

Economic Outlook



FEDERAL RESERVE BANK *of* KANSAS CITY

November 15, 2016

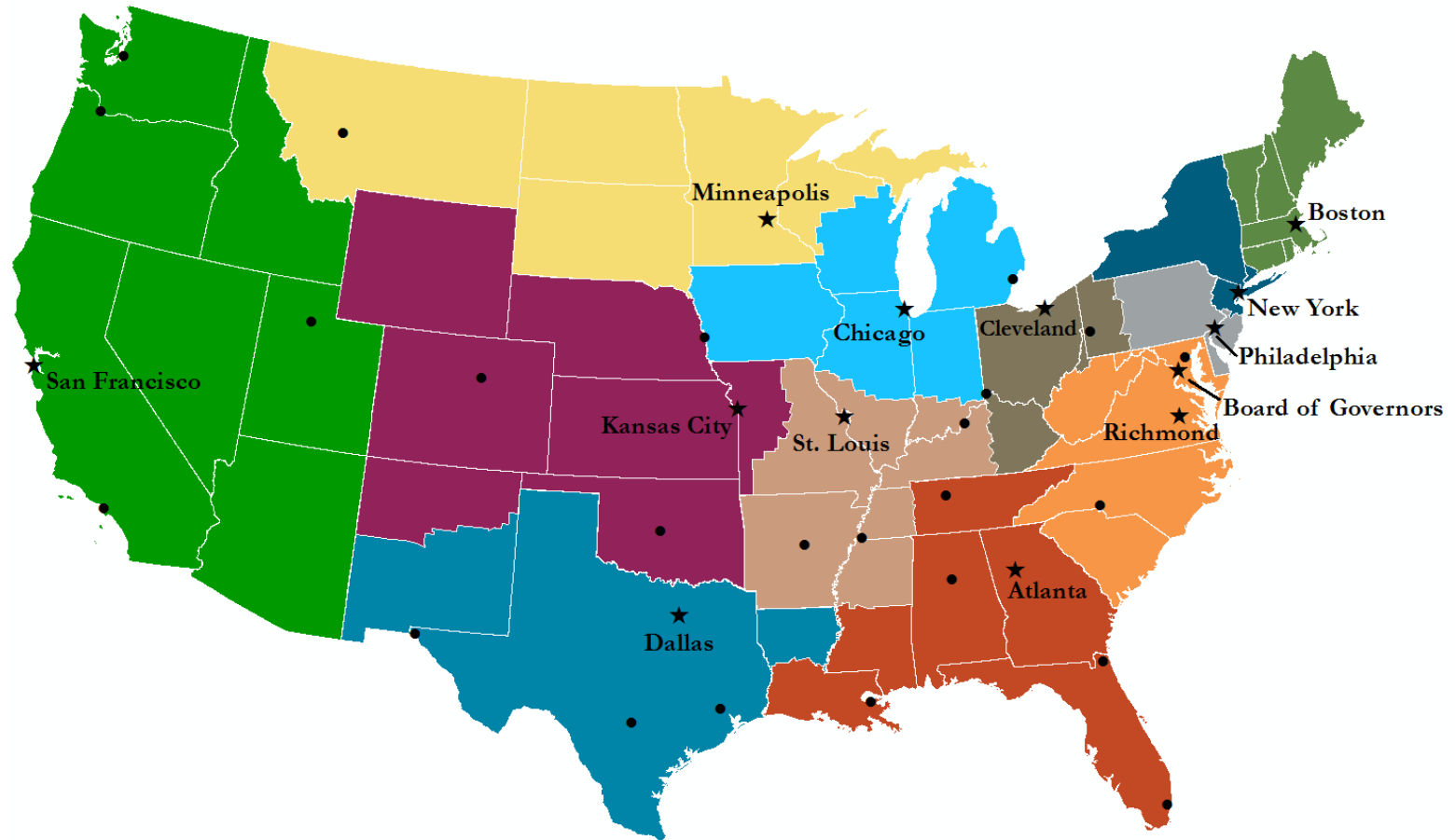
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Omaha Branch Executive and Economist

Federal Reserve Bank of Kansas City

Regional Federal Reserve Banks are an important structural component to U.S. monetary policy.



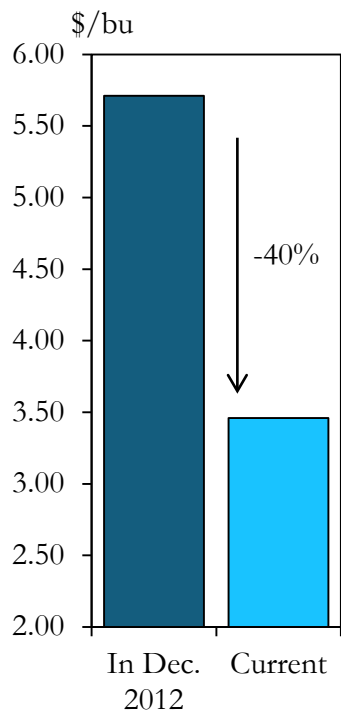
Outlook Themes

- Modest economic growth, but sluggish and short of expectations.
- Divergent economic growth. Some industries and regions performing much better than others.
- A downturn in the agricultural and rural economy continues to raise the risk profile of the sector.

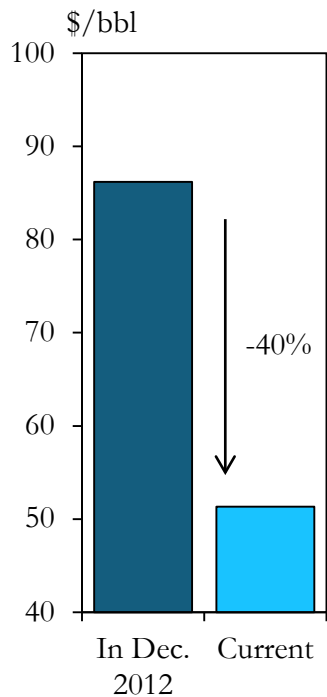


Past expectations about the path of many economic indicators have often missed the mark.

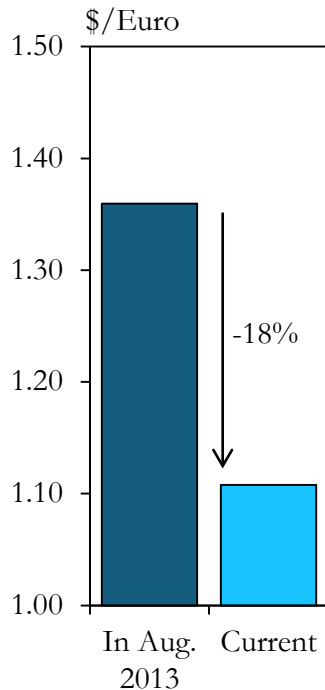
**Dec. 2016
Corn Price**



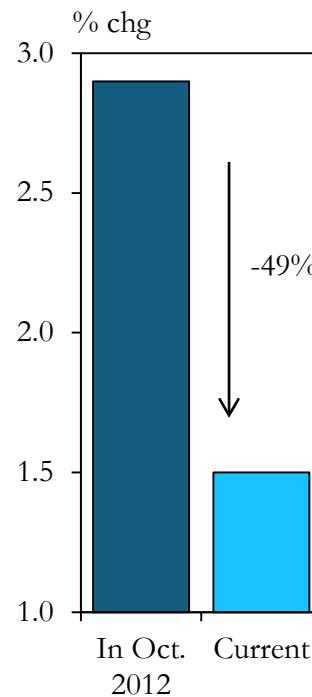
**Dec. 2016
Oil Price**



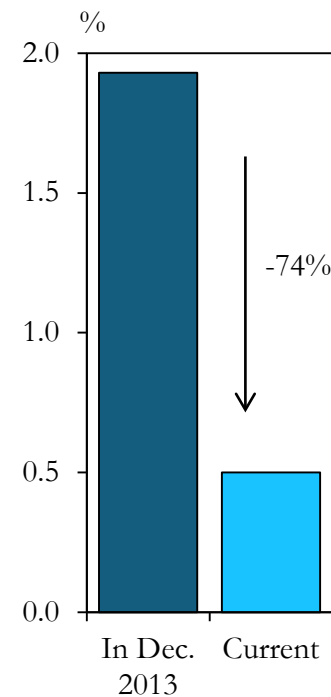
**Dec. 2016
\$/Euro Rate**



**2016 U.S.
Real GDP**



**Dec. 2016
Fed Funds**

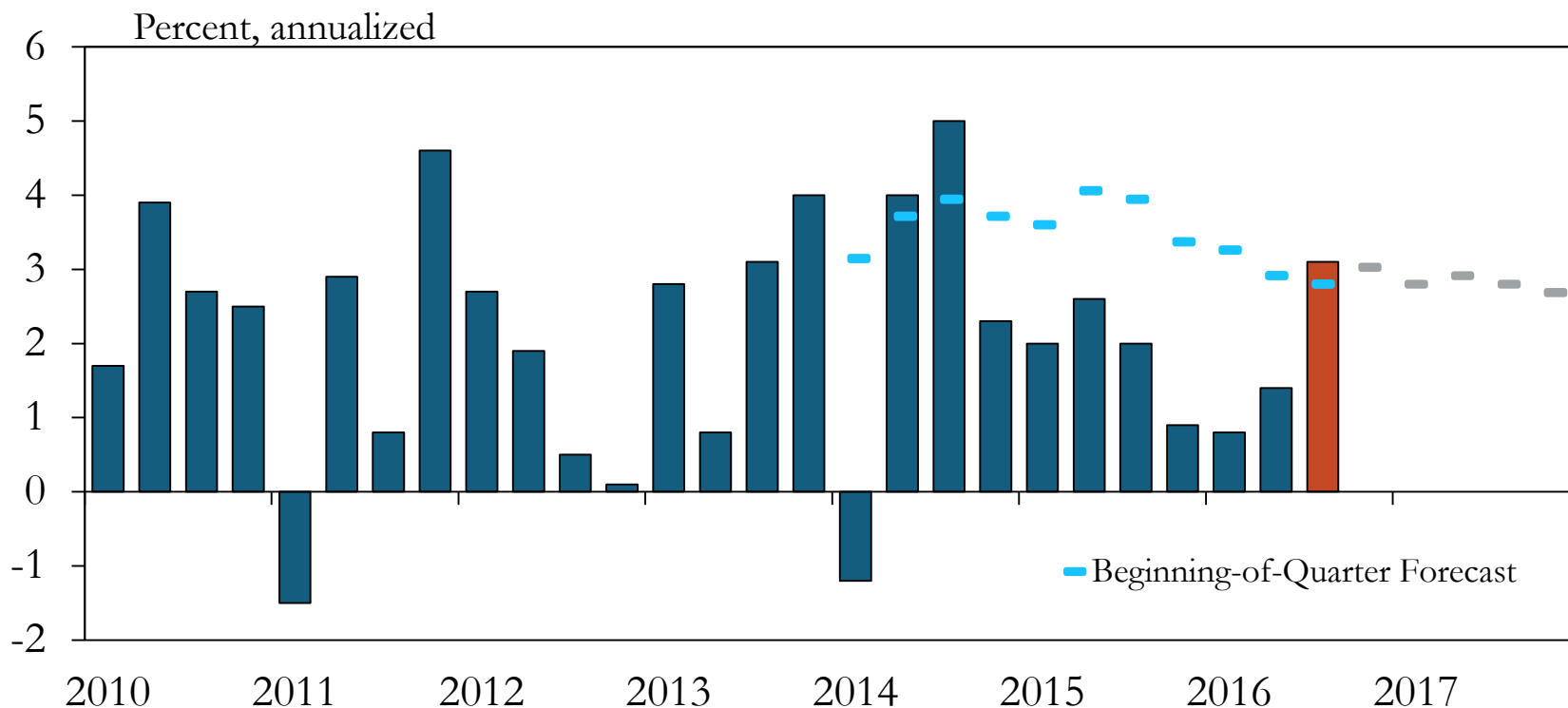


Sources: barchart.com, Blue Chip Financial Forecasts, and Haver Analytics.



