



National Economic Outlook

March 23, 2011

Yelena Takhtamanova, Economist
Federal Reserve Bank of San Francisco

Overview

1. Current national situation

- Economy is expanding
- Pace of recovery has picked up
- Large amount of slack remains

2. FRBSF national economic forecast

- Output and inflation

3. Monetary policy outlook

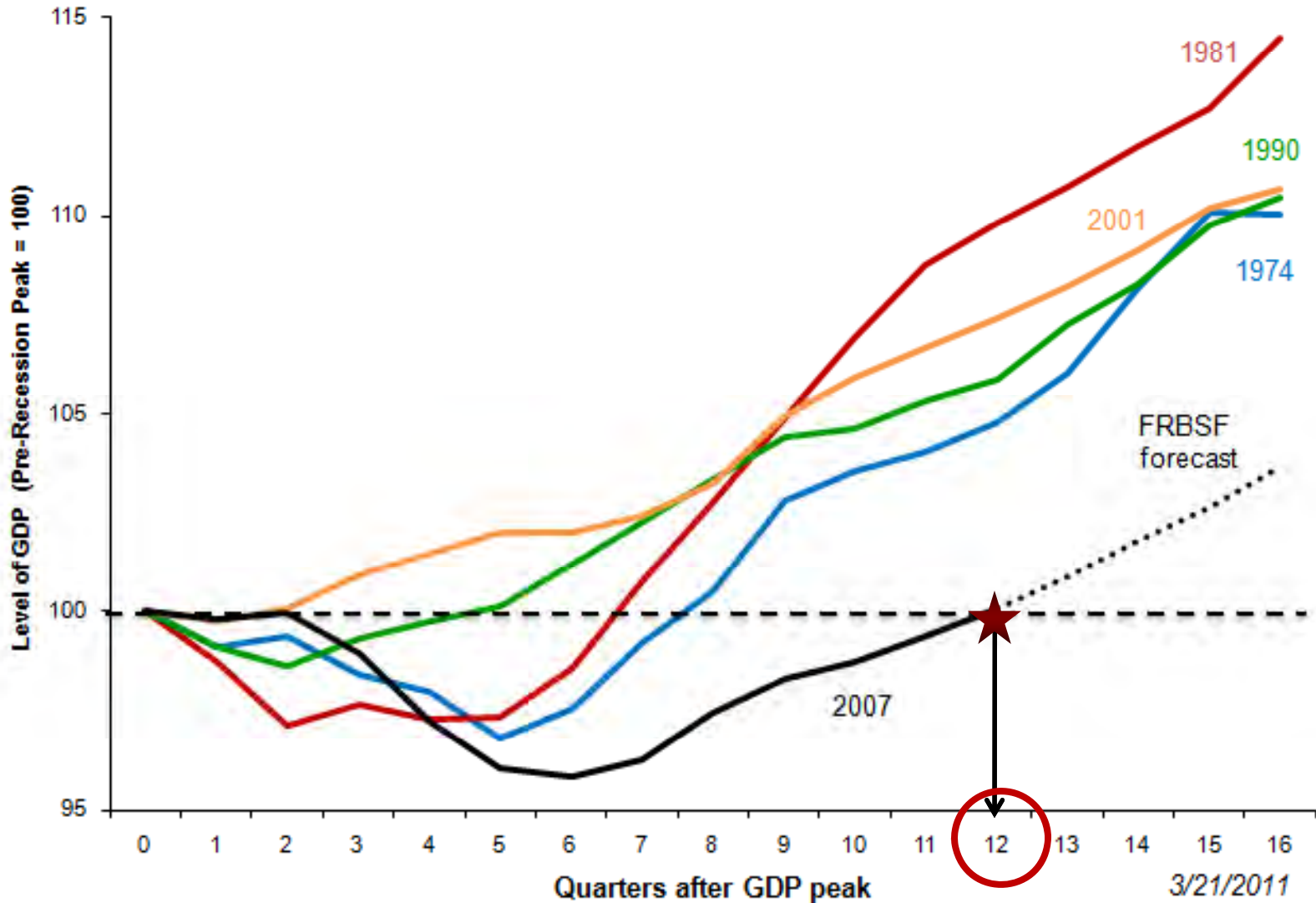
- Conventional and unconventional tools

CURRENT NATIONAL SITUATION

These remarks represent my views and not necessarily those of my colleagues in the Federal Reserve System and the Federal Reserve Bank of San Francisco.

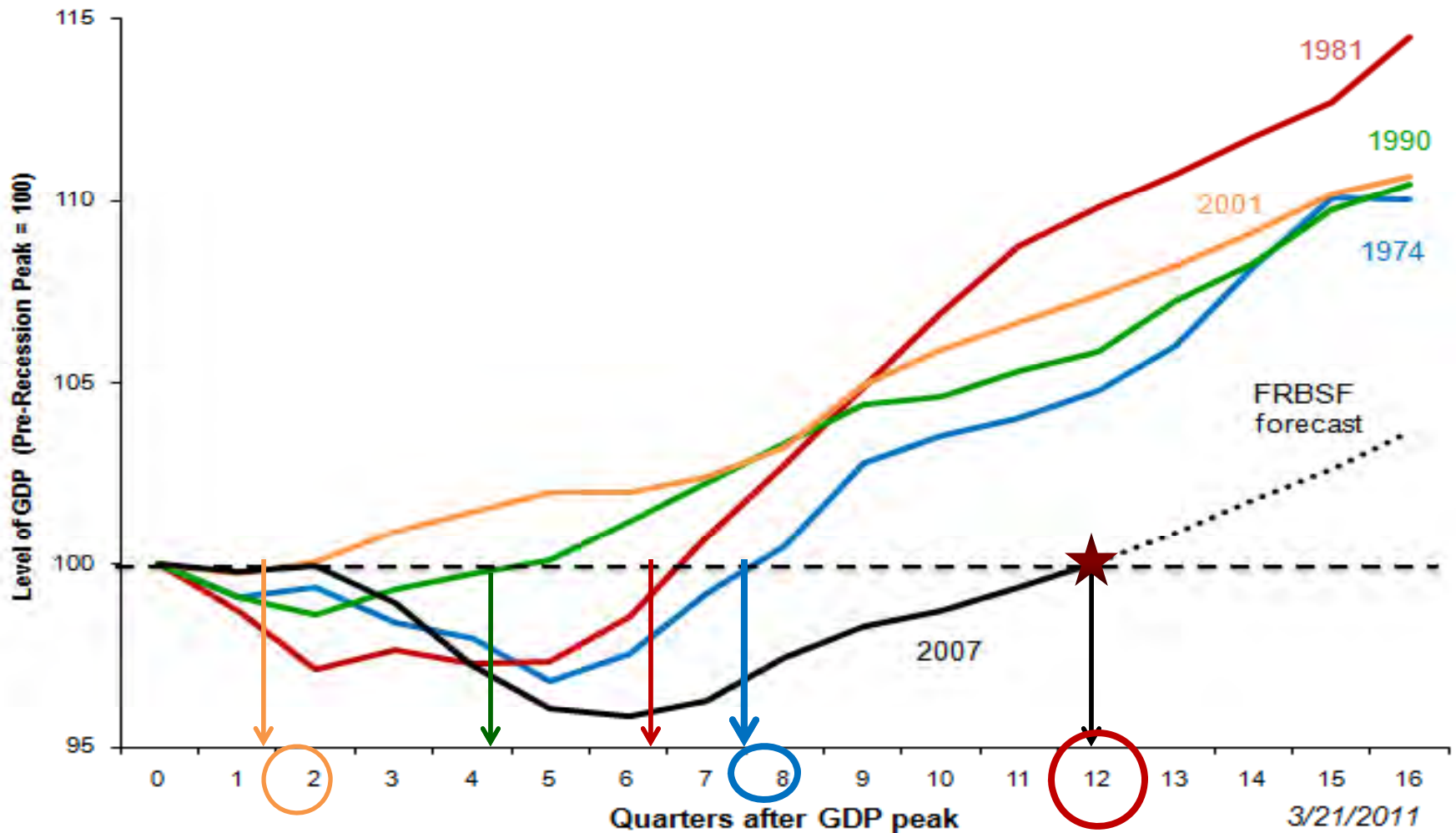
So Far, Only a Moderate Recovery From The Longest and Deepest Post-War Recession

FRBSF Forecast Relative to Previous Recessions



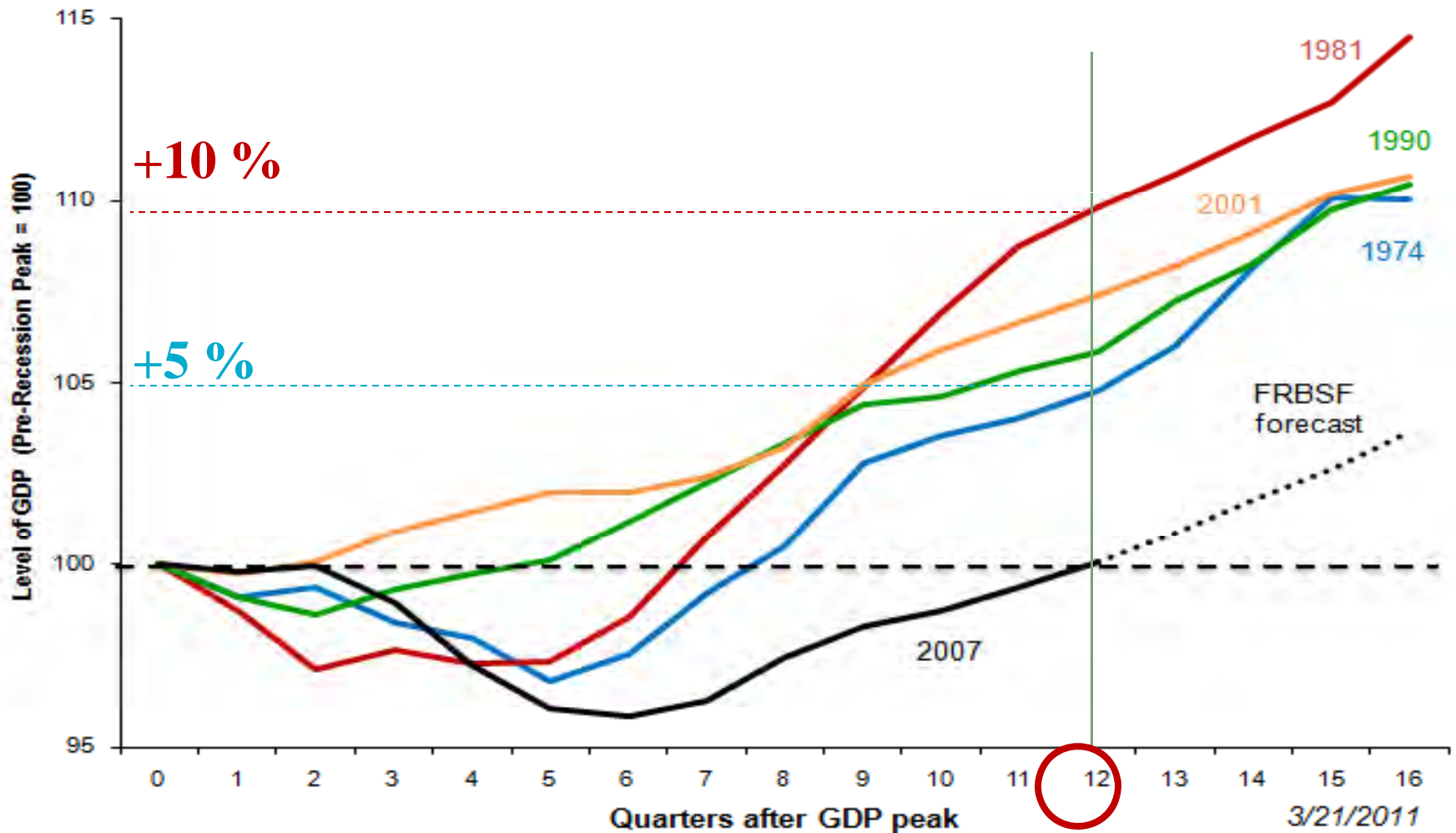
Moderate Recovery From The Longest Post-War Recession: Three Years to Climb Back

FRBSF Forecast Relative to Previous Recessions



Moderate Recovery From The Deepest Post-War Recession: Lagging Behind Earlier Recoveries

