Structure and Functions of the Federal Reserve System

• The “Fed” consists of three 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: 19 members; 12 voting

• As with most central banks, the Fed’s primary responsibilities fall within four general areas:
  • Lender of last resort – provide liquidity in times of crisis
  • Monetary policy – promote full employment and low inflation
  • Bank regulation – ensure safety and soundness of banks
  • Financial services – bank for banks, bank for federal govt.
The Oklahoma City Branch of the Federal Reserve Bank of Kansas City

• Functions – approximately 40 staff
  • Research on U.S. and Oklahoma economies
  • Economic, community, and financial education outreach
  • Examinations of Oklahoma financial institutions

• 2016 Branch Board of Directors
  • Pete Delaney (chair), Retired Chairman, OGE Energy Corp., OKC
  • Clint Abernathy, Owner, Abernathy Farms, Inc., Altus
  • Michael Coffman, CEO, Panhandle Oil & Gas, Inc., Oklahoma City
  • Chuck Hall, Chairman & CEO, Exchange Bank & Trust, Perry
  • Jane Haskin, President & CEO, First Bethany Bank & Trust, Bethany
  • Tina Patel, Co-Owner & CFO, Promise Hotels, Tulsa
  • Doug Stussi, EVP & CFO, Love’s Travel Stops & Country Stores, OKC
The U.S. Economy and Monetary Policy
GDP slowed somewhat in Q4, due to business investments and exports

Growth in Components of Real GDP

Source: U.S. Bureau of Economic Analysis, Macroeconomic Advisors
U.S. factory activity has slowed, but job growth and services remain solid

U.S. Private Payroll Employment and Business Indexes

Change from previous month, thousands
U.S. unemployment is at long-term levels after falling considerably in recent years

Unemployment Rate
Seasonally Adjusted

Current (Jan. 2016): 4.9%

Sources: U.S. Bureau of Labor Statistics, FOMC
U.S. inflation is low but expected to return to close to target in 2016

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PCE Inflation Index

Percent change, year-over-year

Current (Q3 2015): 0.3%
Current Core (Q3 2015): 1.3%

Sept. FOMC Forecast and Range (Shaded)

Dec. FOMC Forecast--Ranges in Yellow

Sources: U.S. Bureau of Labor Statistics, FOMC
Most FOMC participants have projected rate increases this year.

Federal Funds Rate
Year-end target

Current (Jan. 2016): 0.25-0.50%

Sources: Federal Reserve Board, FOMC
Trends in the Oklahoma Economy
Oklahoma employment has fallen from a year ago, especially in non-metro areas.

Source: U.S. Bureau of Labor Statistics
Energy jobs have fallen sharply the past year, pulling down overall state employment.

Job Growth by Industry
Dec-15

Percent change, year-over-year

Source: Bureau of Labor Statistics
State tax receipts continue to fall, and in January had the worst decline since late ‘09

State Tax Receipts
Through Jan-16

Source: OK Tax Commission
The energy sector is not as large as in the 1980s on some measures, but is on others.
The KC Fed’s Q4 energy survey showed further declines, with more expected
Firms’ average price needed to increase drilling is above levels expected through most of 2017.

Firms’ Price Needed to Increase Drilling and Future Price Expectations
Q4 KC Fed Energy Survey

$/Barrel

Price Needed to Increase Drilling

2016 Year-End Expected WTI Price

2017 Year-End Expected WTI Price

Source: FRBKC Energy Survey
Most energy firms have decreased employment and are planning further cuts

Total Employment Change by Energy Firms
Q4 KC Fed Energy Survey

Number of responses

Source: FRBKC Energy Survey
Most firms are also expecting increased mergers, defaults, and bankruptcies.

Q4 Energy Survey Firm Expectations for 2016

Large increase in both M&A activity and defaults/bankruptcies

Large increase in M&A but little change in defaults/bankruptcies

Little change in M&A but large increase in defaults/bankruptcies

Little change in both M&A activity and defaults/bankruptcies

Source: FRBKC Energy Survey
Oklahoma farm income has now also dropped after holding up in first half 2015

Source: KCFRB Ag Credit Survey
Energy and Ag are even more important in Grady County than in the state as a whole.

Grady County Personal Income Share by Industry
2014

<table>
<thead>
<tr>
<th>Industry</th>
<th>Percent of Total Income</th>
<th>Grady Co Location Quotient</th>
<th>OK Location Quotient</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Grady Co</td>
<td>U.S.</td>
<td></td>
</tr>
<tr>
<td>Mining</td>
<td>17.1</td>
<td>1.8</td>
<td>9.5</td>
</tr>
<tr>
<td>Farming</td>
<td>7.3</td>
<td>1.1</td>
<td>6.6</td>
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<tr>
<td>Construction</td>
<td>12.5</td>
<td>5.8</td>
<td>2.1</td>
</tr>
<tr>
<td>Trade, Transportation &amp; Utilities</td>
<td>20.9</td>
<td>15.8</td>
<td>1.3</td>
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<tr>
<td>State &amp; Local Government</td>
<td>16.3</td>
<td>13.2</td>
<td>1.2</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>10.3</td>
<td>10.0</td>
<td>1.0</td>
</tr>
<tr>
<td>Leisure &amp; Hospitality</td>
<td>3.1</td>
<td>4.5</td>
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<tr>
<td>Financial Activities</td>
<td>5.9</td>
<td>9.5</td>
<td>0.6</td>
</tr>
<tr>
<td>Federal Government</td>
<td>1.6</td>
<td>4.3</td>
<td>0.4</td>
</tr>
<tr>
<td>Professional and Business Services</td>
<td>4.6</td>
<td>17.3</td>
<td>0.3</td>
</tr>
<tr>
<td>Information</td>
<td>0.5</td>
<td>3.5</td>
<td>0.1</td>
</tr>
<tr>
<td>Education &amp; Health*</td>
<td>0.0</td>
<td>13.1</td>
<td>n/a</td>
</tr>
</tbody>
</table>

Note - Location quotient is the division of local share by national share
*Not disclosed for Grady County

But Grady County is one of the few spots in the state still seeing rig activity.
And Grady Co. unemployment remains below the U.S. rate, similar to the state as a whole.
Summary

• Oklahoma employment and tax revenues continue to suffer from the oil downturn, and ag-related industries are also now declining.

• The latest KC Fed energy survey showed another decline in the sector in Q4, with expectations of more difficulties ahead.

• Grady County has high concentrations in energy and agriculture, but some drilling continues and unemployment remains low.