Economic growth generally has been positive, but has consistently fallen short of expectations.

U.S. Real GDP Growth



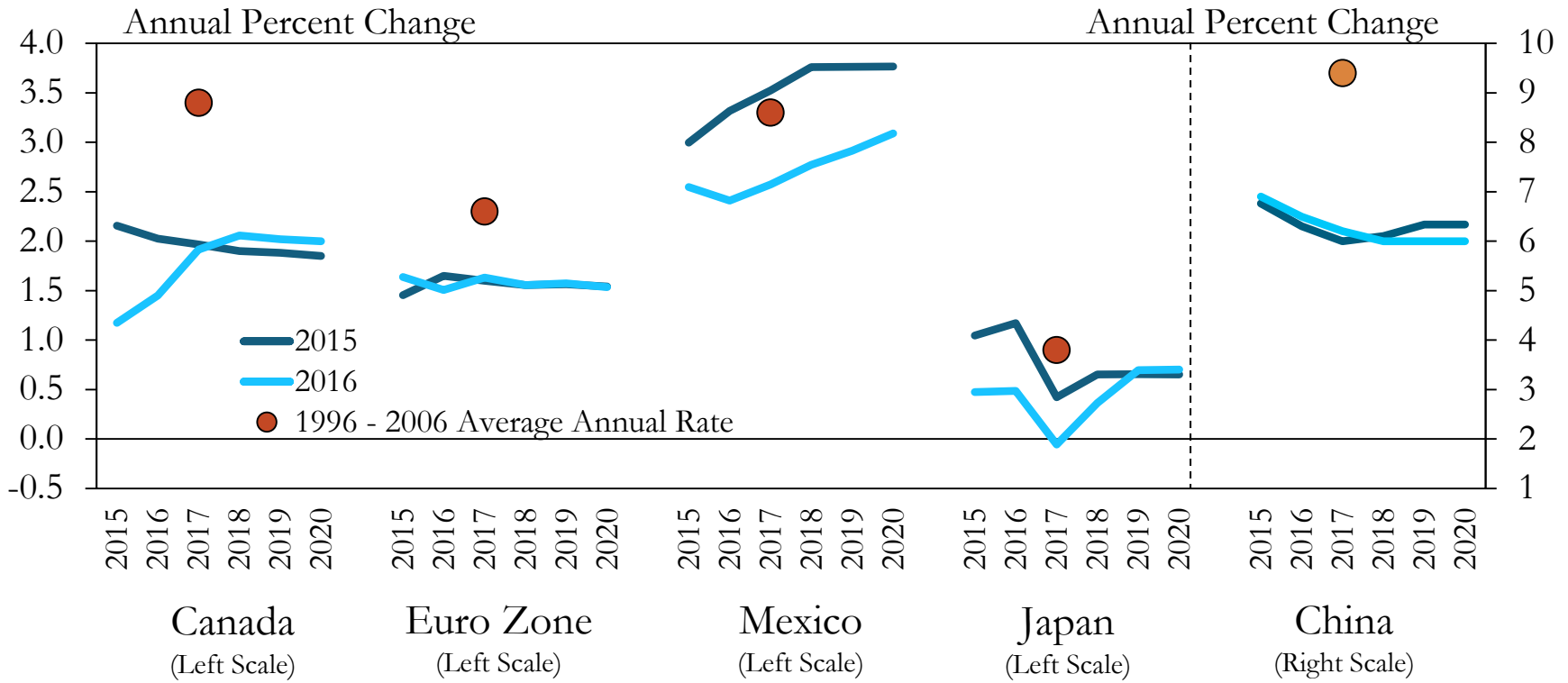
Sources: Bureau of Economic Analysis, Haver Analytics, Macroeconomic Advisors and Blue Chip Financial Forecasts.

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Economic growth has also softened globally.

Global Real GDP Growth

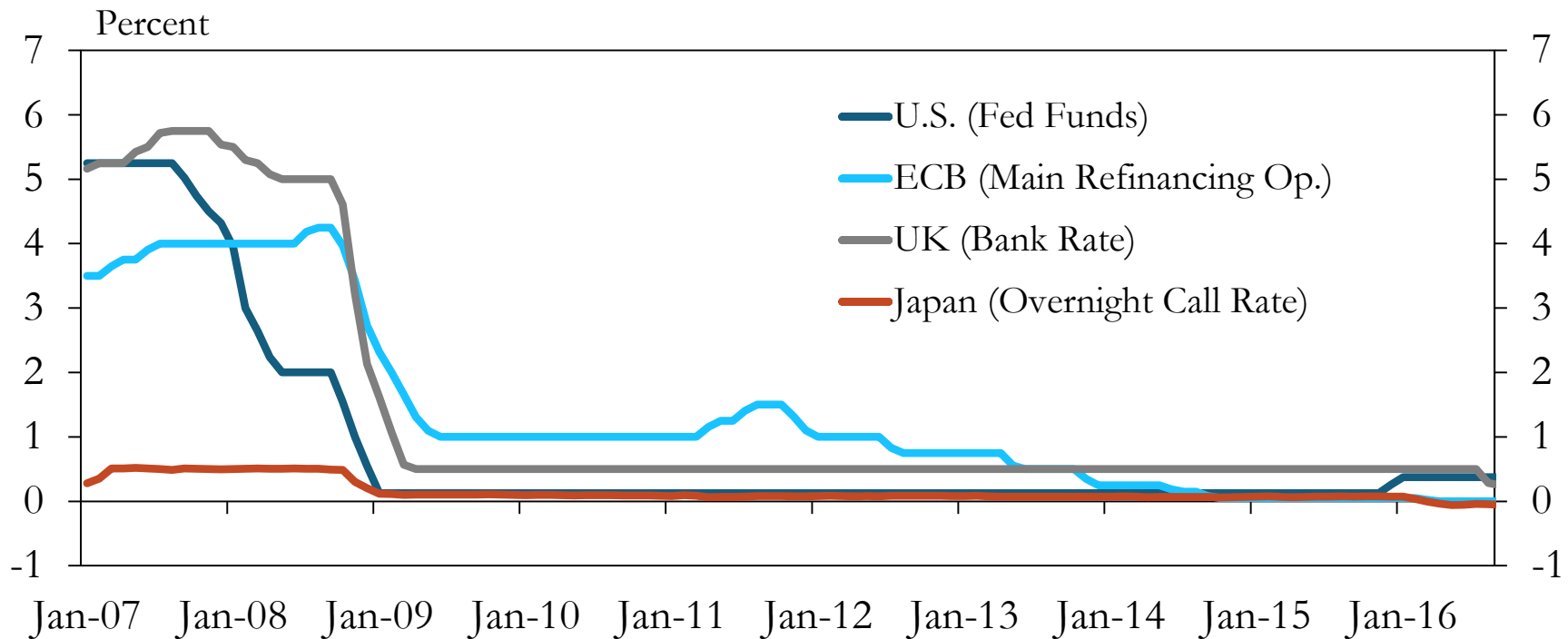


Sources: IMF and Haver Analytics.



Central banks have sought to stimulate growth with very accommodative monetary policy.

Central Bank Interest Rate Targets



Sources: Federal Reserve Board, ECB, Bank of England, Bank of Japan and Haver Analytics.

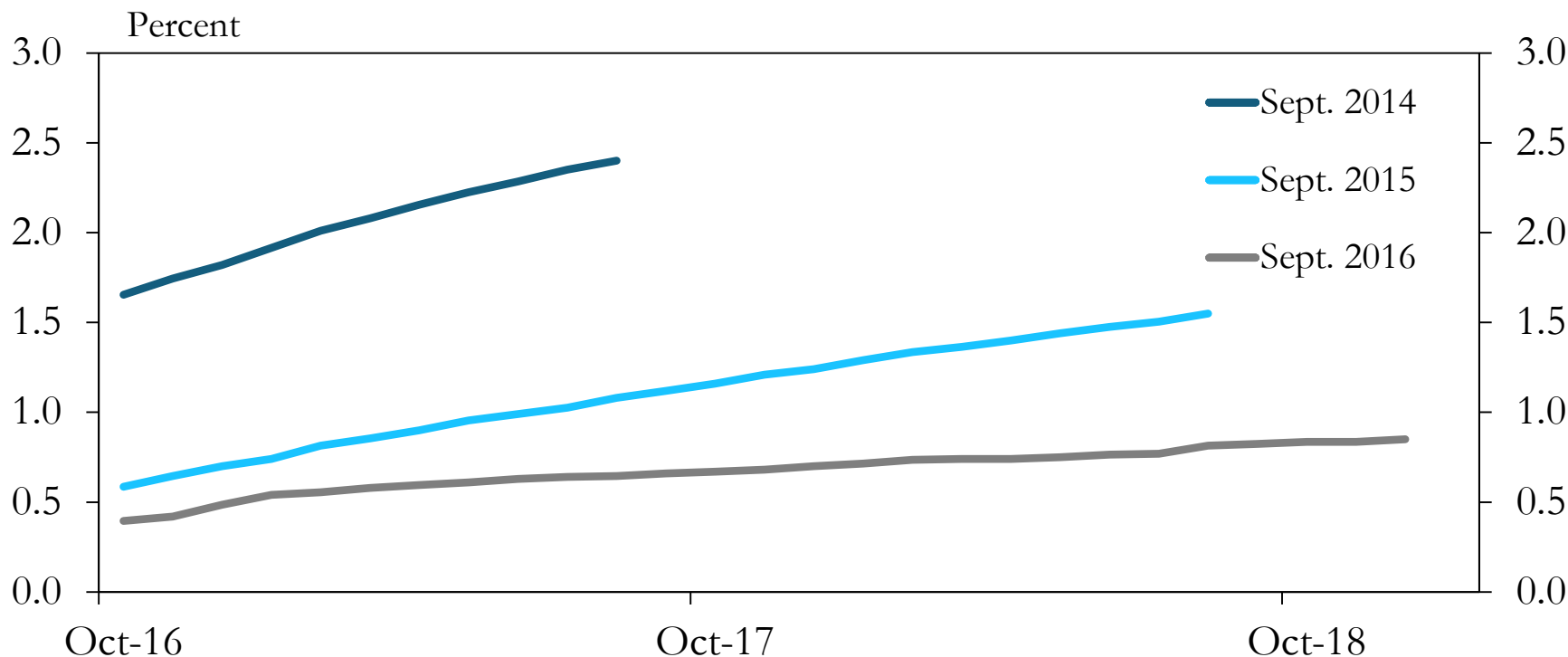
Note: Interest rates for each region shown are the following: U.S. (Fed Funds Rate), ECB (Main Refinancing Operation), UK (Bank Rate), Japan (Overnight Call Rate).