FRBSF Forecast Relative to Previous Recessions

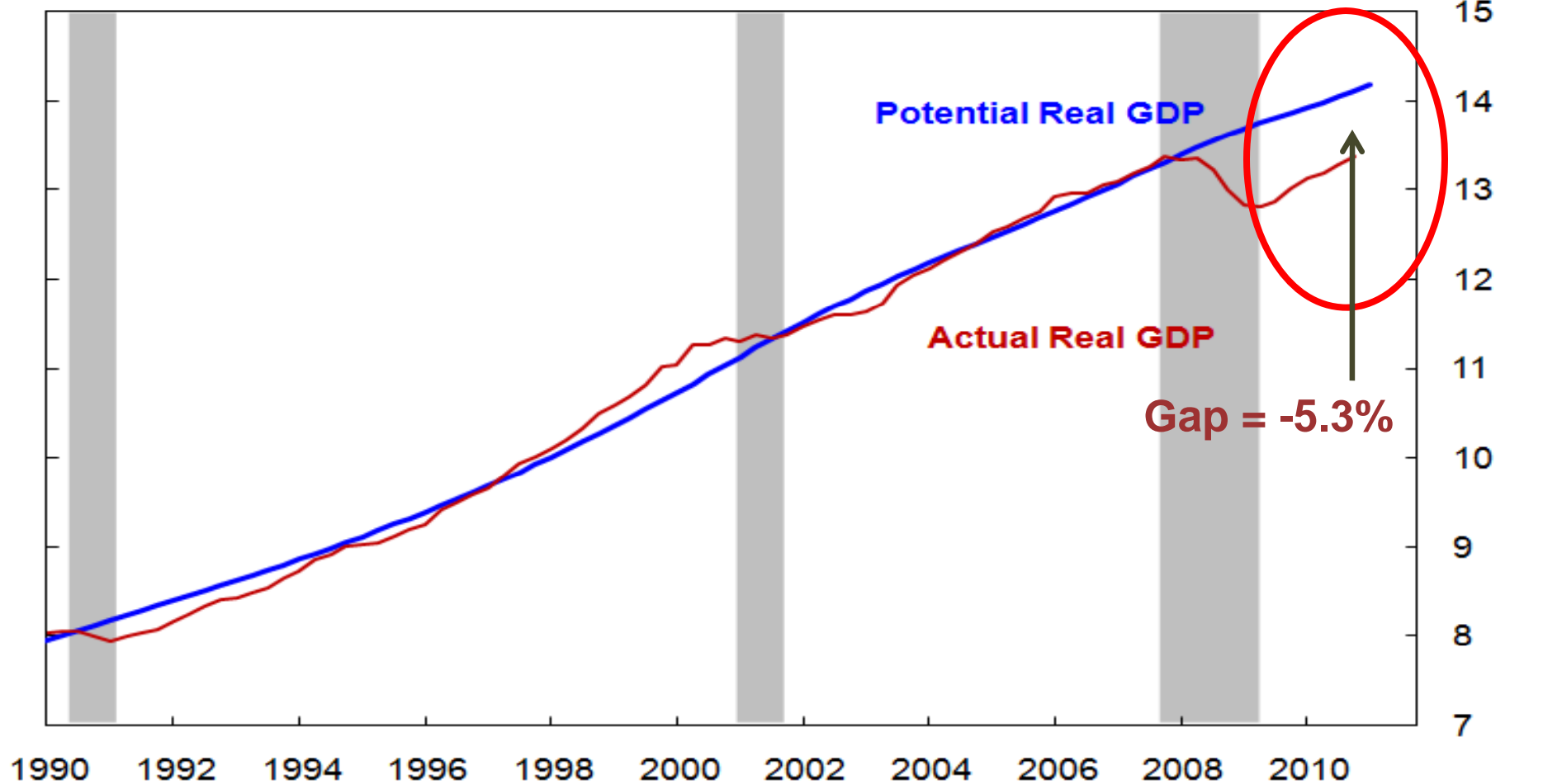


The Deep Recession and Mild Recovery Resulted in an Economy Operating Well Below Capacity

Actual Real GDP versus Potential Real GDP

Trillions of chained 2005\$; SAAR

\$Trillion



Source: Bureau of Economic Analysis, Congressional Budget Office

3/16/2011

*Several Developments Give Reason
to Expect More Rapid Growth in 2011*

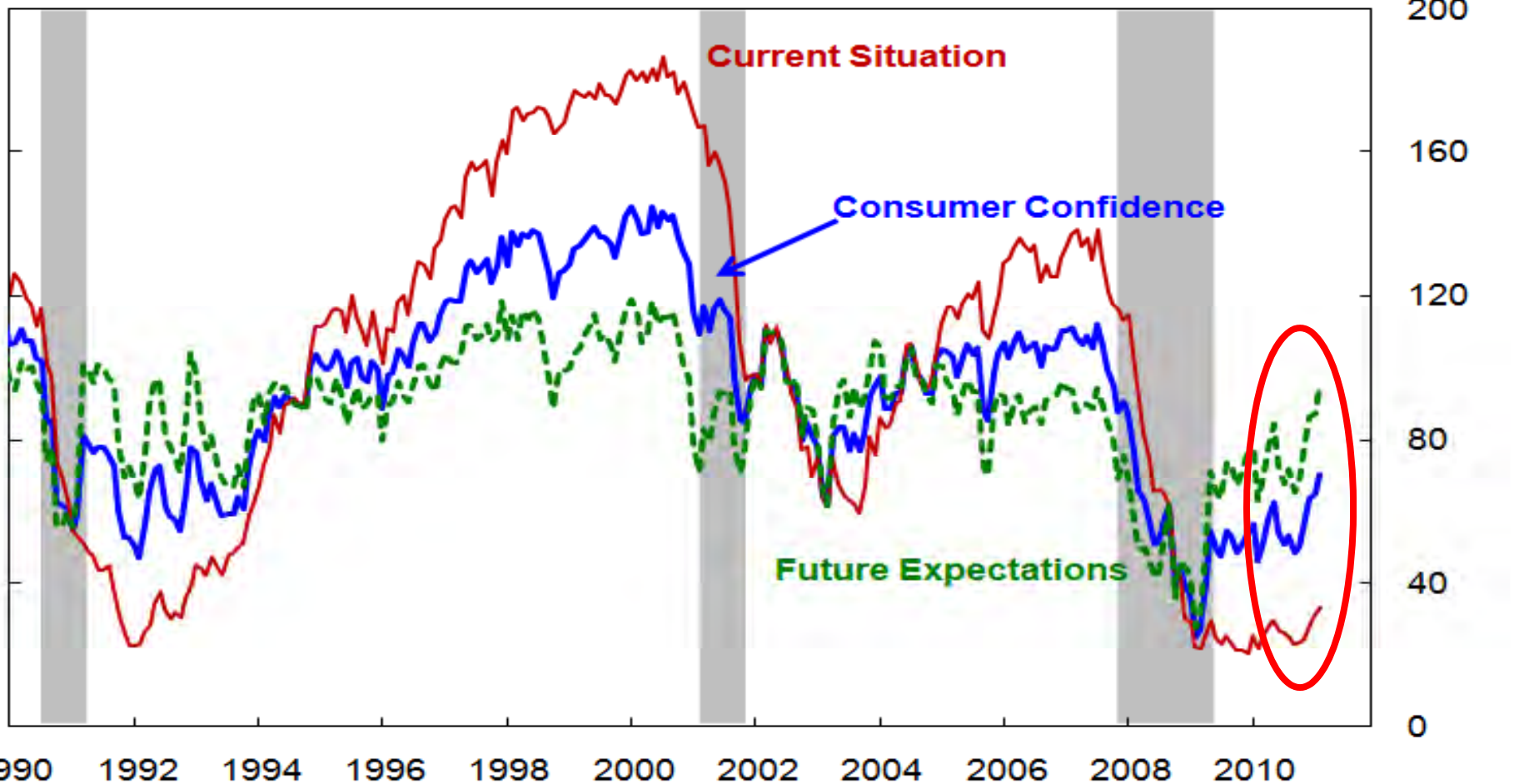
- **Improving household and business confidence**
- **Pent-up demand for durable goods**
- **Some thawing of tight credit conditions**
- **Accommodative monetary policy**

Although Concerns Remain Evident in Survey Data, Consumer Sentiment Improves

Consumer Confidence Index and Components

Monthly index values

Index values



Source: The Conference Board

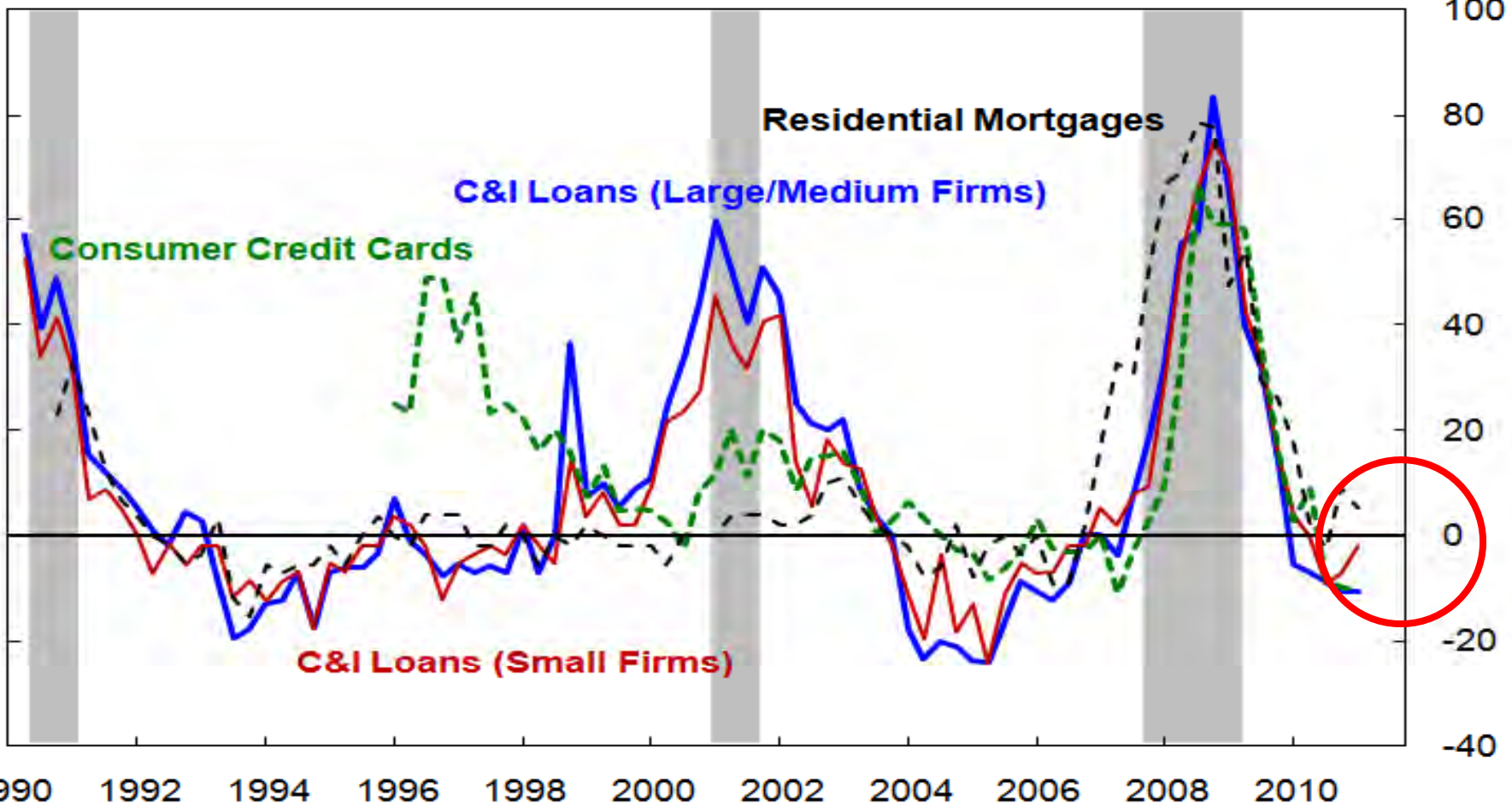
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Although Credit Remains Tight, U.S. Bank Lending Standards Continue to Show Some Loosening in 2010 – Residential Lending Is the Exception

FRB Sr. Loan Officer Opinion Survey by Loan Type

Net percentage reporting tightening of lending standards

Percent
100



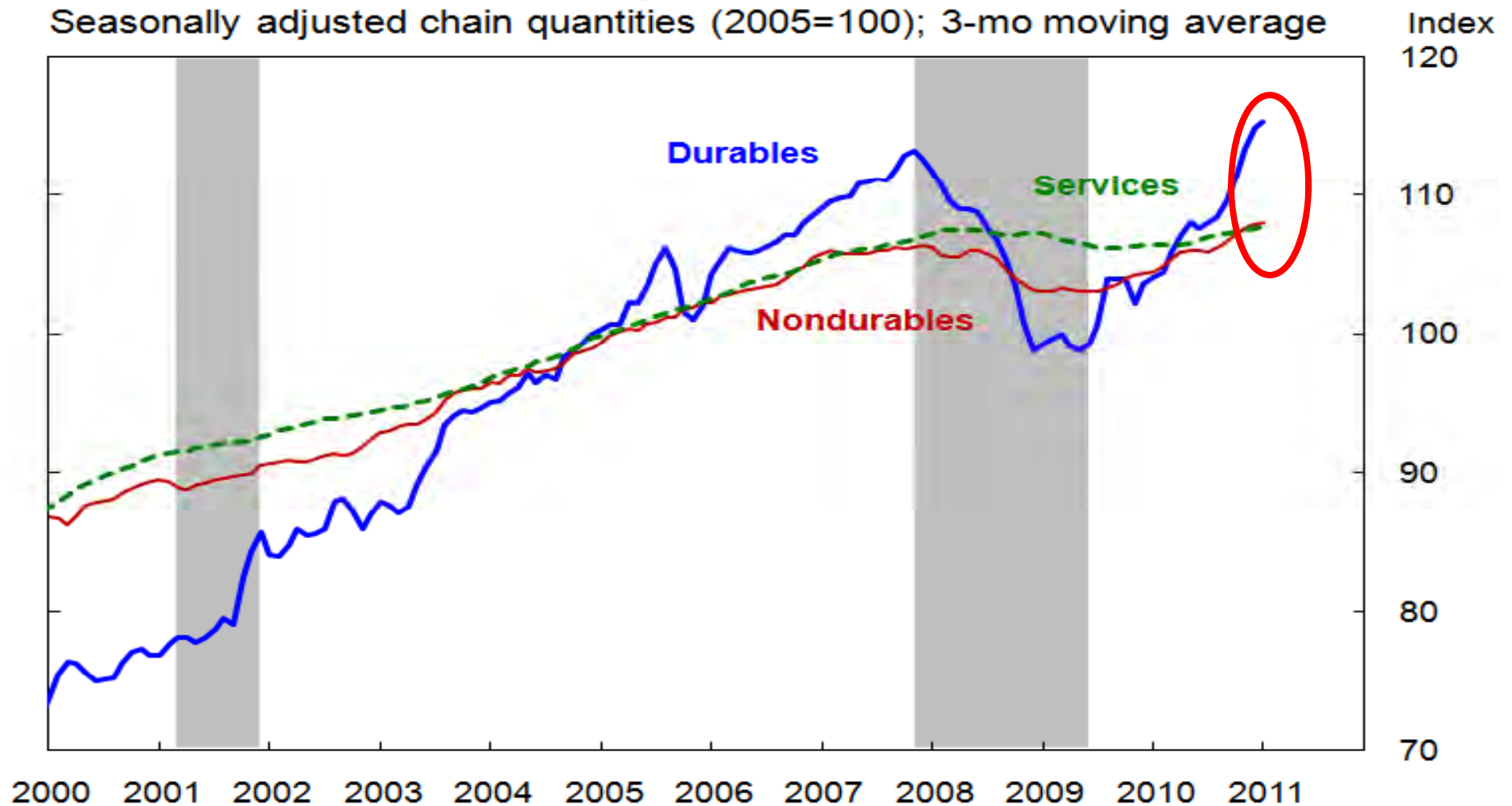
Source: Federal Reserve Board

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Consumer Spending Has Climbed to Pre-Recession Levels – Holiday Season Was Best Since 2006

