of the distribution in income growth, with Cincinnati and Pittsburgh well above the median metropolitan area. This move up the rankings for Cleveland and Cincinnati is particularly noticeable. These cities had modest nominal income growth compared to other cities but experienced below-average regional inflation, which resulted in relatively stronger real per capita income growth.

## Banking and Financial Markets

### Business Loan Markets

### Domestic Banks Reporting Tighter Credit Standards



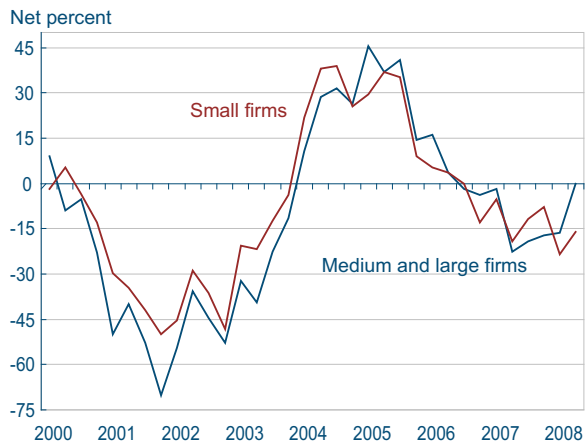
Source: Senior Loan Officer Opinion Survey on Bank Lending Practices, Board of Governors of the Federal Reserve System, April 2008.

05.27.08

by Joseph G. Haubrich and Saeed Zaman

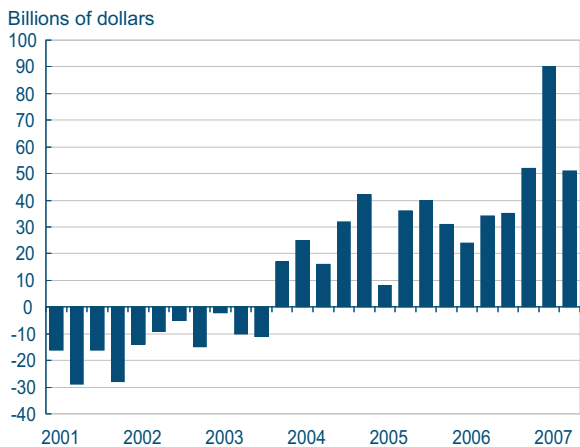
The Federal Reserve Board's April 2008 survey of senior loan officers (covering the months of January through March 2008) found significant tightening of standards for commercial and industrial loans since the last survey. About 55 percent of the domestic banks and 60 percent of the foreign banks surveyed reported having tightened standards for commercial and industrial loans to large and medium-sized firms. The remaining fraction of those surveyed reported little change in lending standards. The reasons cited for tightening included a more-uncertain economic outlook, reduced tolerance for risk, decreased liquidity in the secondary market for these loans, and worsening of industry-

## Domestic Banks Reporting Stronger Demand



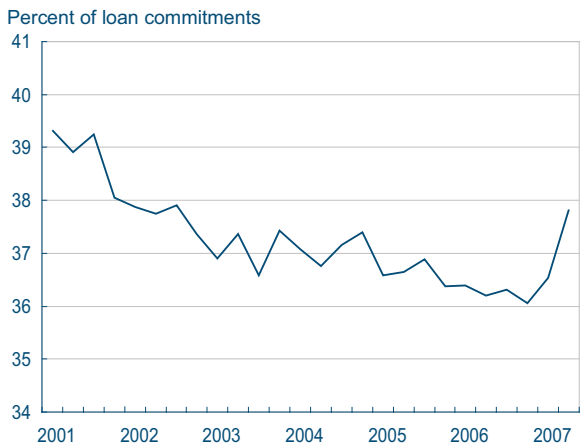
Source: Senior Loan Officer Opinion Survey on Bank Lending Practices, Board of Governors of the Federal Reserve System, April 2008.

## Quarterly Change in Commercial and Industrial Loans



Source: Federal Deposit Insurance Corporation, *Quarterly Banking Profile*, Fourth Quarter 2007.