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Markets have adjusted their expectations of future short-term interest rates.

Futures-Implied Federal Funds Rate Path

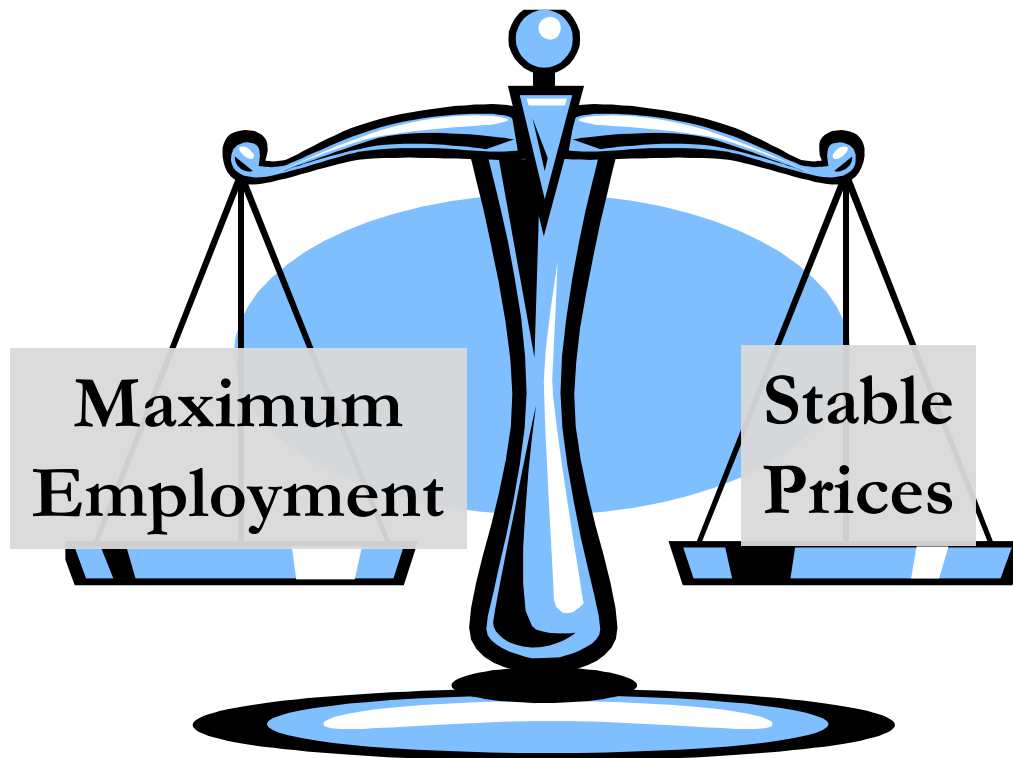


Sources: CME Group and barchart.com.

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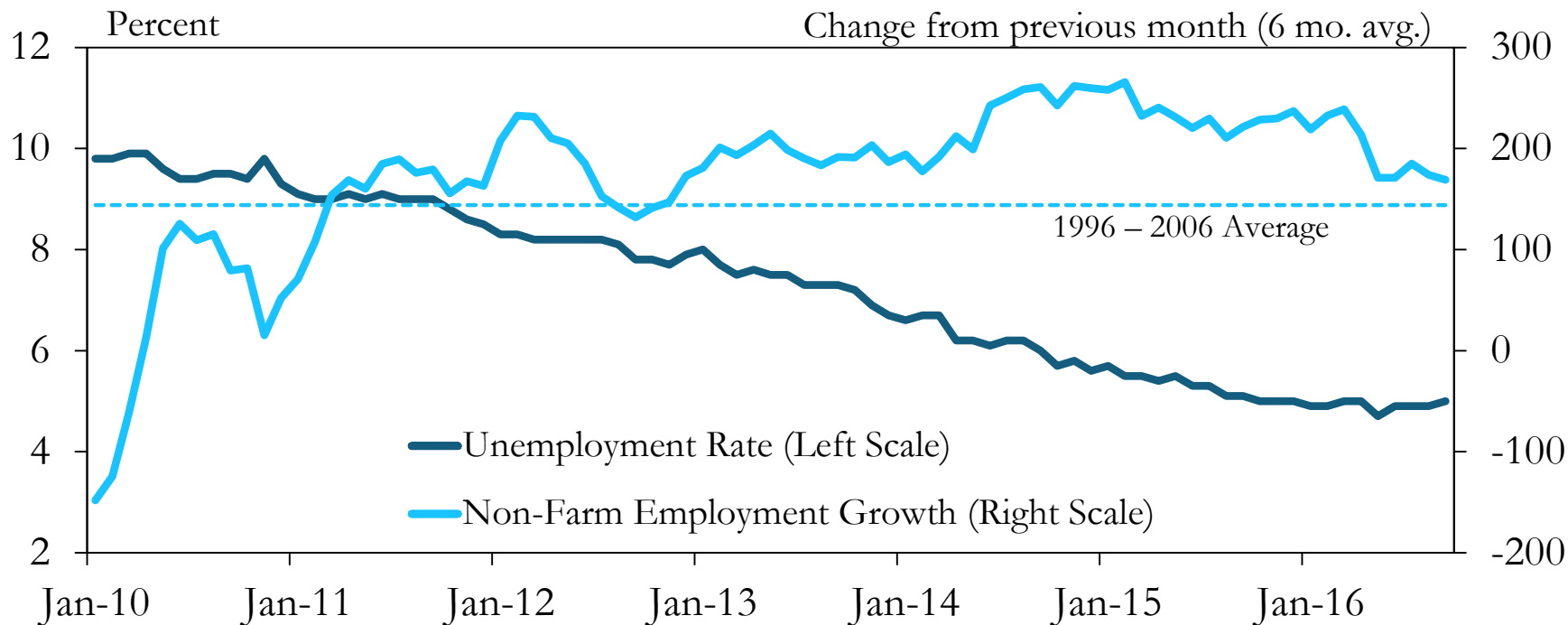
The Fed's monetary policy
is based on a “Dual Mandate”.



... and moderate long-term interest rates.

U.S. labor markets have improved steadily since the Great Recession.

U.S. Unemployment Rate and Job Growth

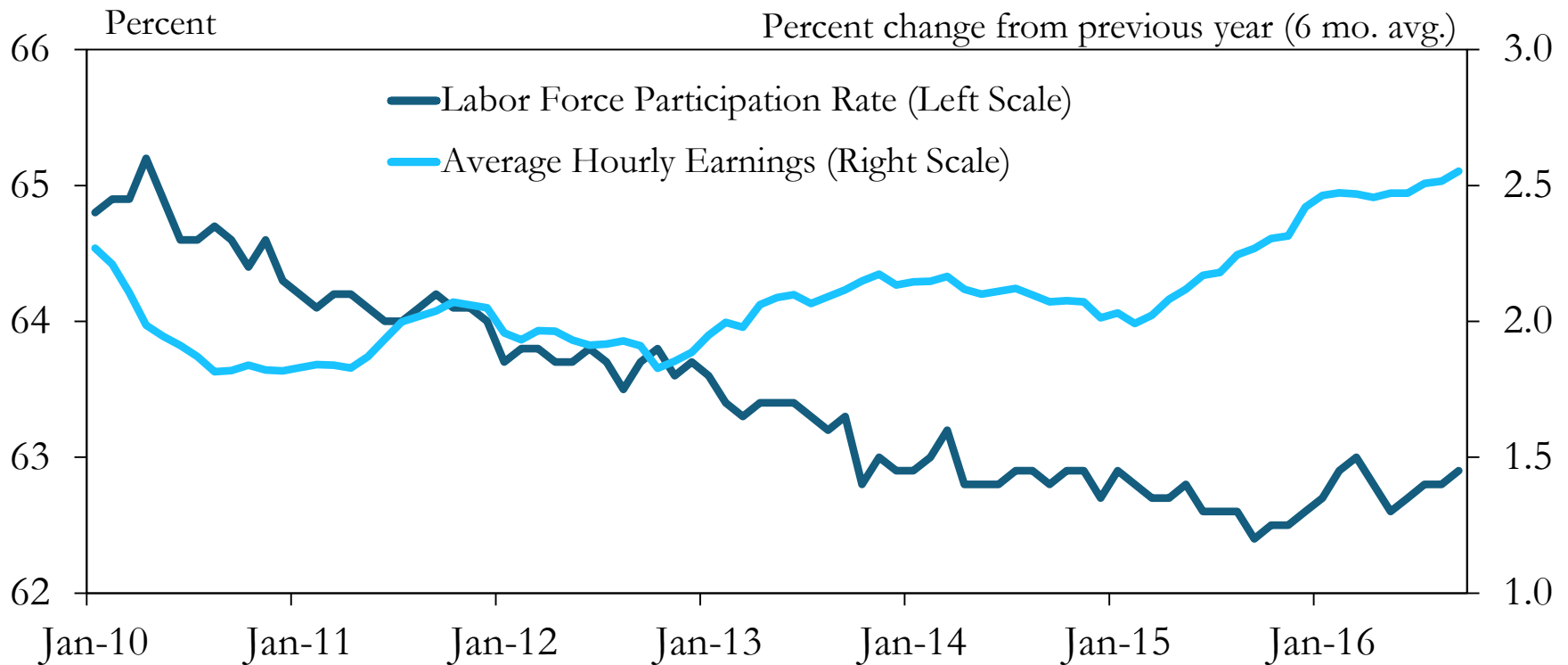


Sources: Bureau of Labor Statistics and Haver Analytics.



Wages have also begun to pick up and labor force participation has steadied somewhat.