Real Personal Consumption Expenditures

Seasonally adjusted chain quantities (2005=100); 3-mo moving average



Source: Bureau of Economic Analysis

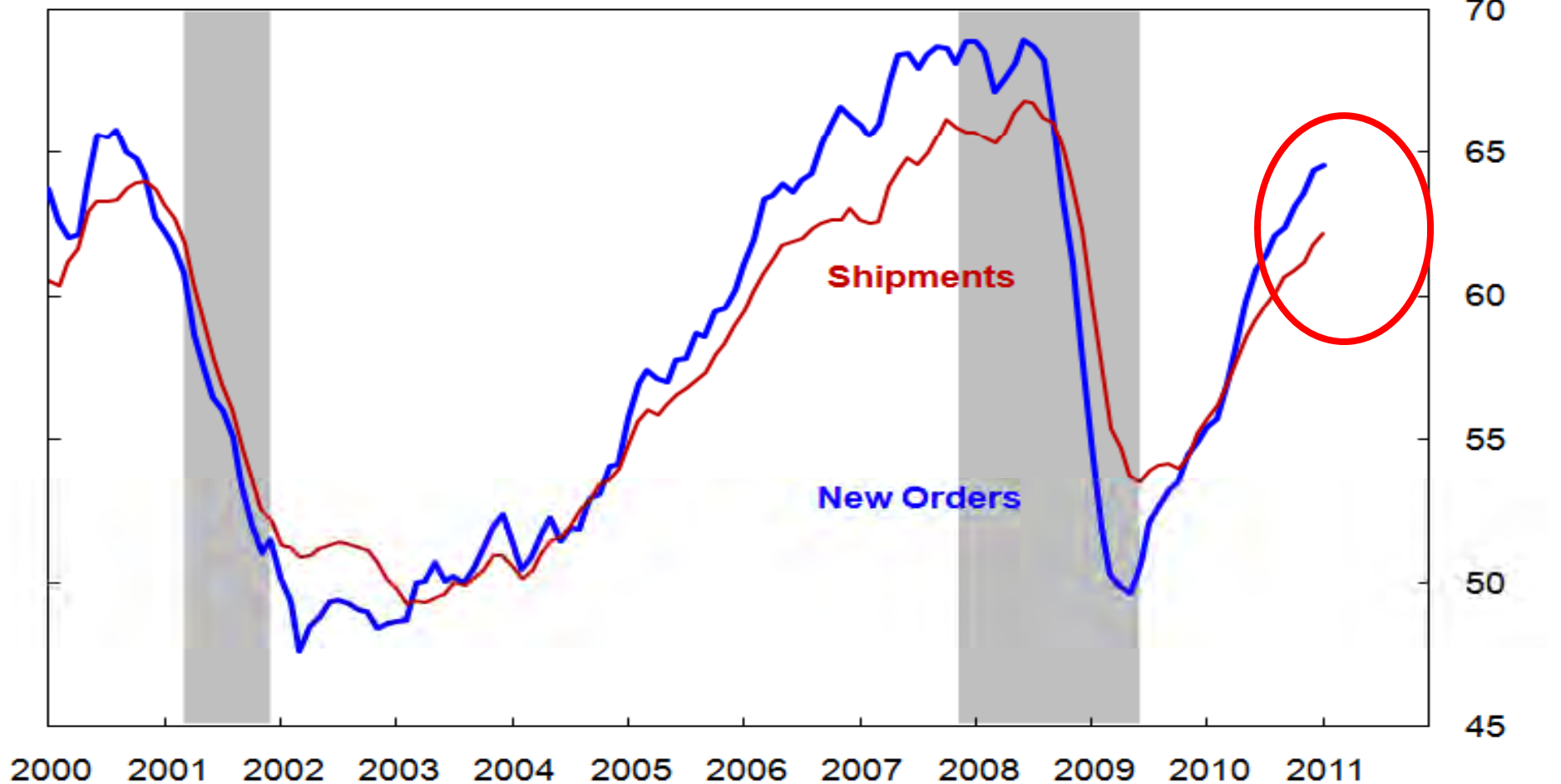
3/16/2011

Although Business Spending Remains Below Peak Levels, It Has Rebounded and the Outlook Is Favorable

Non-Defense Capital Goods (Ex Aircraft)

Three month moving average; seasonally adjusted

Billions\$



Source: Census Bureau

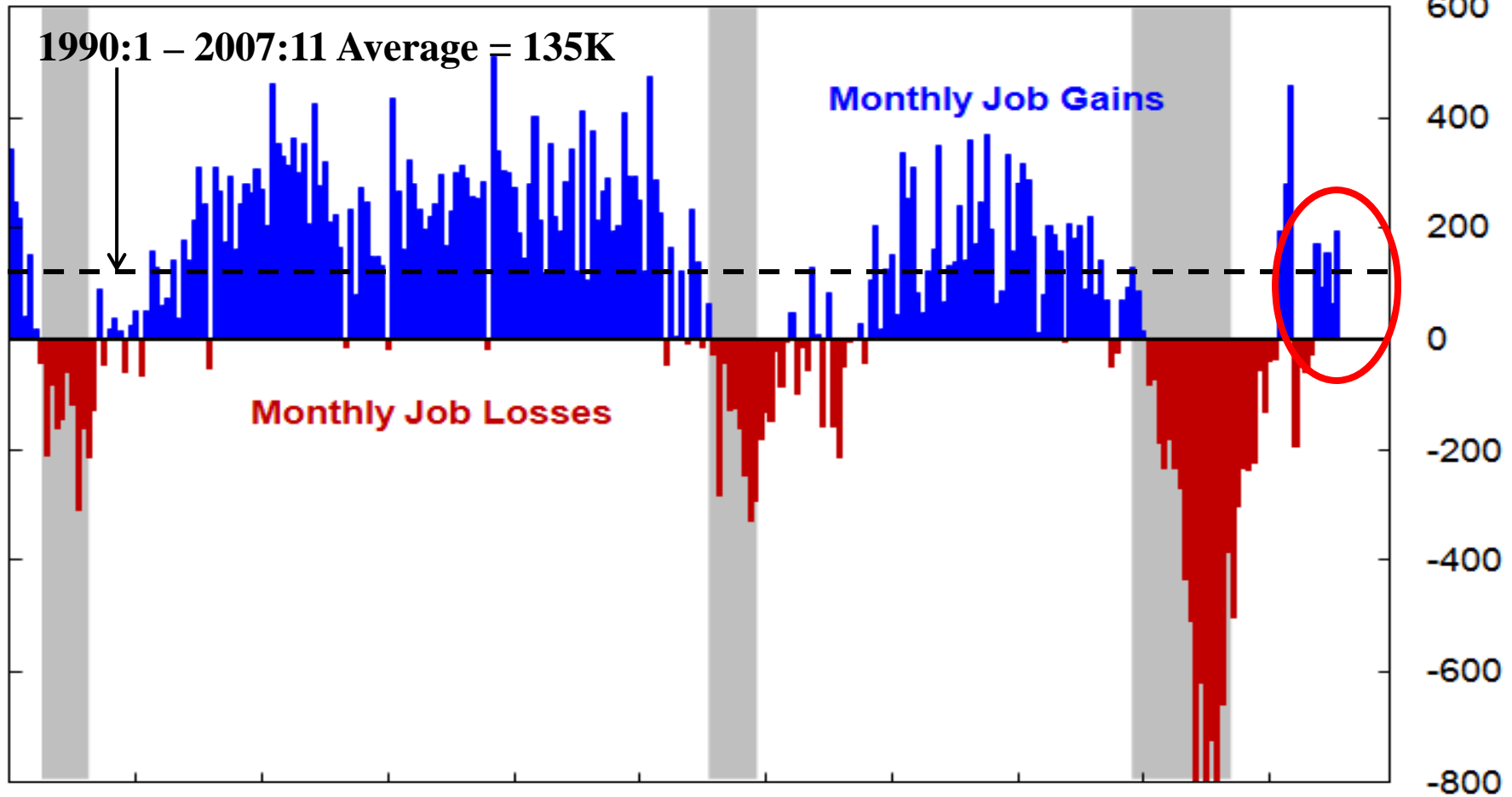
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Total Payroll Job Growth Has Resumed

Nonfarm Payroll Employment

Month-to-month difference in thousands; seasonally adjusted

Thousands
600



1990 1992 1994 1996 1998 2000 2002 2004 2006 2008 2010

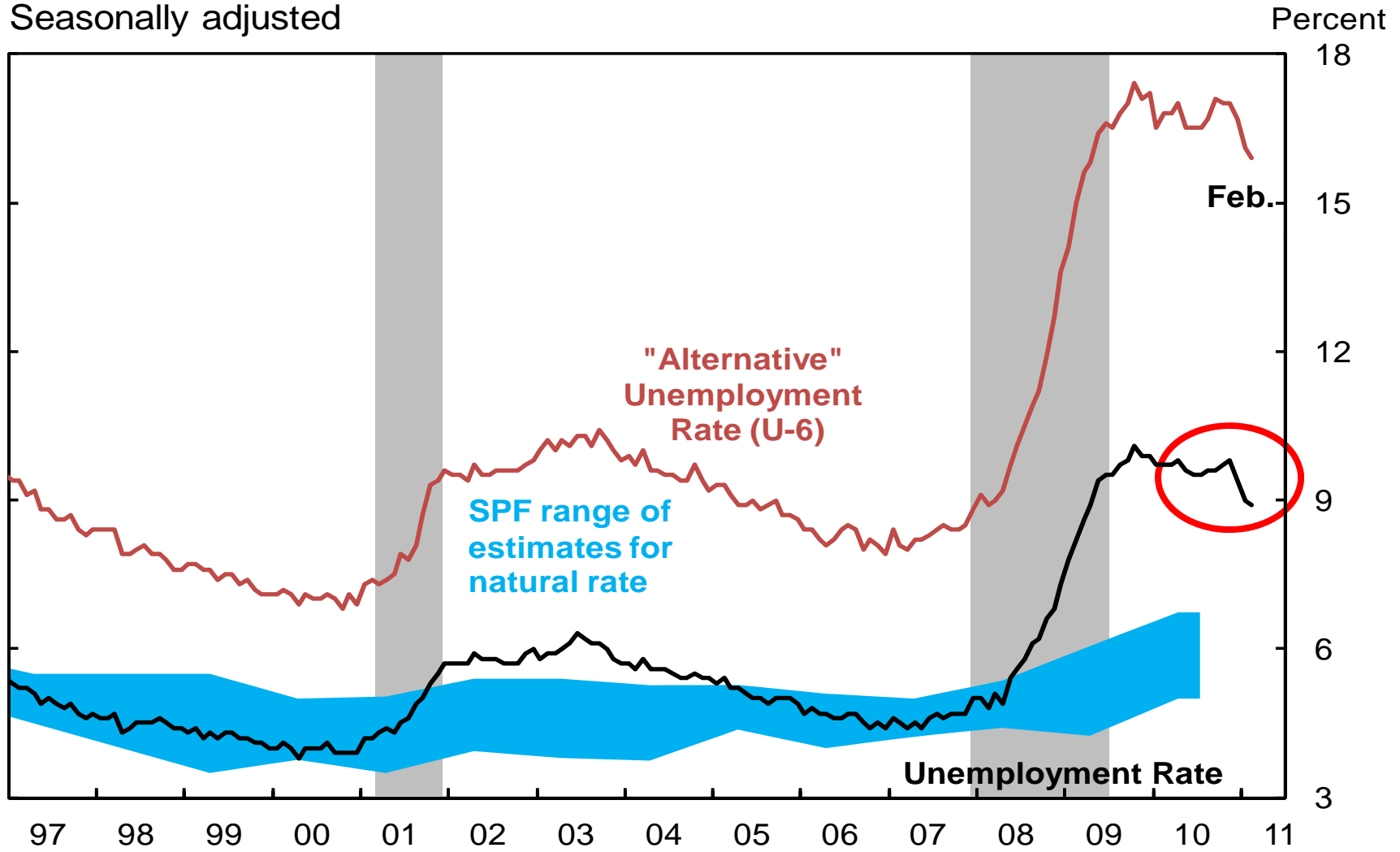
Source: Bureau of Labor Statistics

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Unemployment Rate Noticeably Improved, but Remains Well Above Estimates of Natural Unemployment Rate