## Utilization Rate of Commercial and Industrial Loan Commitments



Source: Federal Deposit Insurance Corporation, *Quarterly Banking Profile*, Fourth Quarter 2007.

specific problems. A large fraction of domestic and foreign banks increased the cost of credit lines and premiums charged on loans to riskier borrowers. A substantial majority of the domestic and foreign banks surveyed raised their lending spreads (loan rates over the cost of funds).

Demand for commercial and industrial loans continued to weaken over the period surveyed, although by less than in the previous survey period. About 20 percent of the domestic banks and 25 percent of the foreign banks surveyed reported weaker demand. Those who reported weaker demand cited decreased investment in inventories, plants and equipment as a reason, as well as a decrease in customers' need to finance mergers and acquisitions. Those who reported stronger demand said that it was caused by customers who were shifting their borrowing to the banks from other banks or financial firms with less attractive borrowing terms.

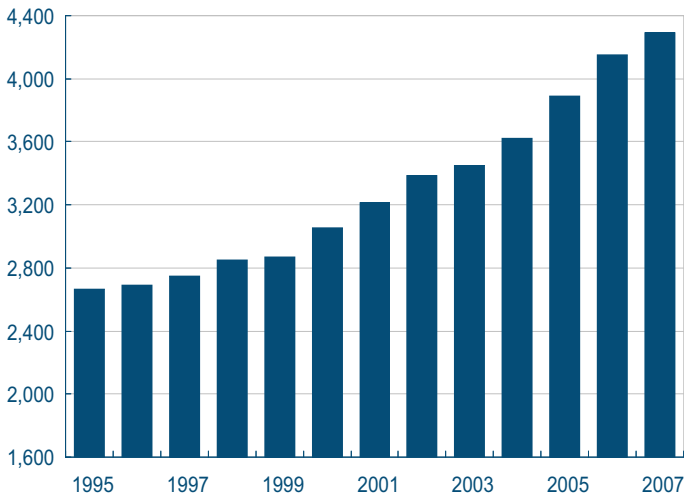
After recording the biggest-ever quarterly increase of \$90 billion in third quarter of 2007, bank and thrift holdings of business loans went up moderately by \$51 billion in the fourth quarter of 2007. This increase marks the fifteenth consecutive quarterly increase in these holdings. The sharp reversal in the trend of quarterly declines in commercial and industrial loan balances on the books of FDIC-insured institutions prior to the second quarter of 2004 is still going strong.

The utilization rate of business loan commitments (draw downs on prearranged credit lines extended by banks to commercial and industrial borrowers) jumped up to 37.83 percent of total commitments. The higher demand by borrowers may point to the difficulty in obtaining credit from the capital markets due to the recent financial turmoil.

## FDIC Funds

### FDIC-Insured Deposits

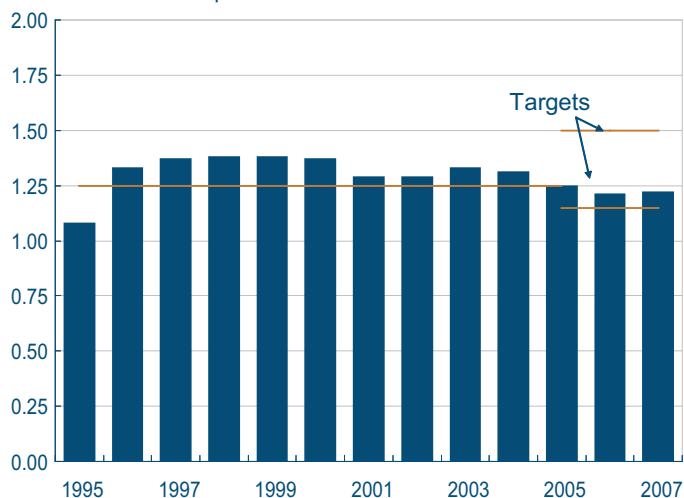
Billions of dollars



Source: Federal Deposit Insurance Corporation, *Quarterly Banking Profile*, Fourth Quarter 2007.

### Fund Reserve Ratio

Percent of insured deposits



Source: Federal Deposit Insurance Corporation, *Quarterly Banking Profile*, Fourth Quarter 2007.