U.S. Labor Force Participation and Earnings



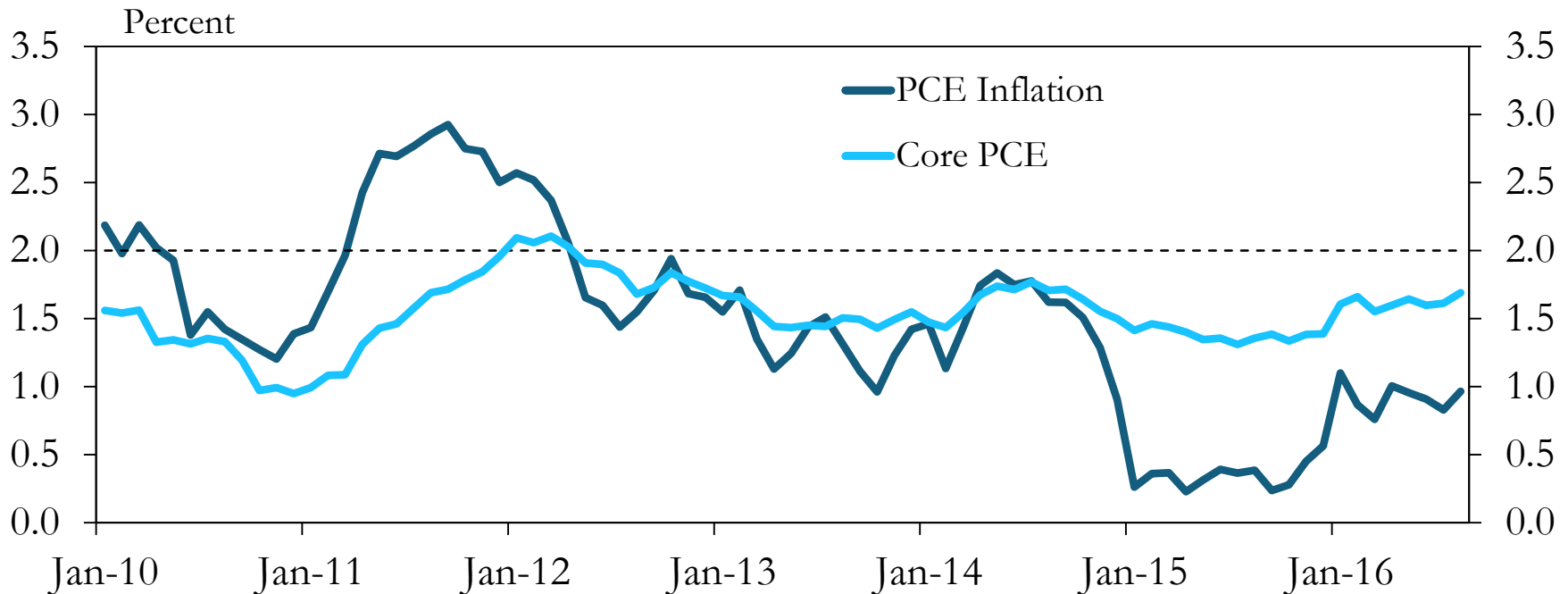
Sources: Bureau of Labor Statistics and Haver Analytics.

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However, inflation has been persistently low.

U.S. Price Indexes



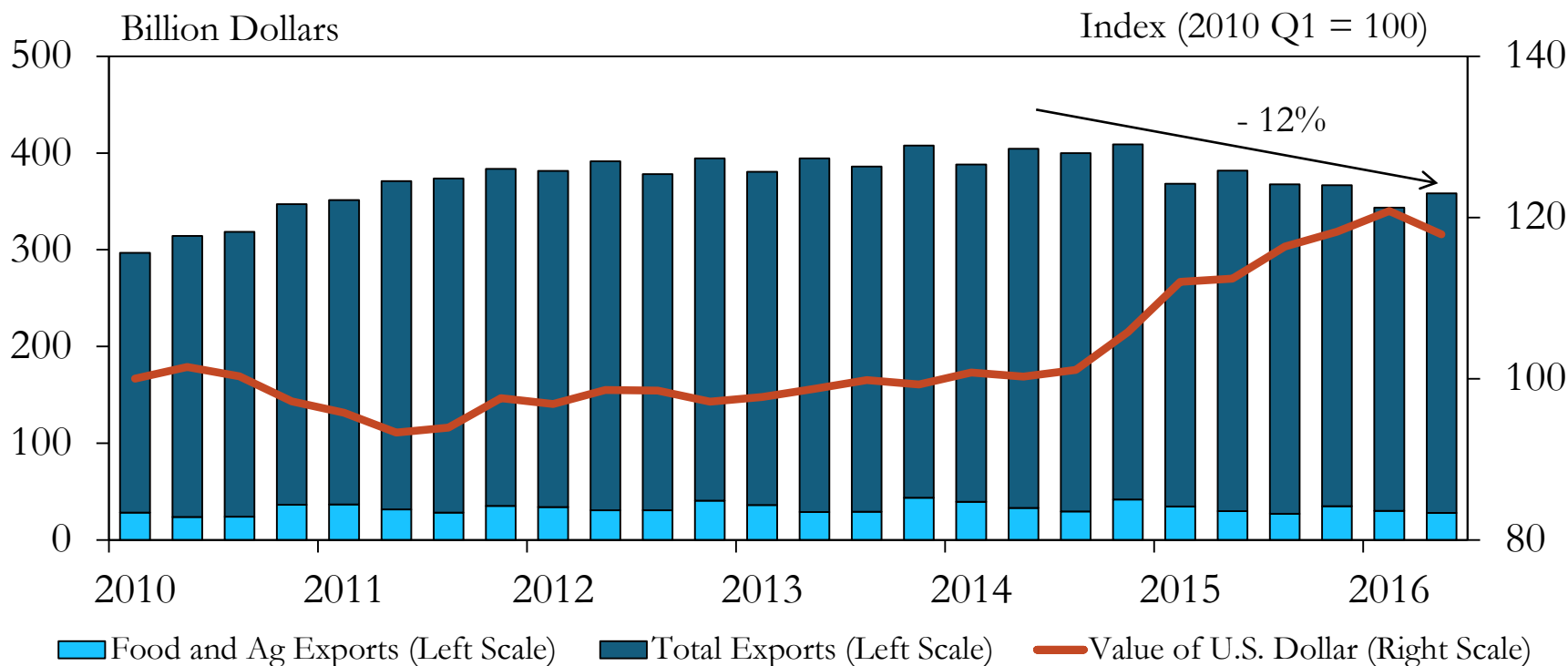
Sources: BEA and Haver Analytics.

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A stronger dollar has reduced inflationary pressure and has been a headwind for export activity.

U.S. Exports and Value of U.S. Dollar



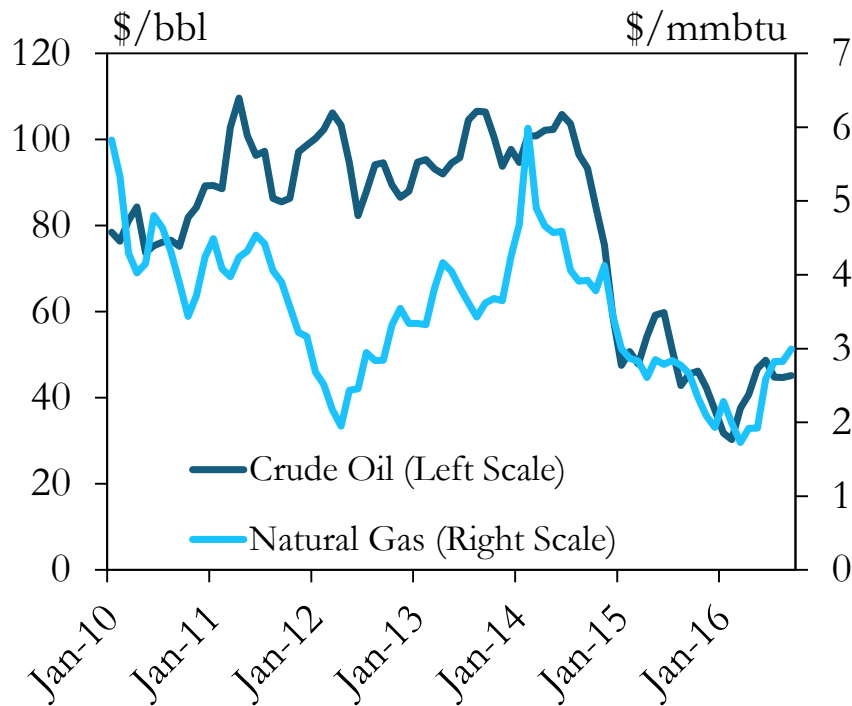
Sources: WiserTrade, U.S. Census Bureau, and Haver Analytics.

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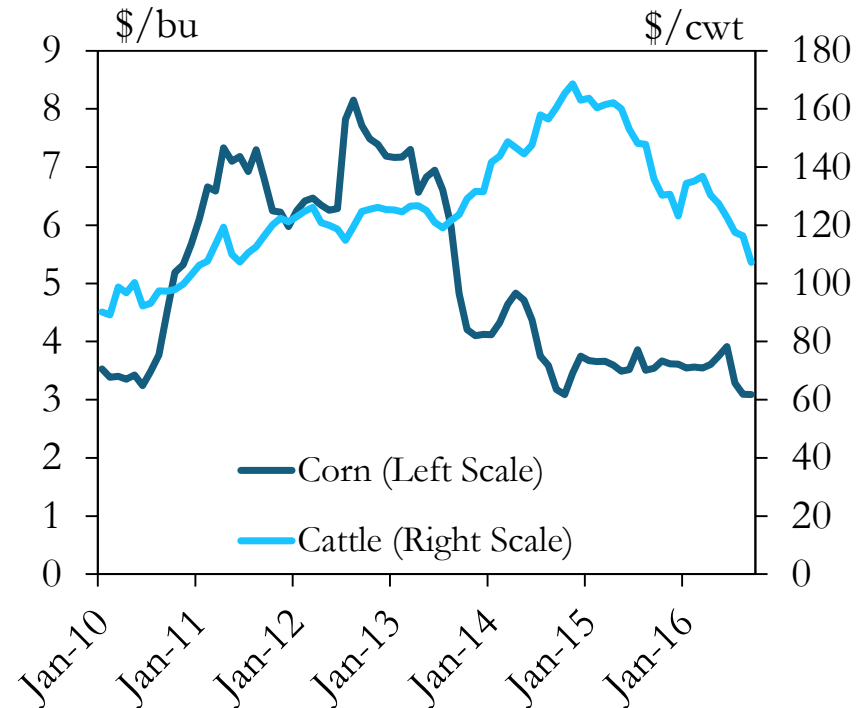
Low commodity prices have also contributed to reduced inflationary pressures.