Unemployment Rate

Seasonally adjusted



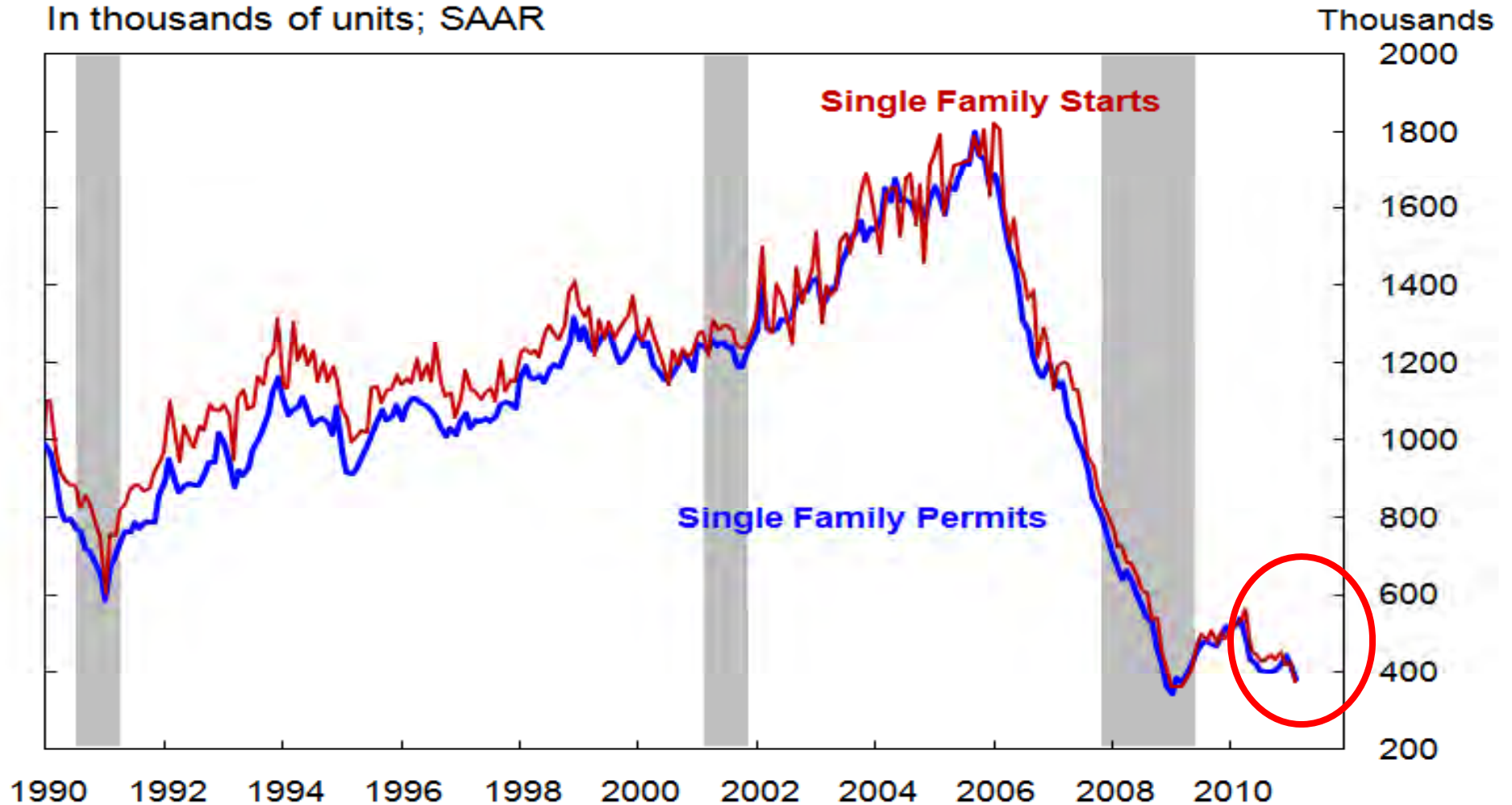
SPF = Survey of Professional Forecasters, FRB Philadelphia.

3/21/2011

Homebuilding Activity Remains Weak and Is Not Likely to Provide a Boost to Growth for Some Time

New Single Family Housing Units

In thousands of units; SAAR

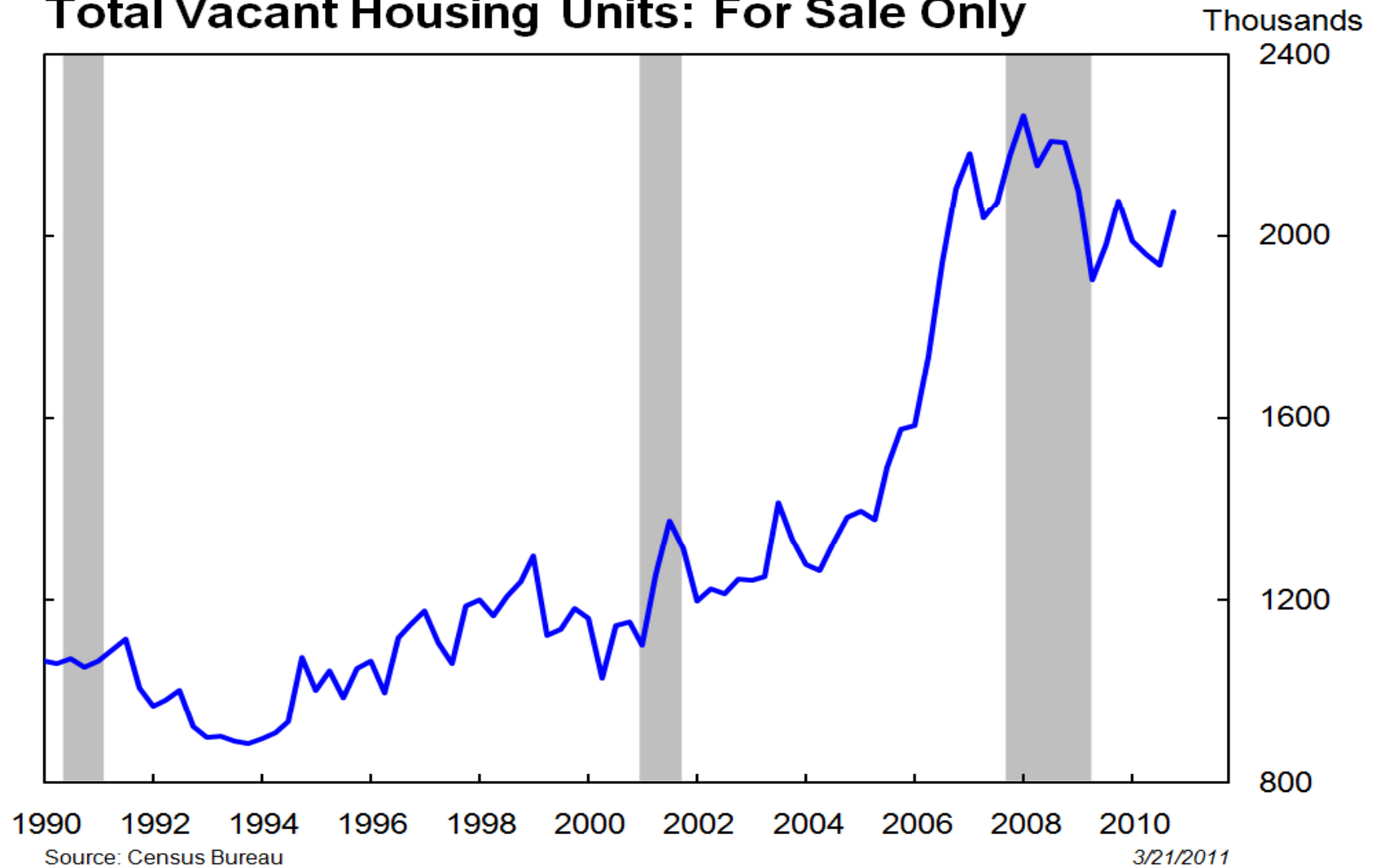


Source: Census Bureau

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Inventory of Unsold Homes Remains Large

Total Vacant Housing Units: For Sale Only

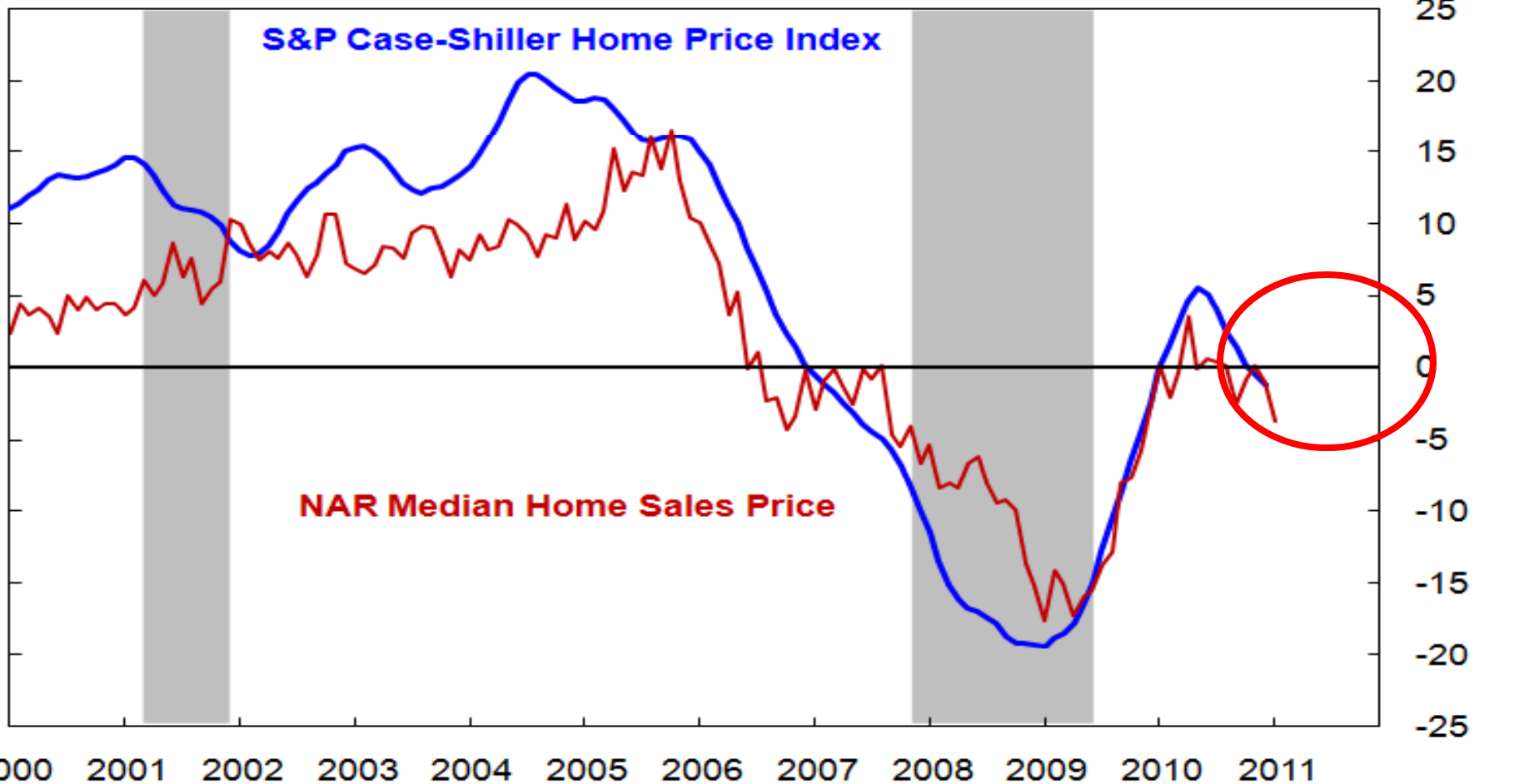


National House Prices Are Again Falling at a Slow Pace – Supply Side Risks and Uncertainties Remain

House Price Changes

Year-over-year percent change

Percent



Source: Standard & Poor's, National Association of Realtors

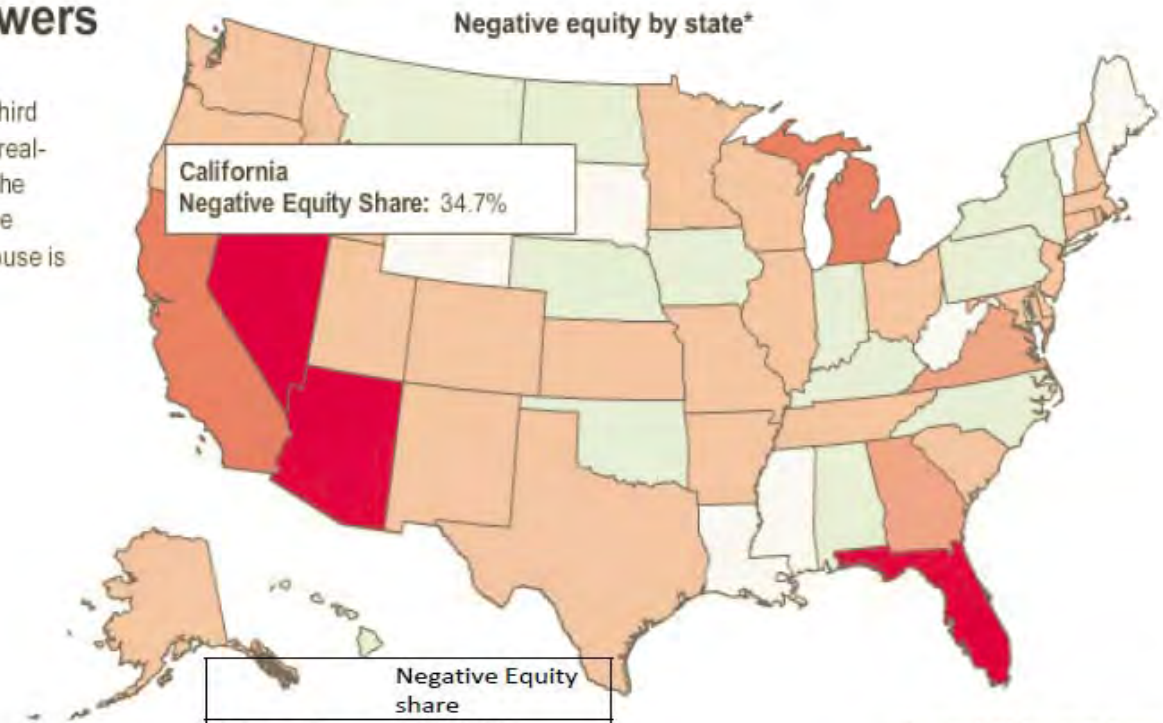
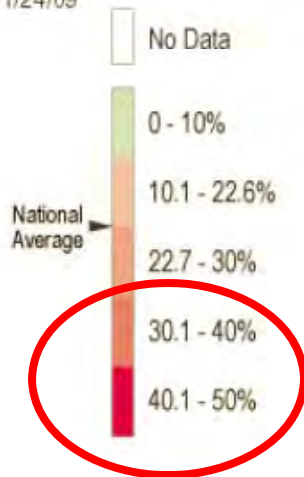
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Huge Share of Underwater Mortgages Across Much of the Nation Creates Uncertainty