05.22.08

by Joseph G. Haubrich and Saeed Zaman

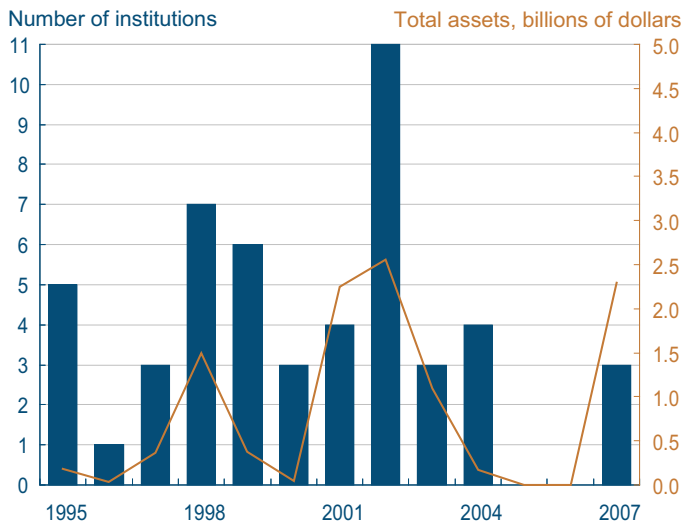
In 2007, deposits insured by the FDIC insurance fund grew at a 3.4 percent annual rate. As of December 31, 2007, the FDIC has insured \$4.3 trillion of member deposits. Growth in reserves outstripped insured deposits. As a result, the insurance fund's reserve-to-deposit ratio increased 1 basis point, from 1.21 percent at year end 2006 to 1.22 percent in 2007. The reserve-to-deposit ratio remained in the mandated target range of 1.15–1.5 percent.

Bank failures since 1995 have been miniscule in terms of numbers and total assets of failed institu-

tions. After a record-breaking trend of 10 consecutive quarters without any bank failure, three institutions failed in 2007, with assets totaling \$2.3 billion. The rarity of thrift institution failures over the past seven years contrasts vividly with the widespread solvency problems that plagued the industry throughout the 1980s.

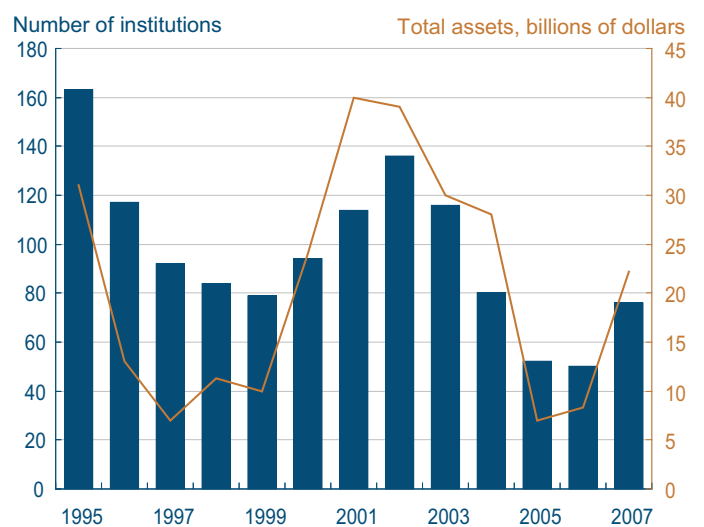
At the end of 2007, the total number of problem institutions (those with substandard examination ratings) rose to 76, an increase of 26 institutions from the end of 2006. Moreover, the increase in the number of problem institutions led to an increase in the amount of total assets held by problem institutions, which ballooned to \$22 billion from \$8.3 billion over the same period. The jump in the number of problem institutions and the high value of those institutions' assets—combined with the ongoing financial mess—suggest that the Deposit Insurance Fund's losses might go up in the near future.

## Failed Institutions



Source: Federal Deposit Insurance Corporation, *Quarterly Banking Profile*, Fourth Quarter 2007.

## Problem Institutions



Source: Federal Deposit Insurance Corporation, *Quarterly Banking Profile*, Fourth Quarter 2007.

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