U.S. Energy Prices



Sources: EIA and Haver Analytics.

U.S. Ag Prices

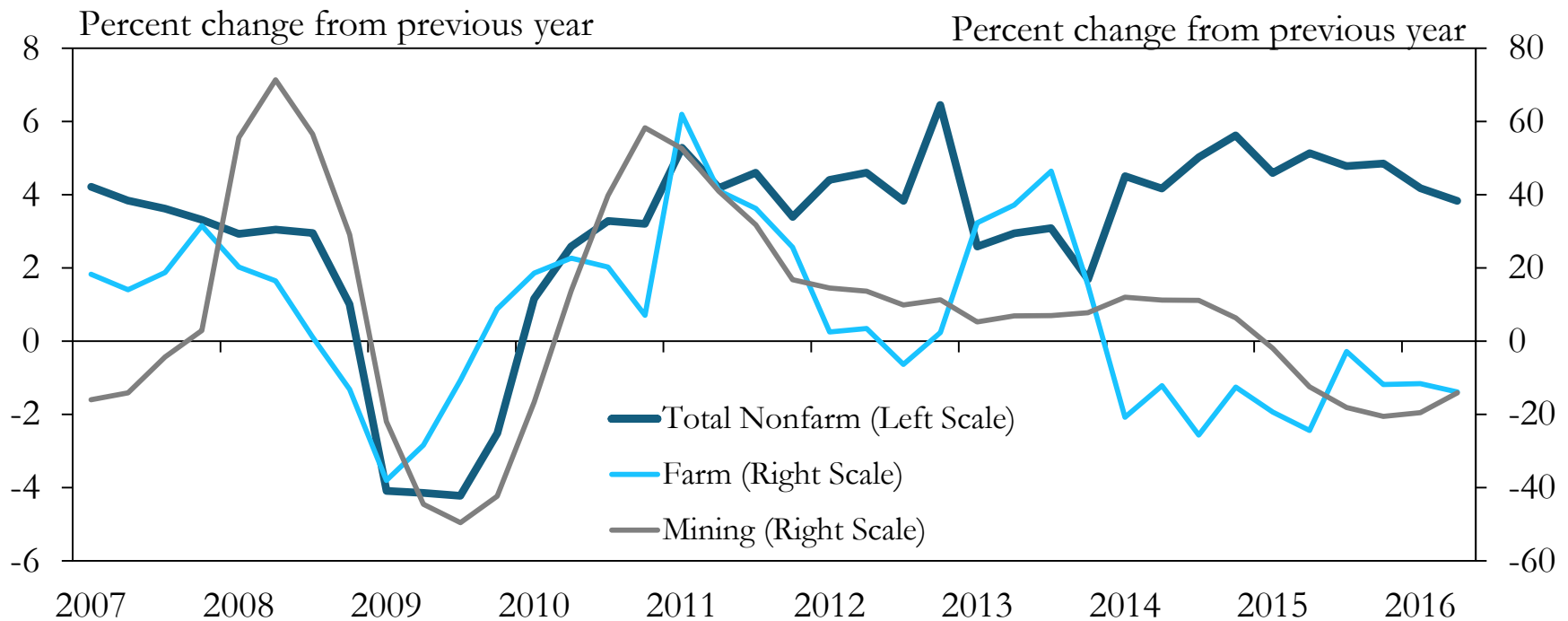


Sources: *Wall Street Journal* and Haver Analytics.



Commodity-based, export-dependent businesses have continued to struggle.

U.S. Earnings by Industry



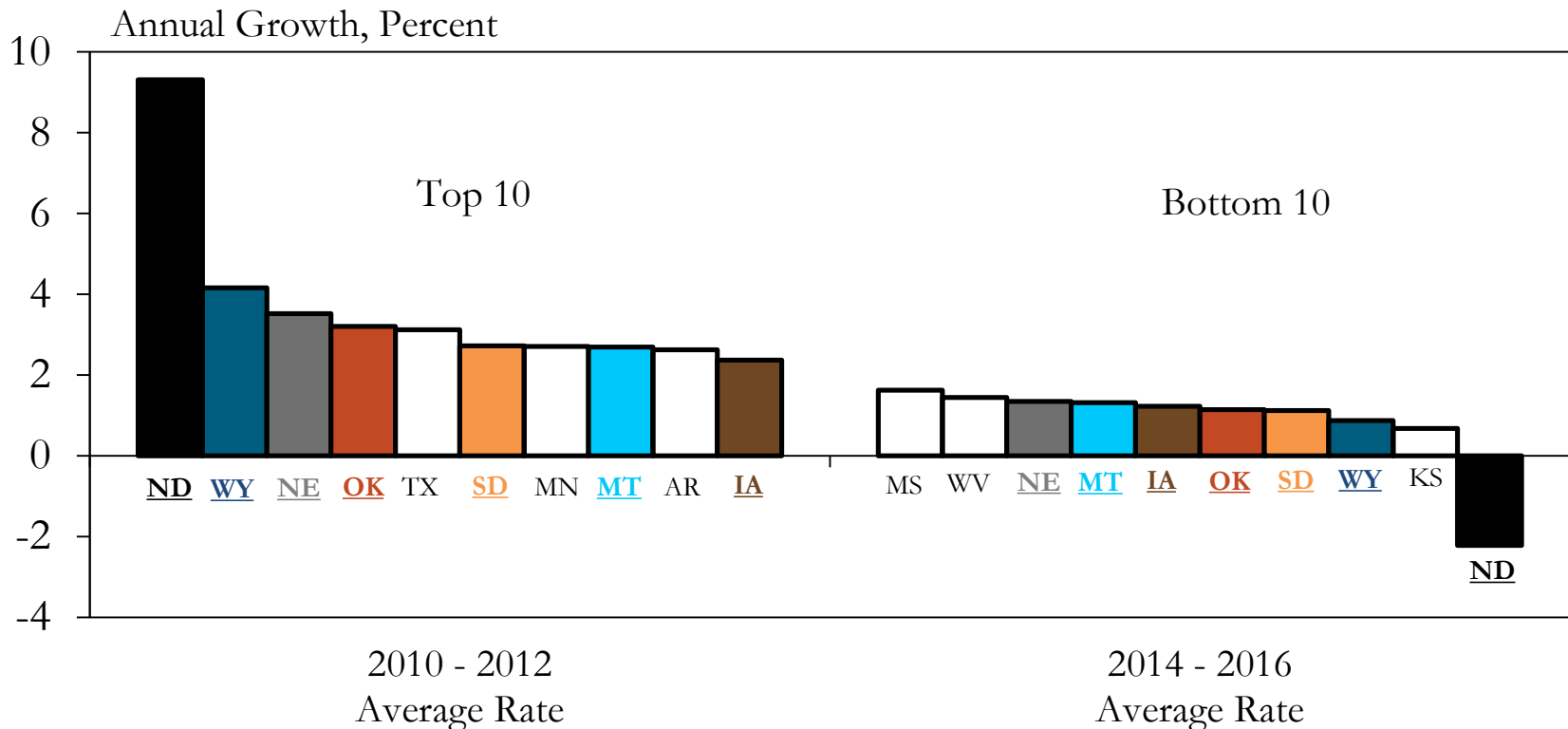
Sources: BEA and Haver Analytics.

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Developments in energy and ag have led to significant swings in personal income growth.

Real Per Capita Personal Income

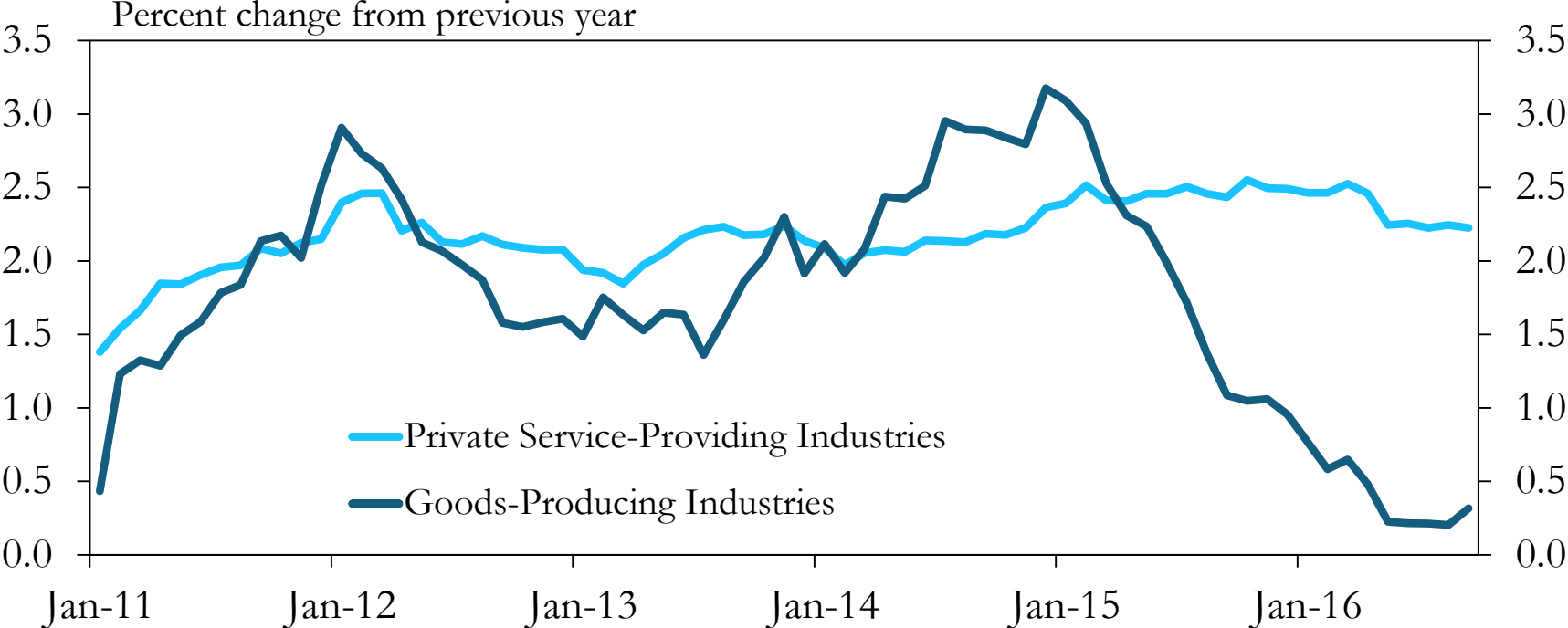


Sources: BEA and Haver Analytics.



Employment growth across sectors has diverged.