One-fourth of all mortgages are underwater

In Deep: Underwater Borrowers

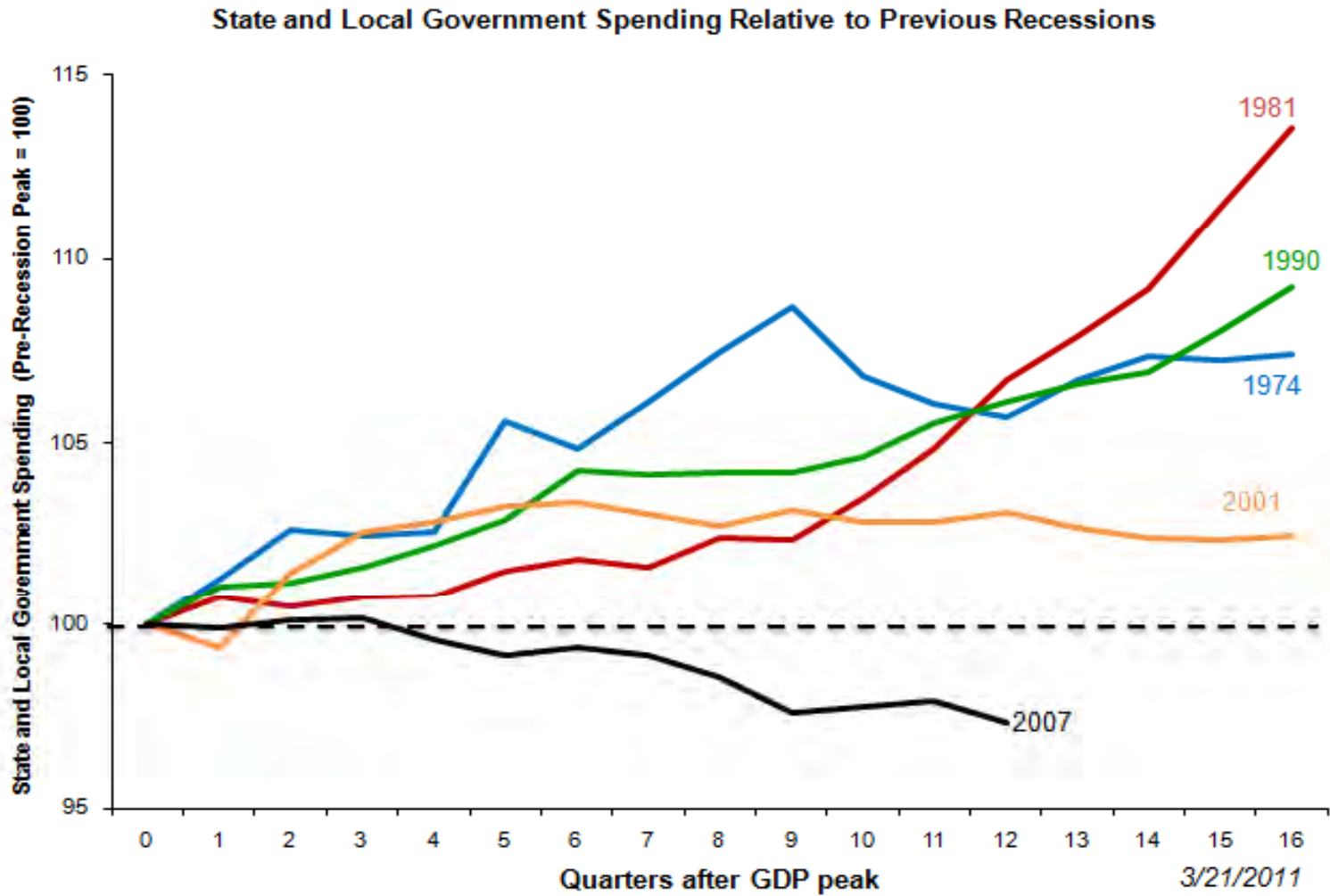
Nearly 10.7 U.S. million households, or about 23% of homeowners with mortgages, had negative equity in the third quarter, according to First American Home CoreLogic, a real-estate information company based in Santa Ana, Calif. The map looks at the percentage of homeowners with negative equity, i.e., who owe more on their mortgage than their house is worth. --11/24/09



State	Negative Equity share
Nevada	65.00%
Arizona	47.90%
Florida	44.70%
California	34.70%
Washington	14.30%
Oregon	13.90%

Source: First American CoreLogic

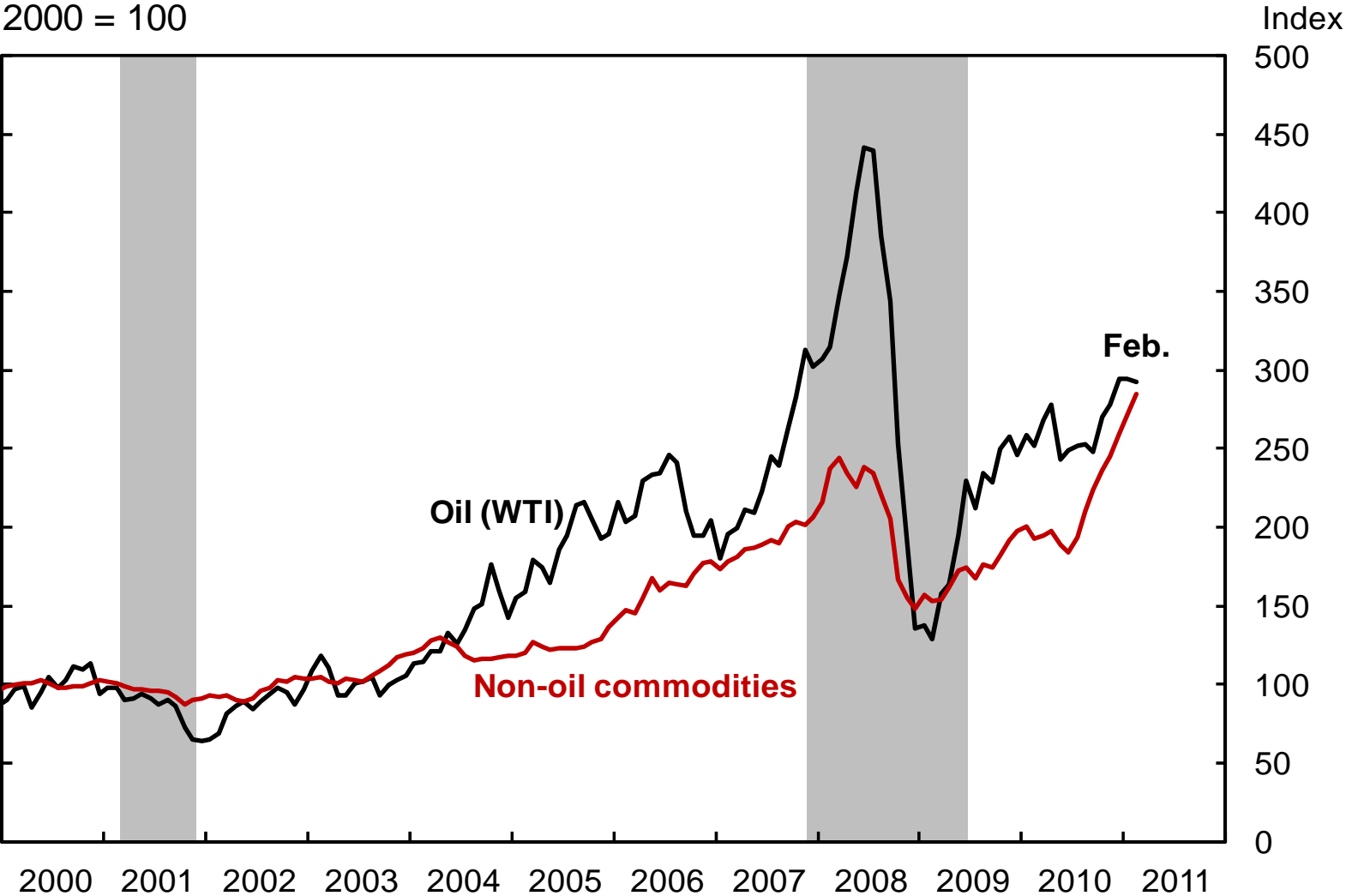
State and Local Government Spending is Expected To Continue Subtracting from GDP Growth



Commodity Prices Increased Significantly Over the Past Year (May Pose Risk to Growth)

Commodity Prices

2000 = 100

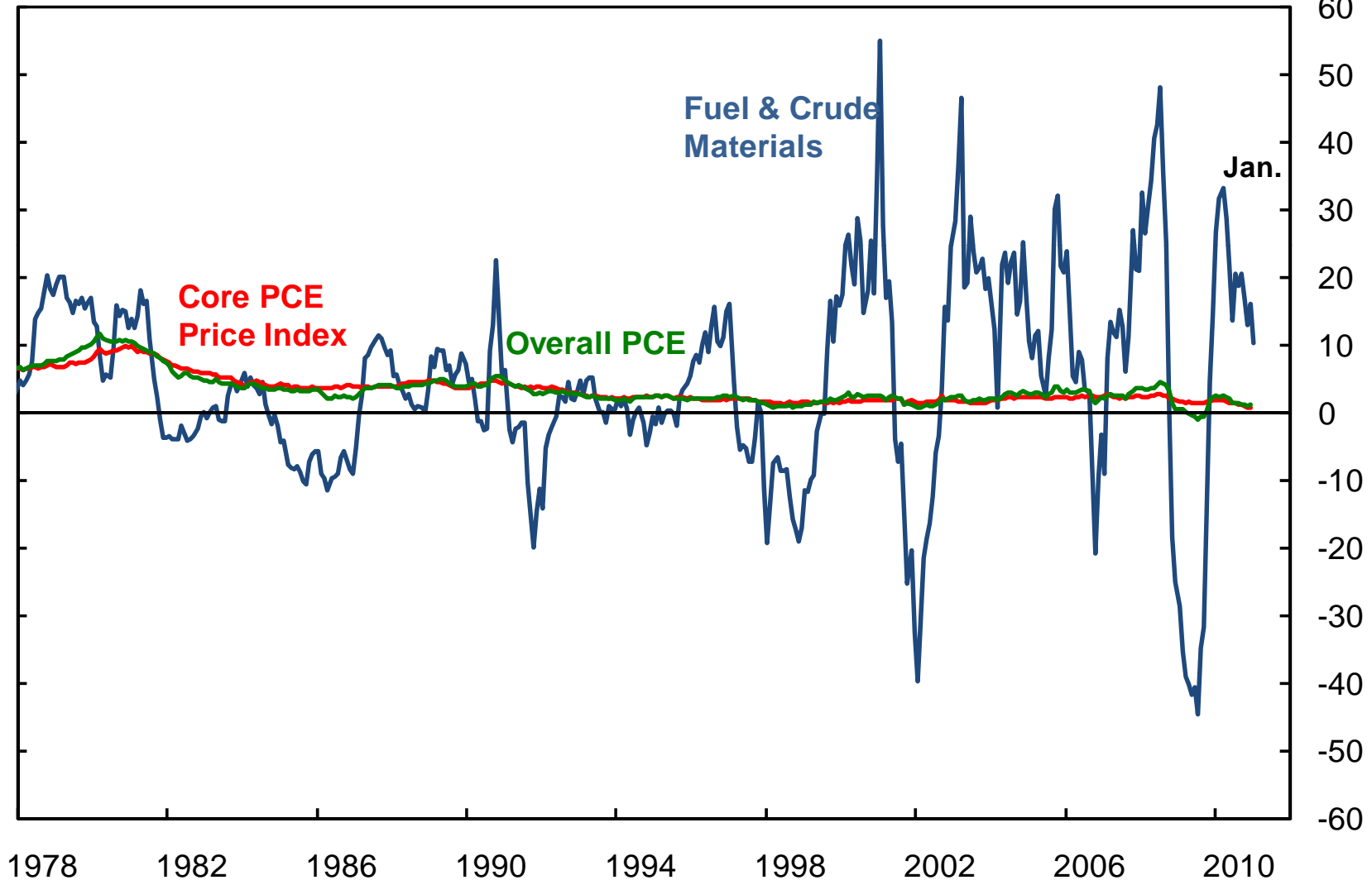


Note: Prices of non-oil commodities are based on S&P Goldman Sachs data.

Despite the Increase in Commodity Prices, Inflation Remains Subdued

Material Prices and Core PCE Price Index

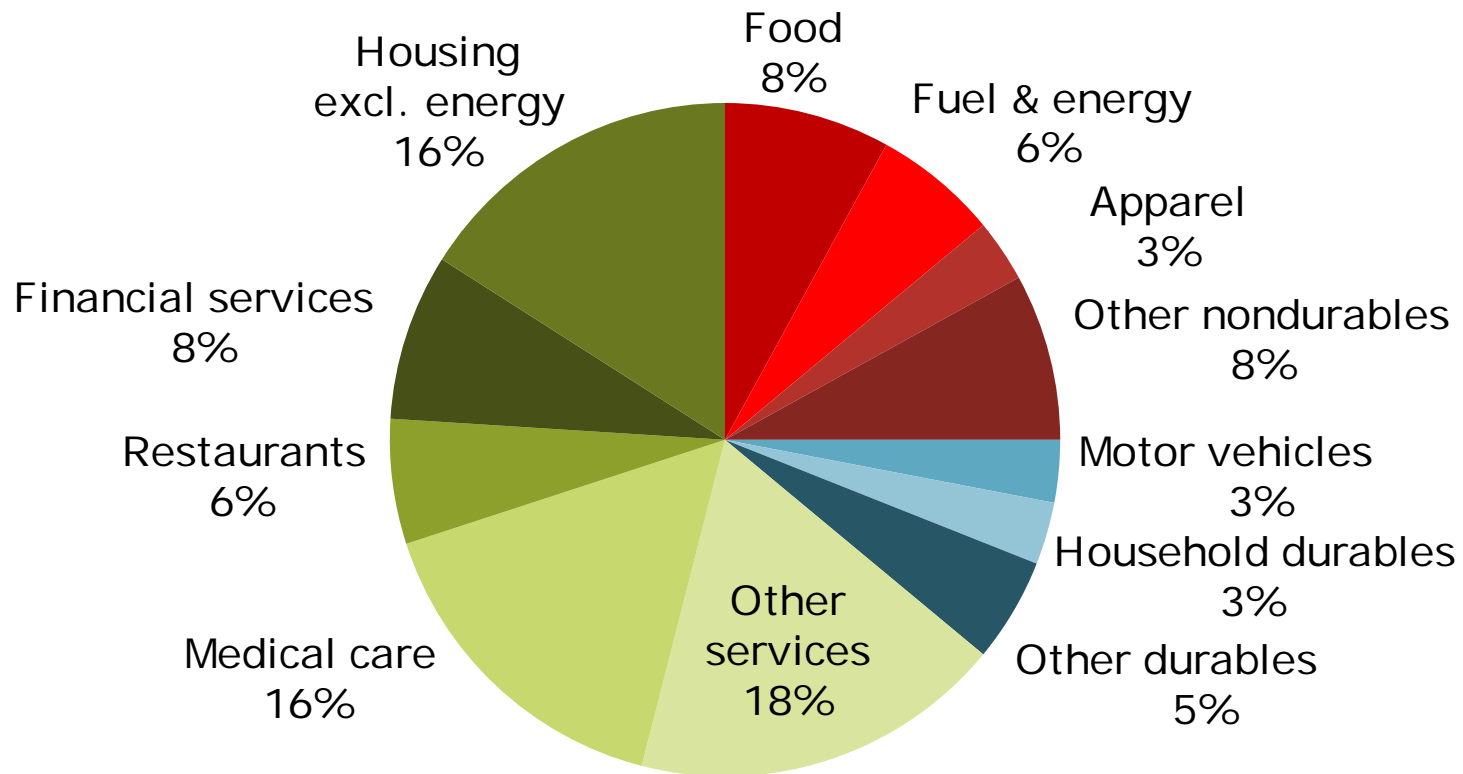
12-month percent



Source: Bureau of Labor Statistics

Food and Energy Are Not a Large Part of Consumer Spending (14% in 2010); Most of Spending is on Services

Composition of Personal Consumption Expenditures 2010



Note: Noncore consumption= Food+Fuel&Energy= 14% of spending;
red=nondurables, blue=durables, green=services. Source: BEA

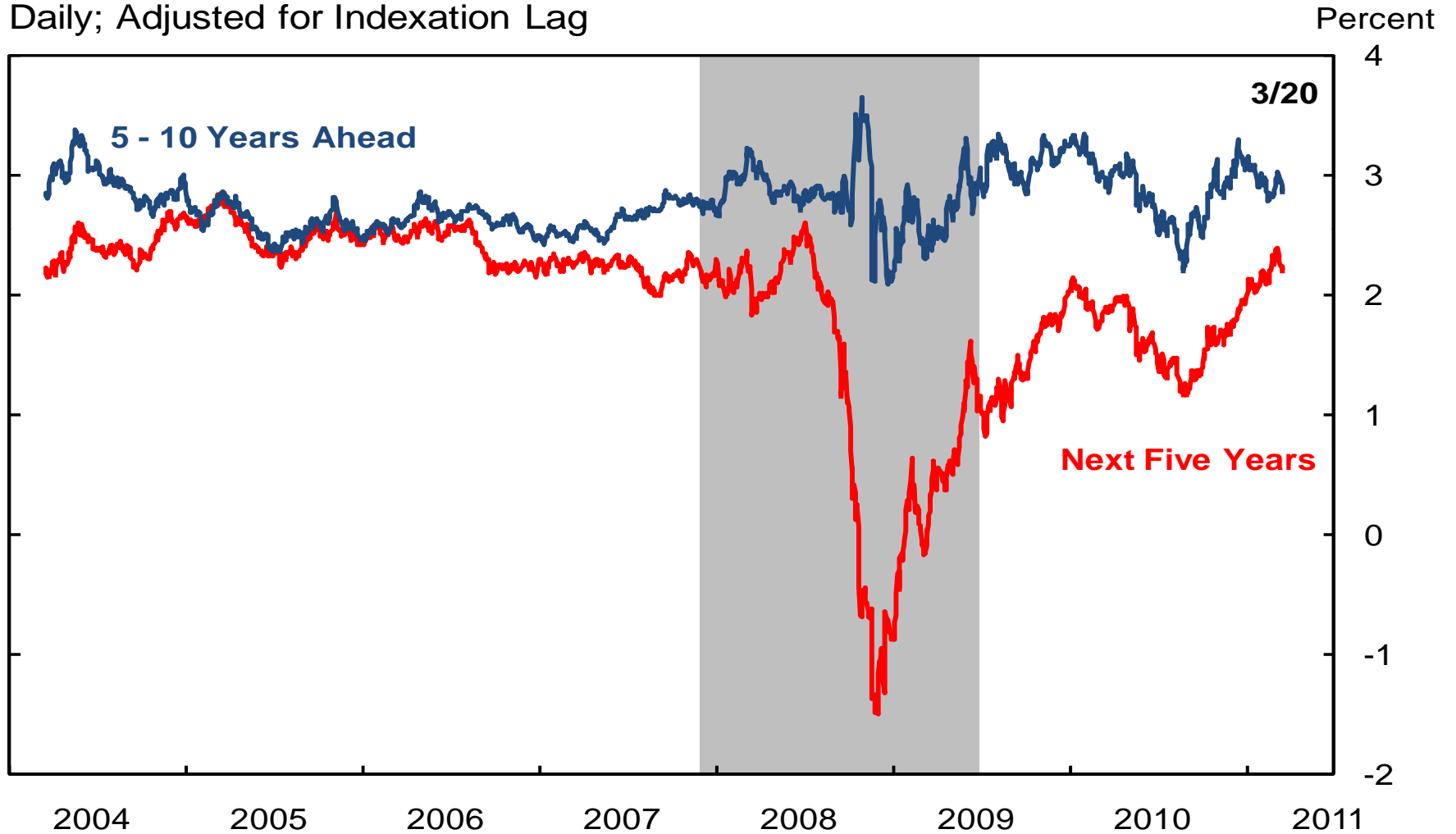
Source: March 2011 FedViews

<http://www.frbsf.org/publications/economics/fedviews/index.php>

Inflation Expectations Remain Anchored

TIPS Implied Inflation Compensation

Daily; Adjusted for Indexation Lag





FRBSF NATIONAL ECONOMIC FORECAST

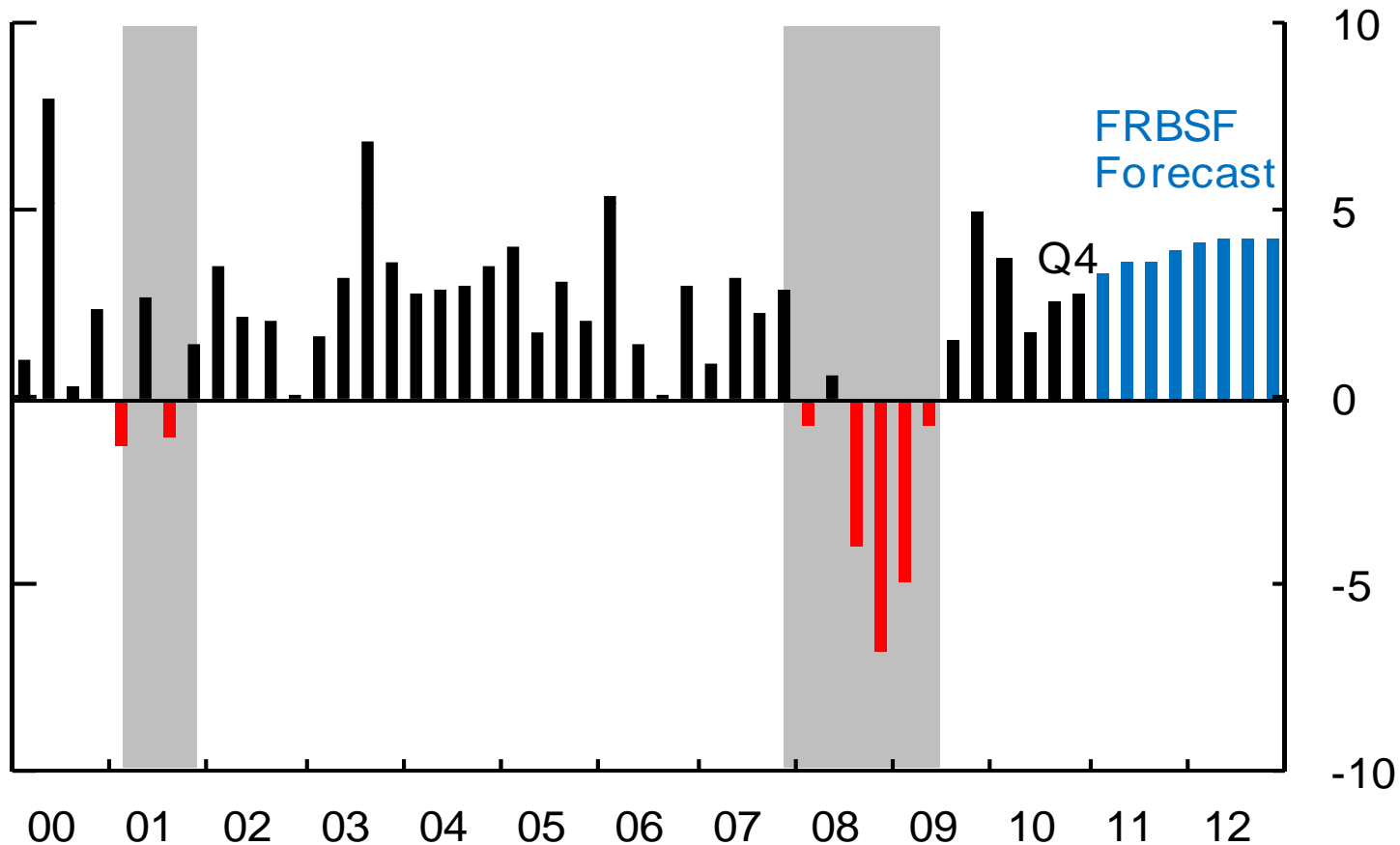
***FedViews* March 10, 2011** -- <http://www.frbsf.org/index.html>