U.S. Nonfarm Employment Growth

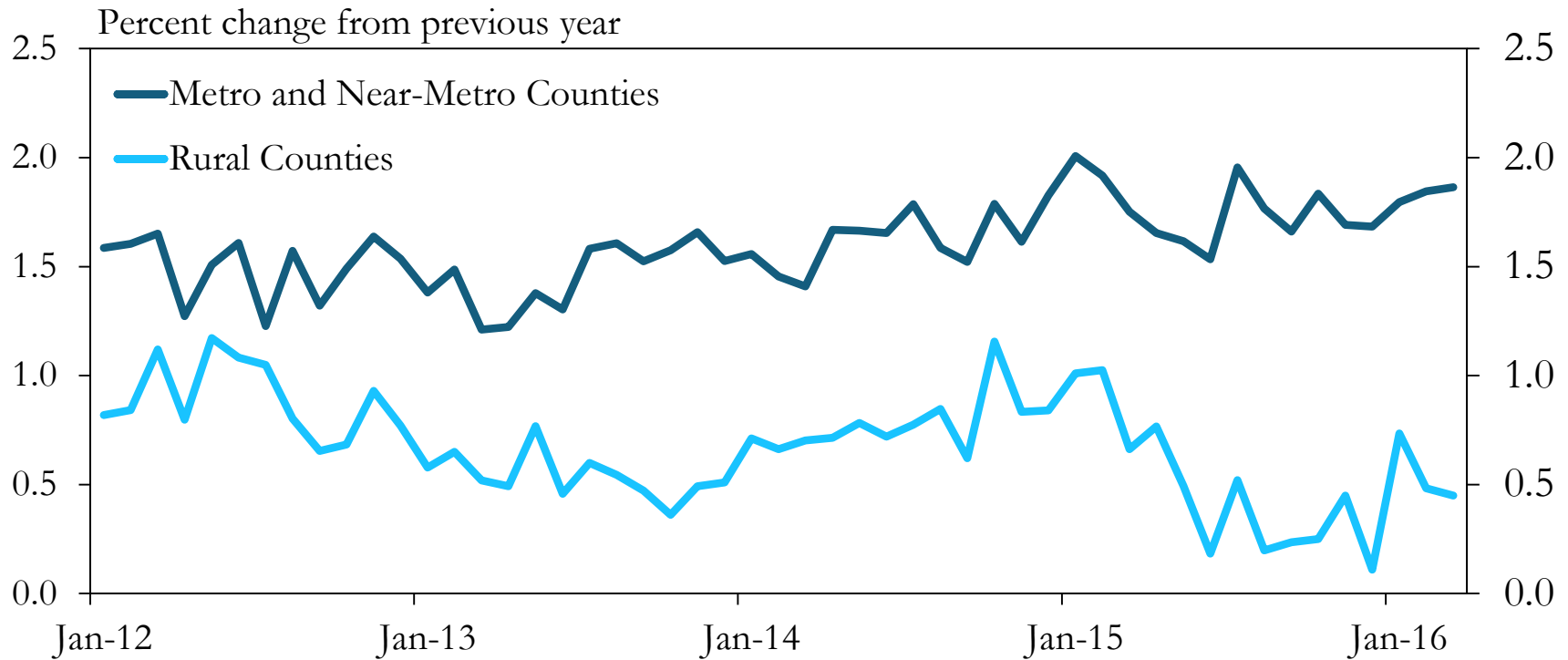


Sources: BLS and Haver Analytics



The gap between metro and rural employment growth has also widened.

Median State Employment Growth by County Type



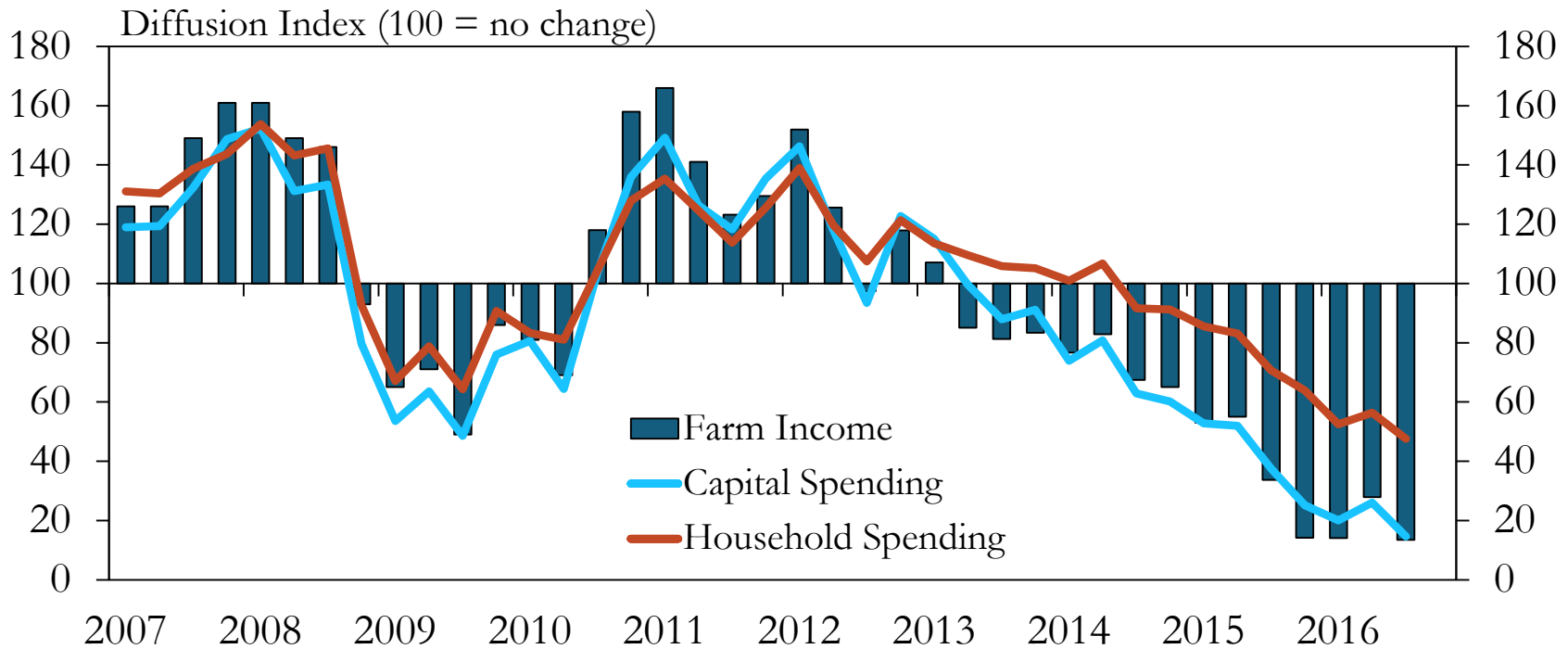
Source: BLS.

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Farm income and spending have continued to trend lower.

Farm Income and Spending KC Fed District



Source: Federal Reserve Bank of Kansas City

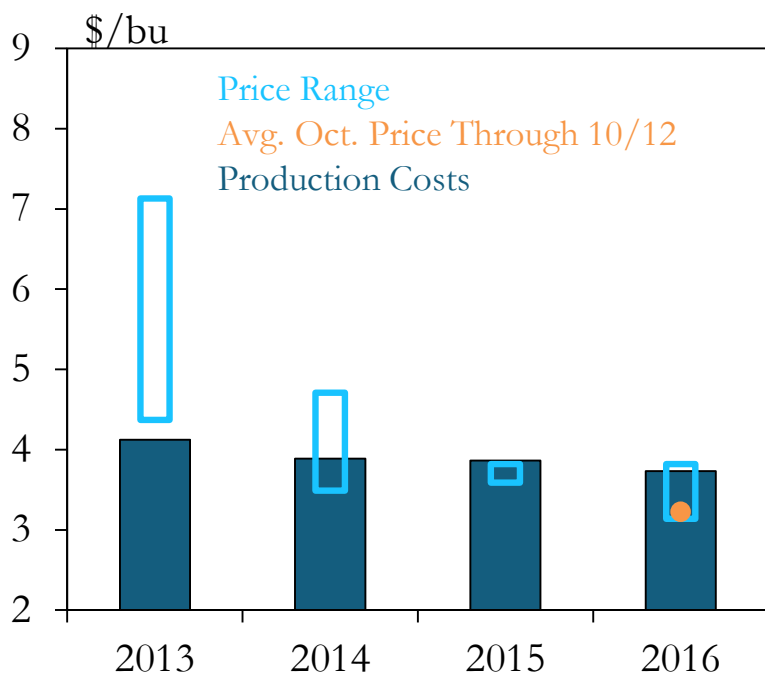
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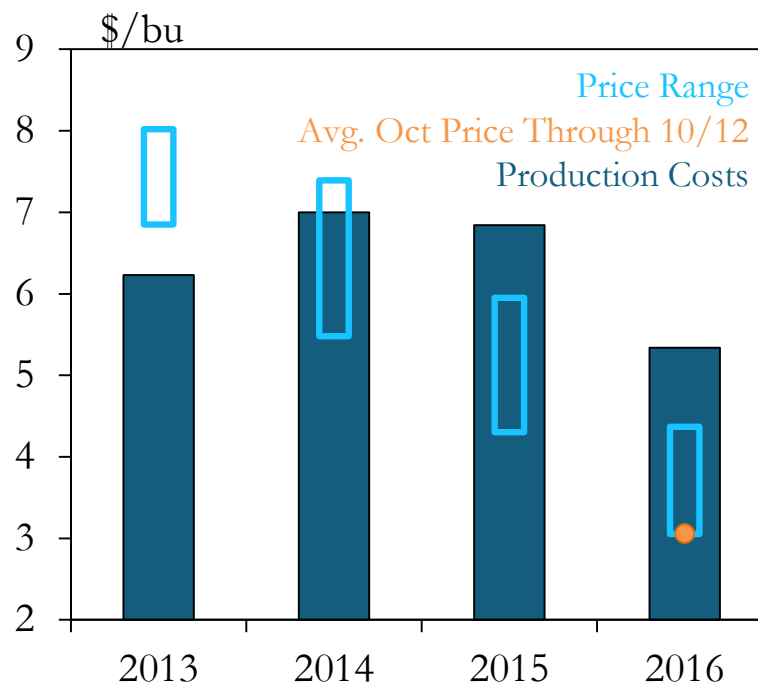
Profit margins in the crop sector have remained weak.

U.S. Crop Sector Profit Margins

Corn



Wheat



Sources: USDA and Haver Analytics.

Note: Production costs are calculated from USDA's Economic Research Service (Commodity Costs and Returns) and national yield averages for each year shown, but exclude the opportunity cost of unpaid labor from the calculation.

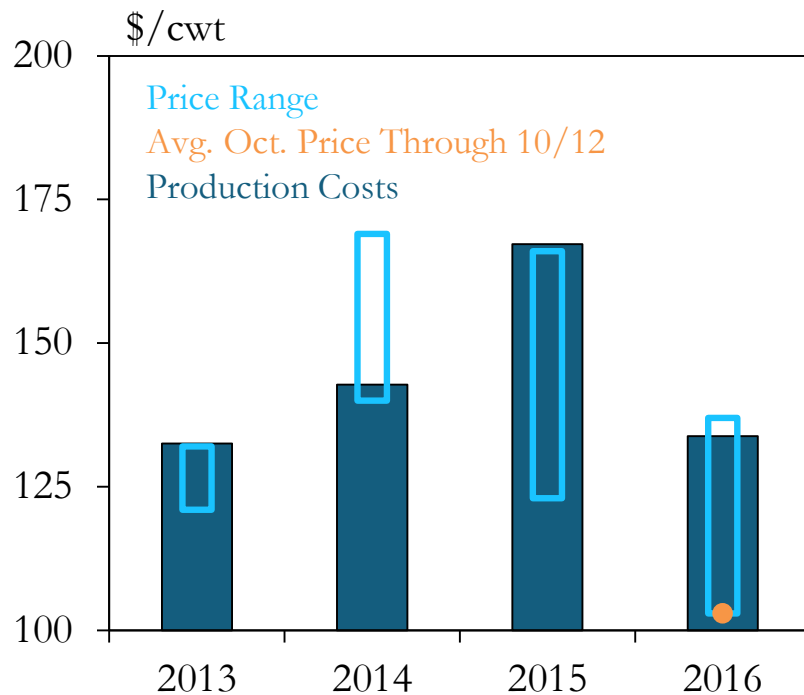
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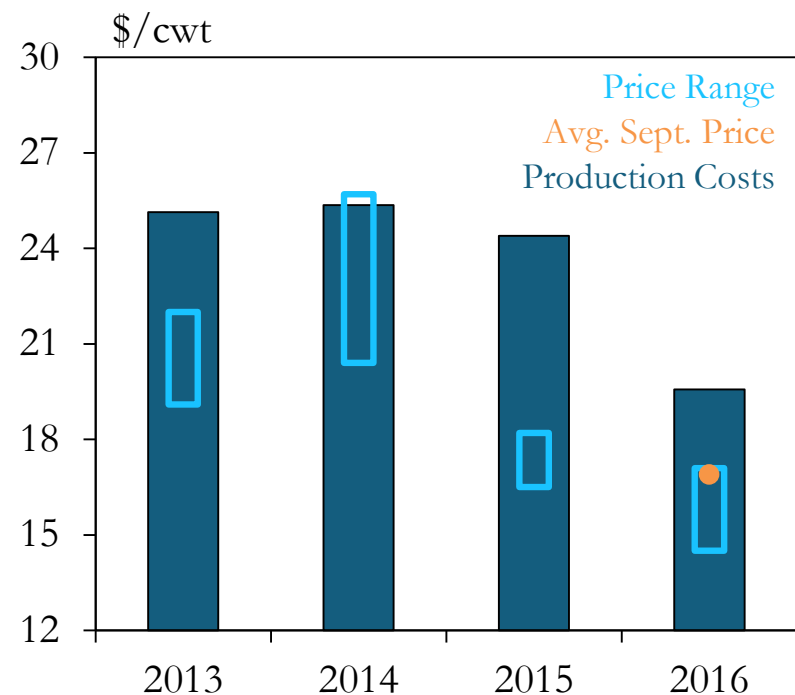
Livestock sector profits have also been poor.

U.S. Livestock Sector Profit Margins

Cattle



Dairy



Sources: USDA and Haver Analytics.

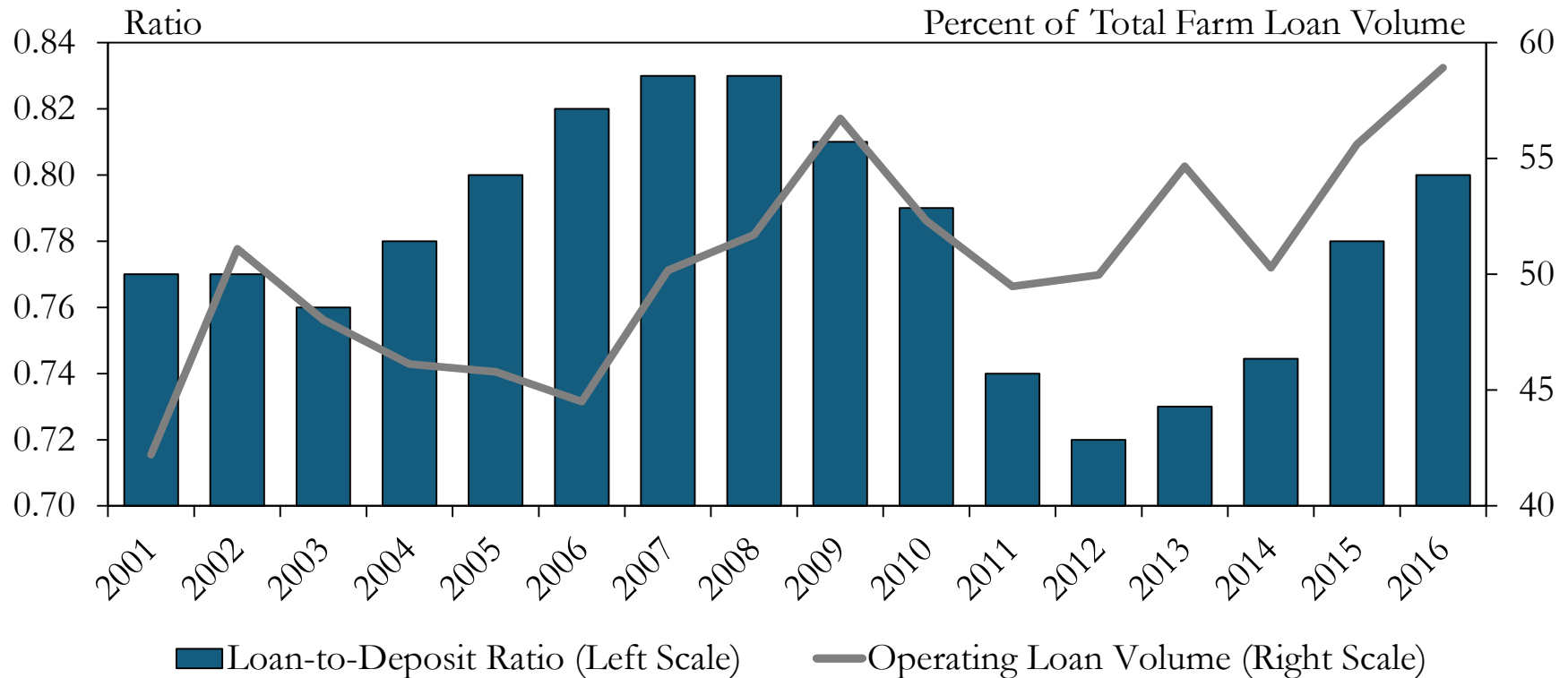
Note: Production costs are calculated from USDA's Economic Research Service (Commodity Costs and Returns) and national yield averages for each year shown, but exclude the opportunity cost of unpaid labor from the calculation.

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Reduced cash flow has sparked persistent increases in demand for financing.

Farm Lending at Agricultural Banks



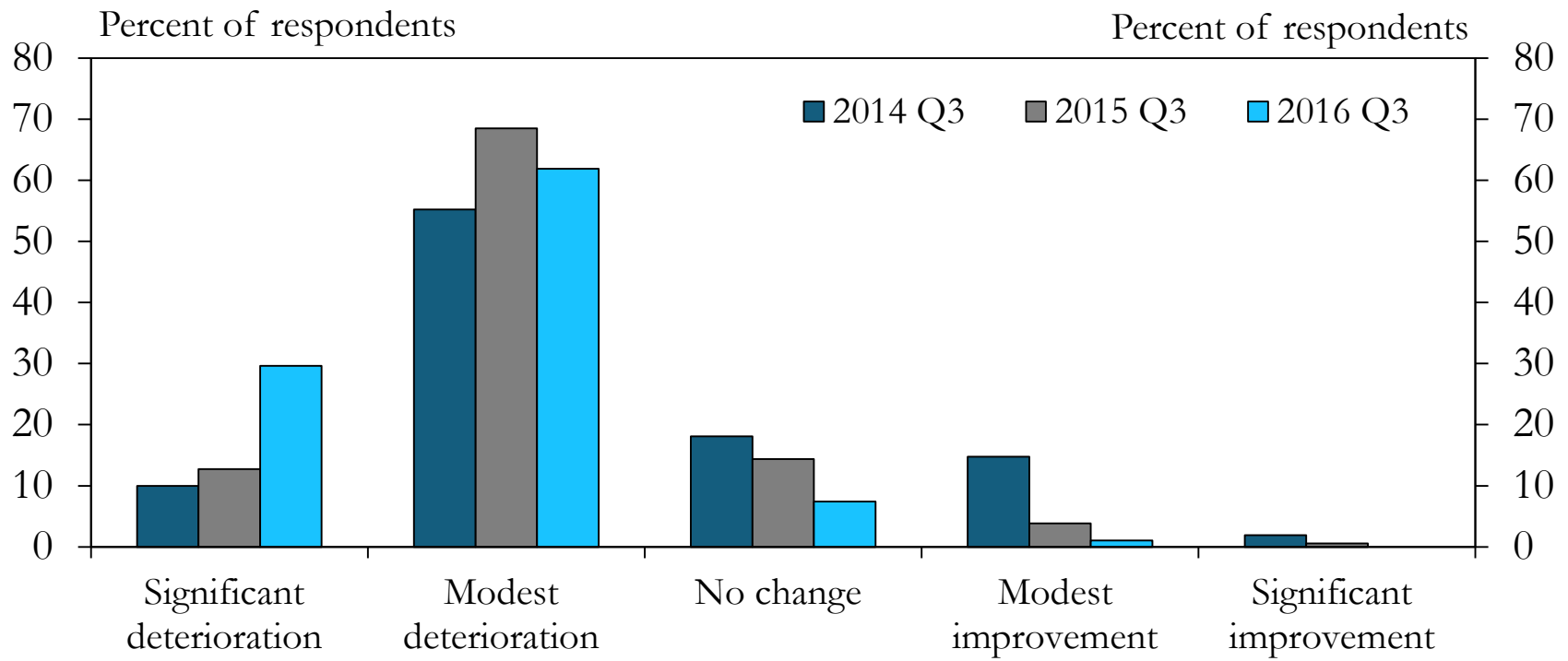
Source: Federal Reserve Bank of Kansas City, Agricultural Finance Databook

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Borrower liquidity has deteriorated more notably in 2016.