Real GDP Growth: Gradual Expansion on Track

Real GDP

Percent change at seasonally adjusted annual rate

Percent

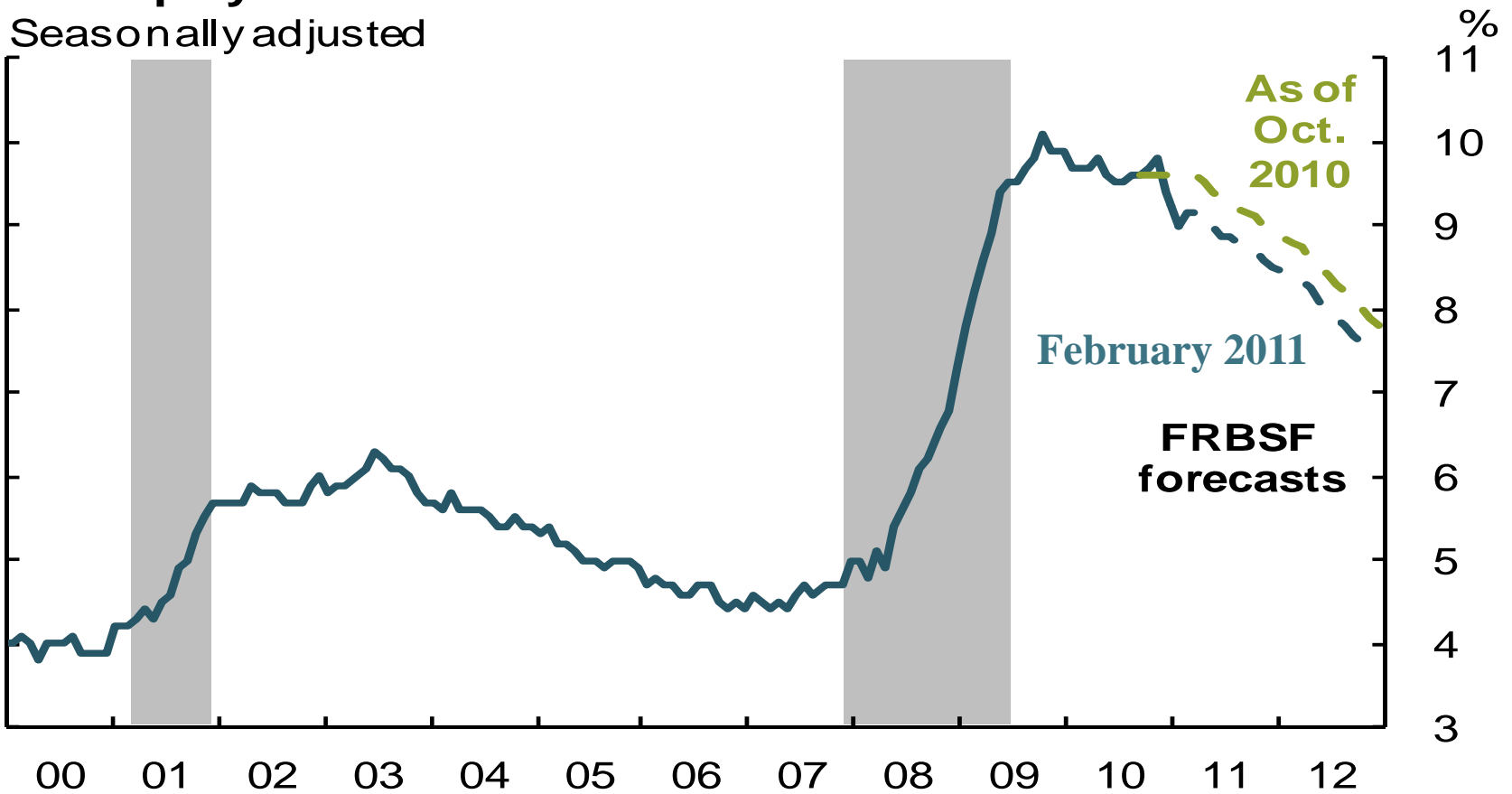


Source: March 2011 FedViews

<http://www.frbsf.org/publications/economics/fedviews/index.php>

Unemployment Rate: More Optimism in the Forecast

Unemployment Rate
Seasonally adjusted



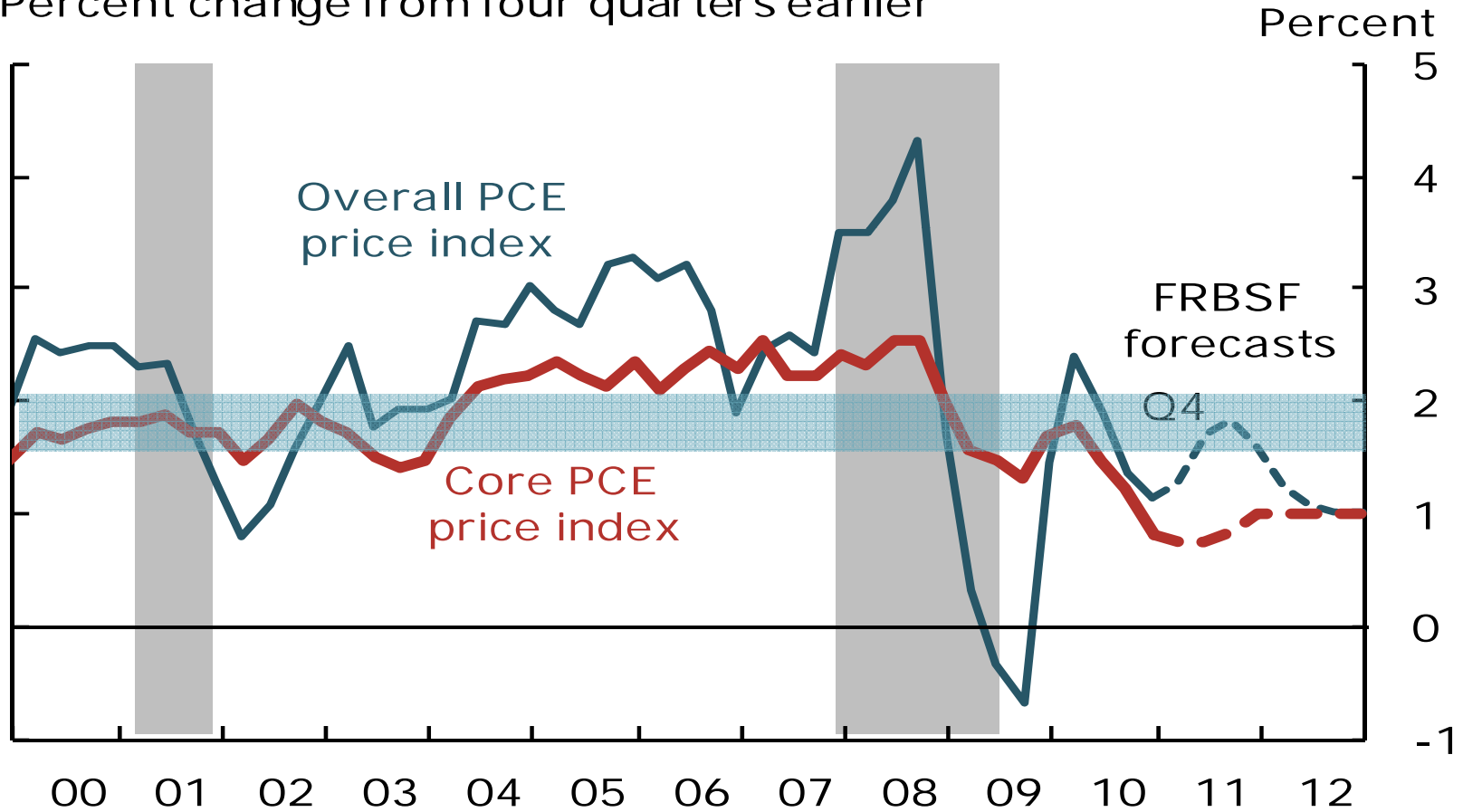
Source: February 10, 2011 FedViews

<http://www.frbsf.org/publications/economics/fedviews/index.php>

Inflation: Subdued; Expected to Remain Low

PCE Price Inflation

Percent change from four quarters earlier



Source: March 2011 FedViews

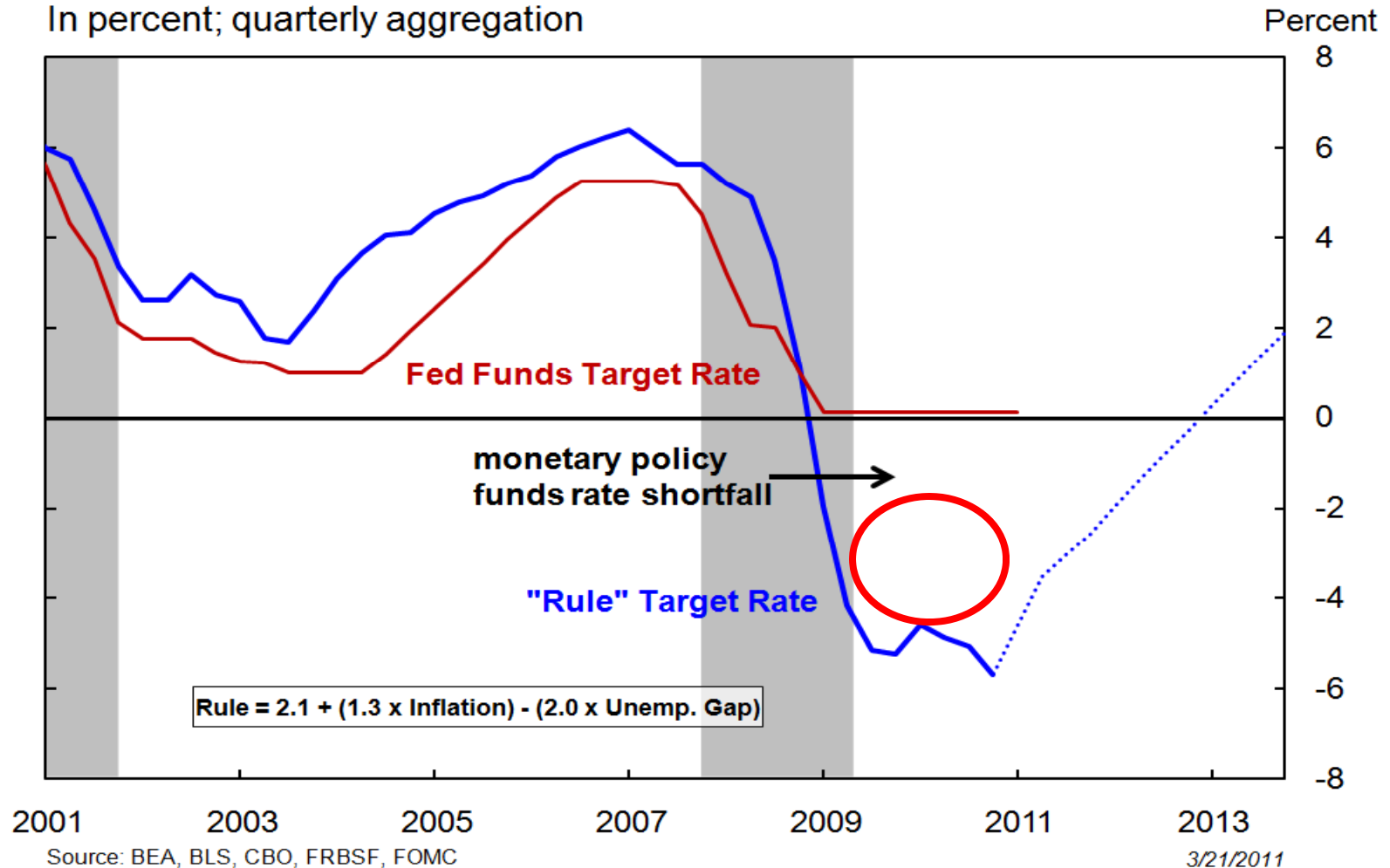
<http://www.frbsf.org/publications/economics/fedviews/index.php>

MONETARY POLICY OUTLOOK

(FOMC Statement, 3/15/2011): "...economic conditions... are likely to warrant exceptionally low levels for the federal funds rate for an extended period."

Actual versus "Recommended" Fed Funds Target

In percent; quarterly aggregation



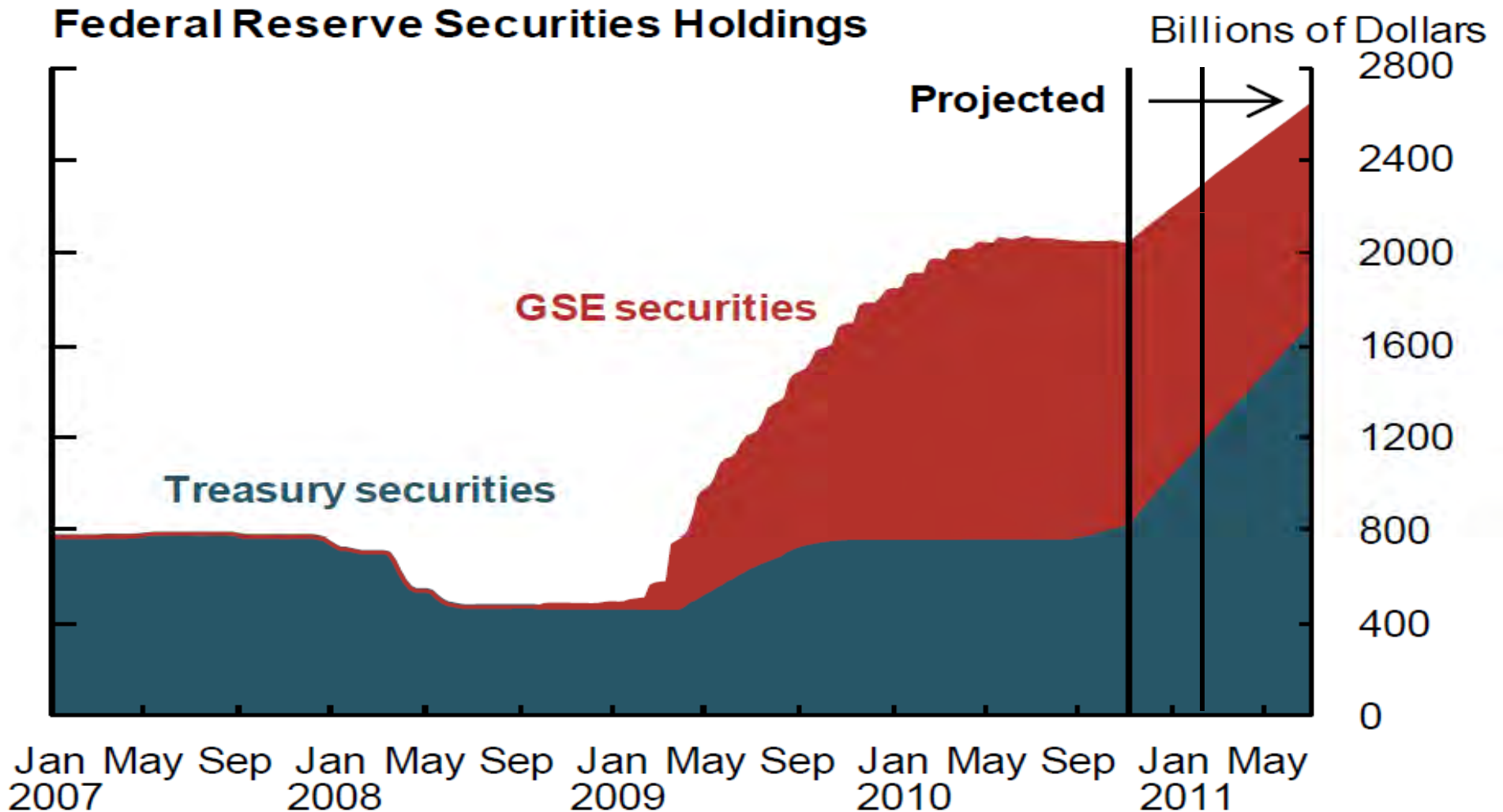
Committee Will Continue with LSAP Plans Announced in FOMC Statement of November 3, 2010

Committee reiterated after the March 15 meeting:

- “...is maintaining its existing policy of reinvesting principal payments from its securities holdings.”
- “... intends to purchase \$600 billion of longer-term Treasury securities by the end of the second quarter of 2011.”
- “... will regularly review the pace of its securities purchases and the overall size of the asset-purchase program in light of incoming information and will adjust the program as needed to best foster maximum employment and price stability.”