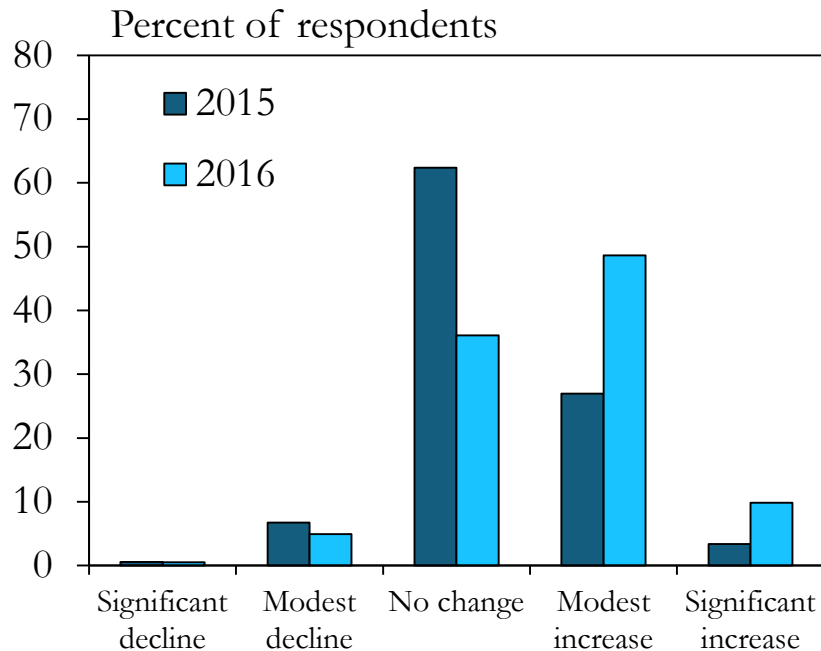
Change in Level of Working Capital Crop Producers: KC Fed District



Lenders have also recognized heightened risk in their farm loan portfolios.

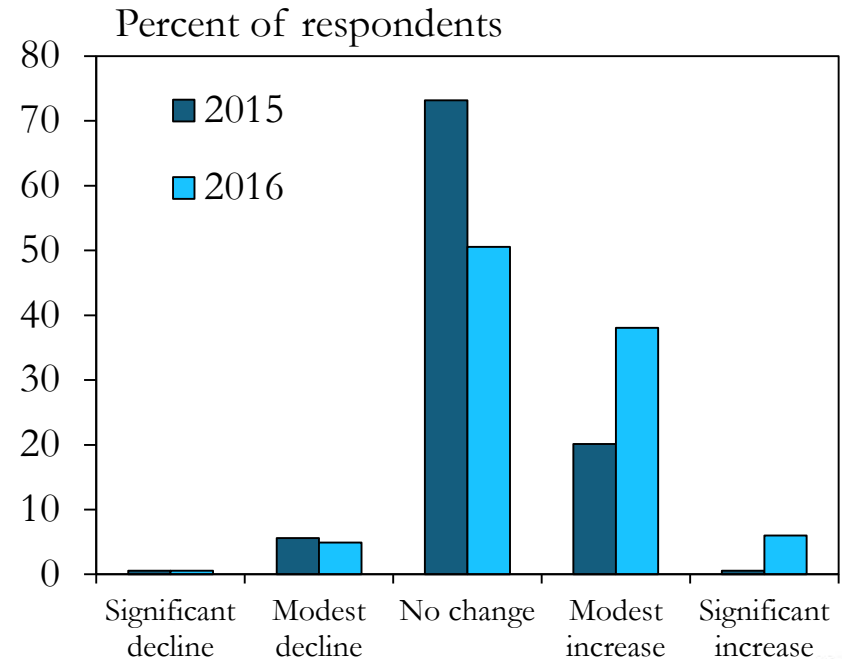
Change in Ag Bank “Watch” and “Classified” Lists KC Fed District

Watch List



Source: Federal Reserve Bank of Kansas City

Classified List

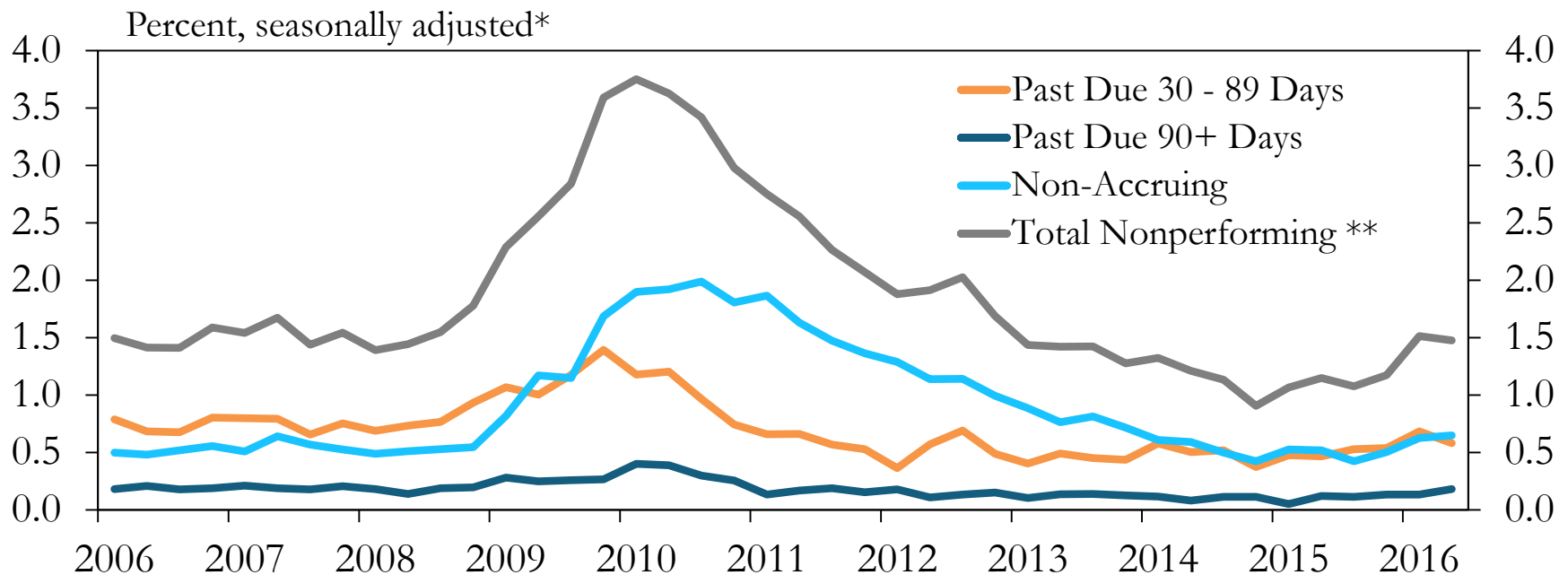


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Farm loan delinquency rates have remained low, but have edged up slightly.

Past Due and Non-Accruing Farm Loans at Commercial Banks



* Percent of all outstanding non-real estate farm production loans at commercial banks.

** Total nonperforming loans includes the share of all past due, non-accruing and net charge-off loans.

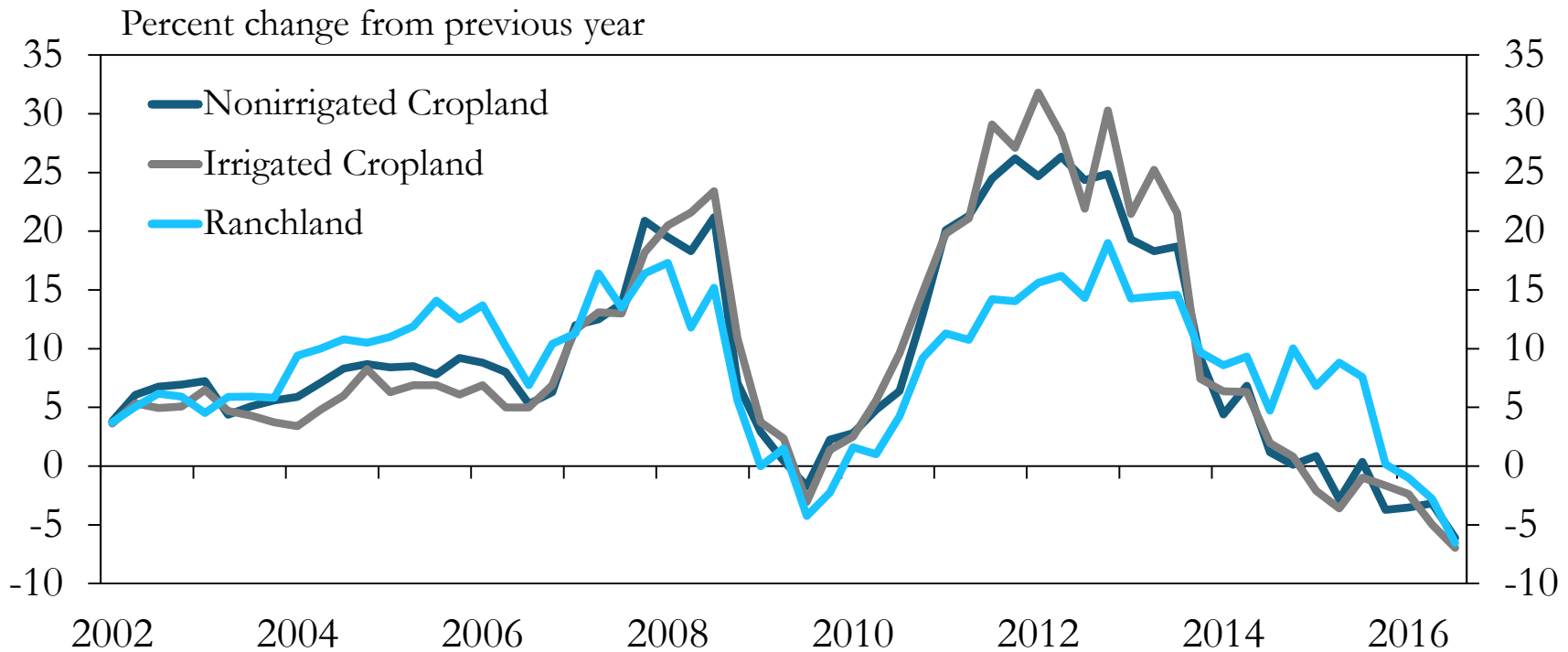
Source: Federal Reserve Bank of Kansas City's Agricultural Finance Databook.

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Farmland values have generally remained strong,
but pressure has been building.

Changes in Farmland Values KC Fed District



Source: Federal Reserve Bank of Kansas City

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Concluding Remarks

- The U.S. economy continues to expand modestly, but growth has often been weaker than initially expected.
- Economic growth has diverged. Commodity-dependent, rural, and export-based regions or industries have struggled.
- Risk in the ag economy has continued to build, but gradually.

What will the next farm loan renewal season look like?



Questions?

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