Monetary Stimulus via Large-Scale Asset Purchases



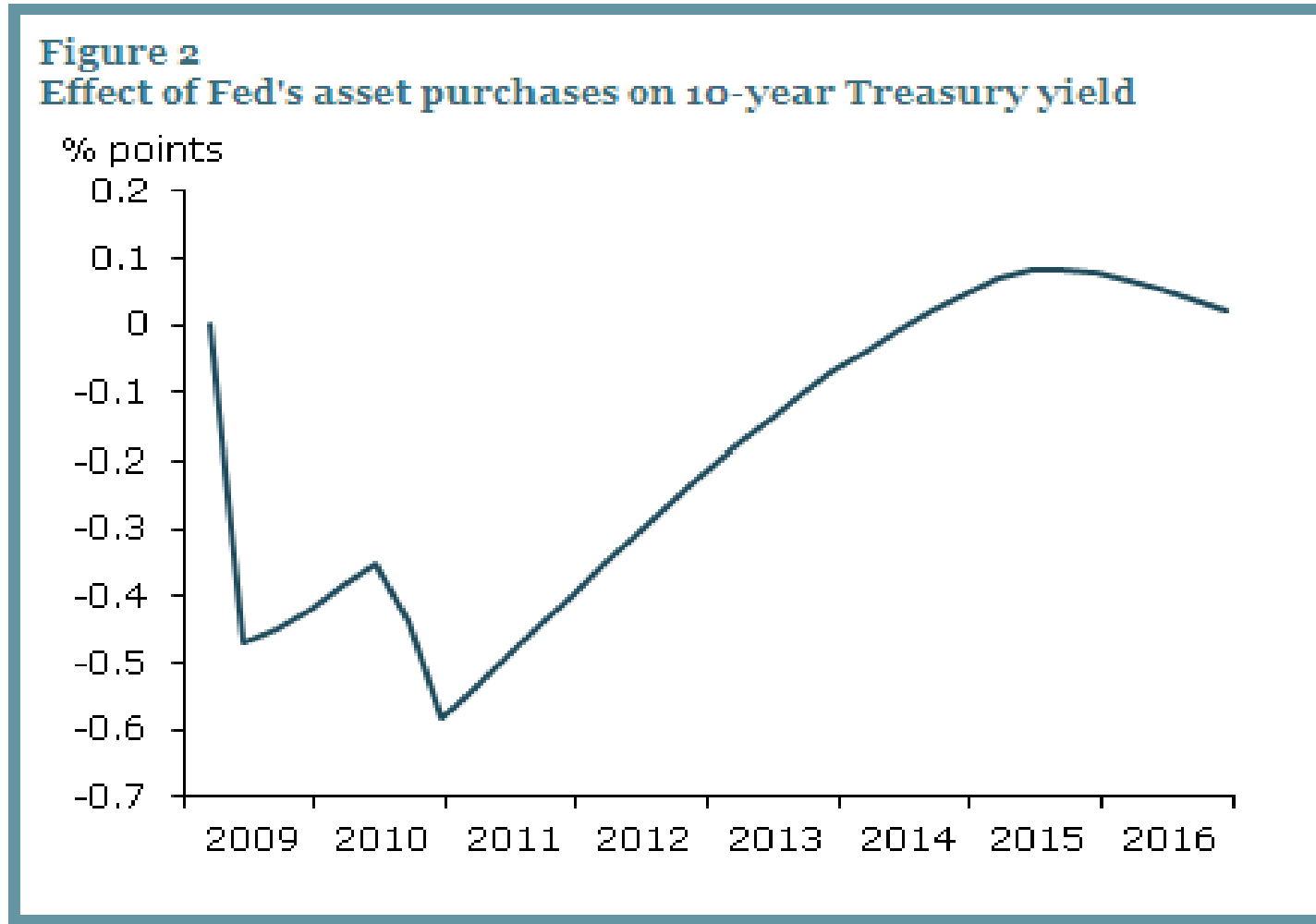
GSE = Government-Sponsored Enterprises (Fannie & Freddie)

FedViews November 10, 2010

Unconventional Policy Action: Expected Effects

- **Lower long-term interest rates**
- **Increased demand**
- **Reduced risk of deflation**

Estimated Effect of the Fed's Large- Scale Asset Purchase Program on a Long-Term Interest Rates



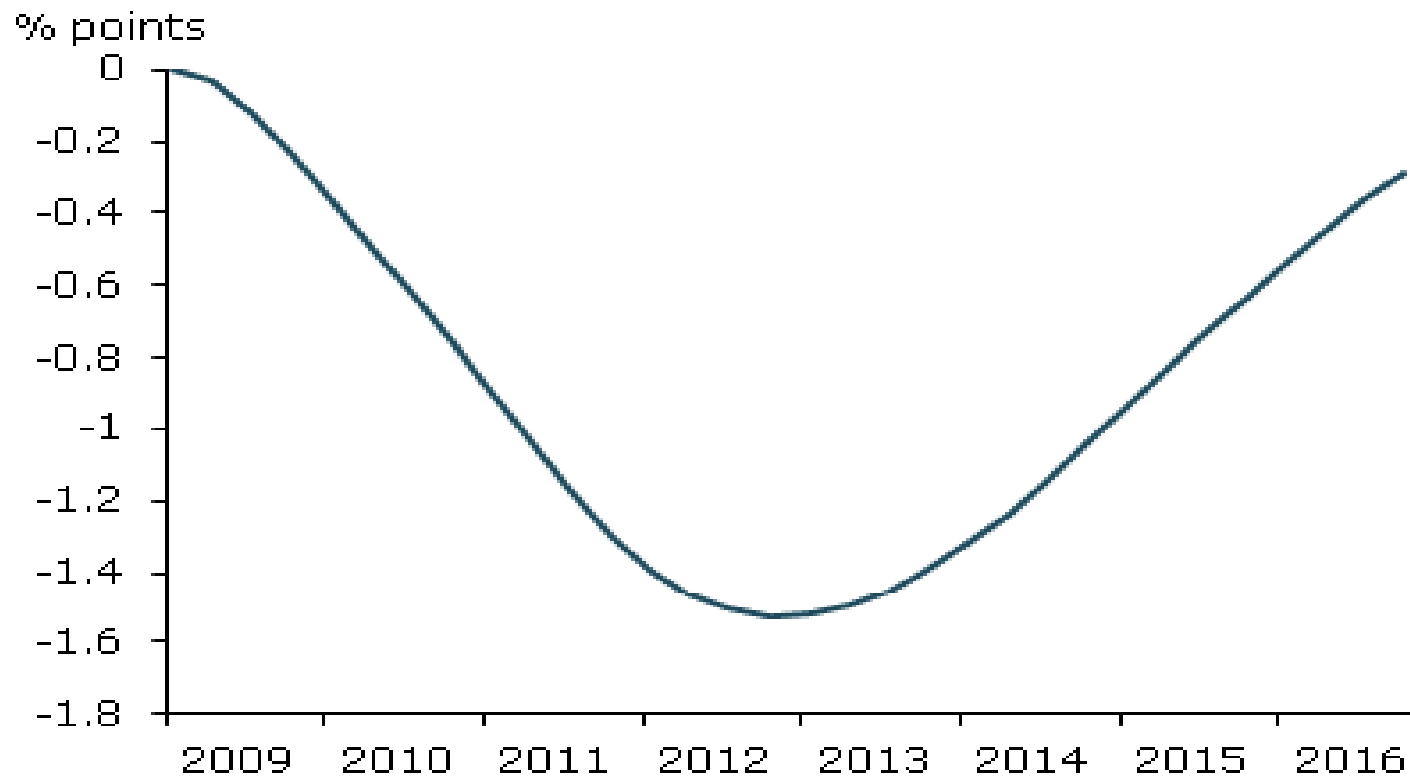
Source: FRBSF Economic Letter 2011-03

<http://www.frbsf.org/publications/economics/letter/2011/el2011-03.html>

Estimated Effect of the Fed's Large- Scale Asset Purchase Program on Unemployment Rate

Figure 3

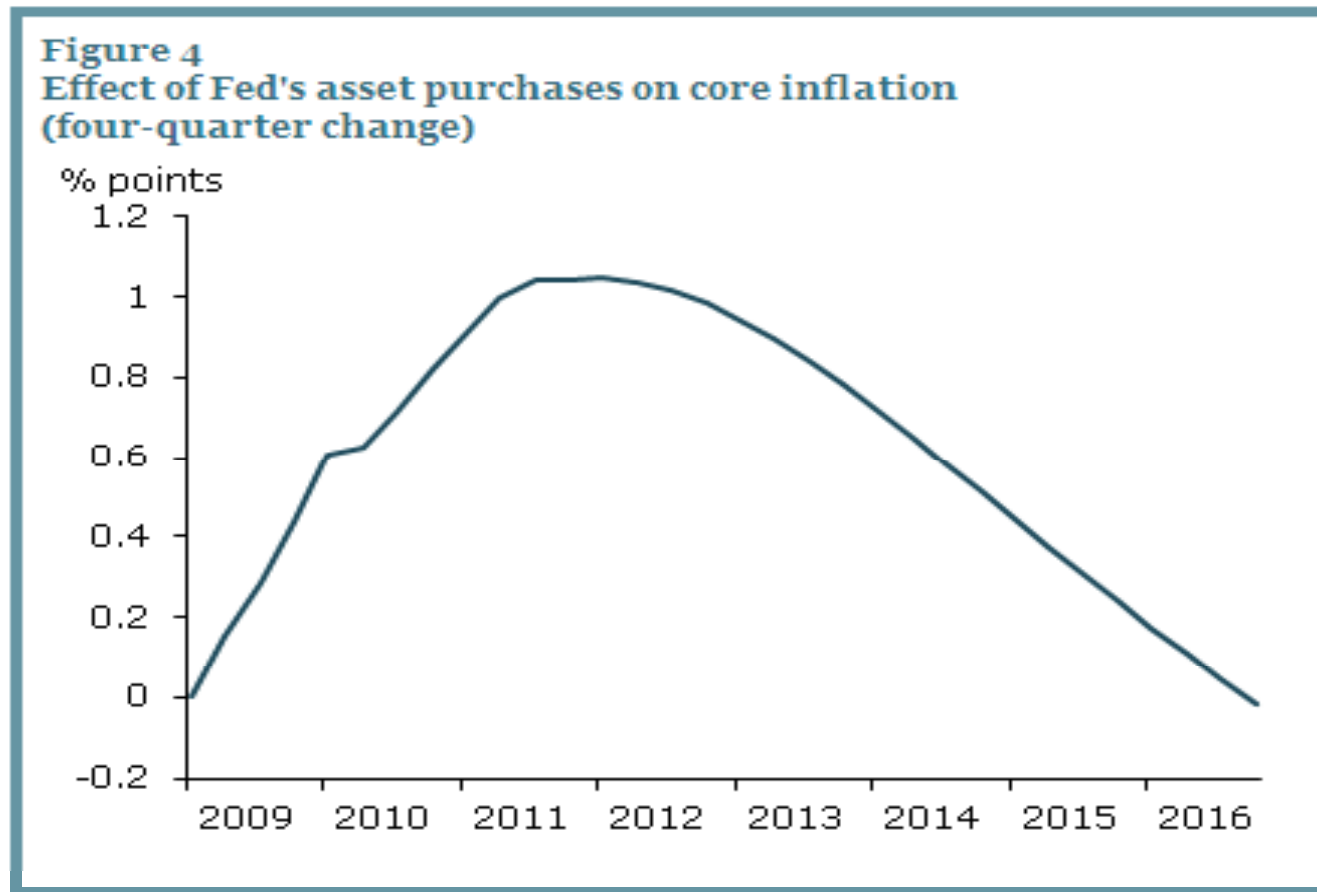
Effect of Fed's asset purchases on unemployment rate



Source: FRBSF Economic Letter 2011-03

<http://www.frbsf.org/publications/economics/letter/2011/el2011-03.html>

Estimated Effect of the Fed's Large- Scale Asset Purchase Program on Inflation



Source: FRBSF Economic Letter 2011-03

<http://www.frbsf.org/publications/economics/letter/2011/el2011-03.html>

Summary Points

Economic output is still far below potential output, but the rate of economic growth is projected to improve:

- To much of the public it may still “feel like a recession” (weakness in the labor market persists, housing market still anemic)
- However, in recent months, the pace of recovery appears to have improved
- New uncertainty introduced by Middle East unrest and potential impacts from the earthquake in Japan

Inflation is trending below the FOMC’s preferred rate and is expected to remain low

- Underutilized industrial capacity and a high unemployment rate are expected to persist

Questions?



Yelena Takhtamanova, Economist

Yelena.Takhtamanova@sf.frb.org

www.frbsf.org