

Tennessee State Funding Board

December 14, 2012

Lee Jones

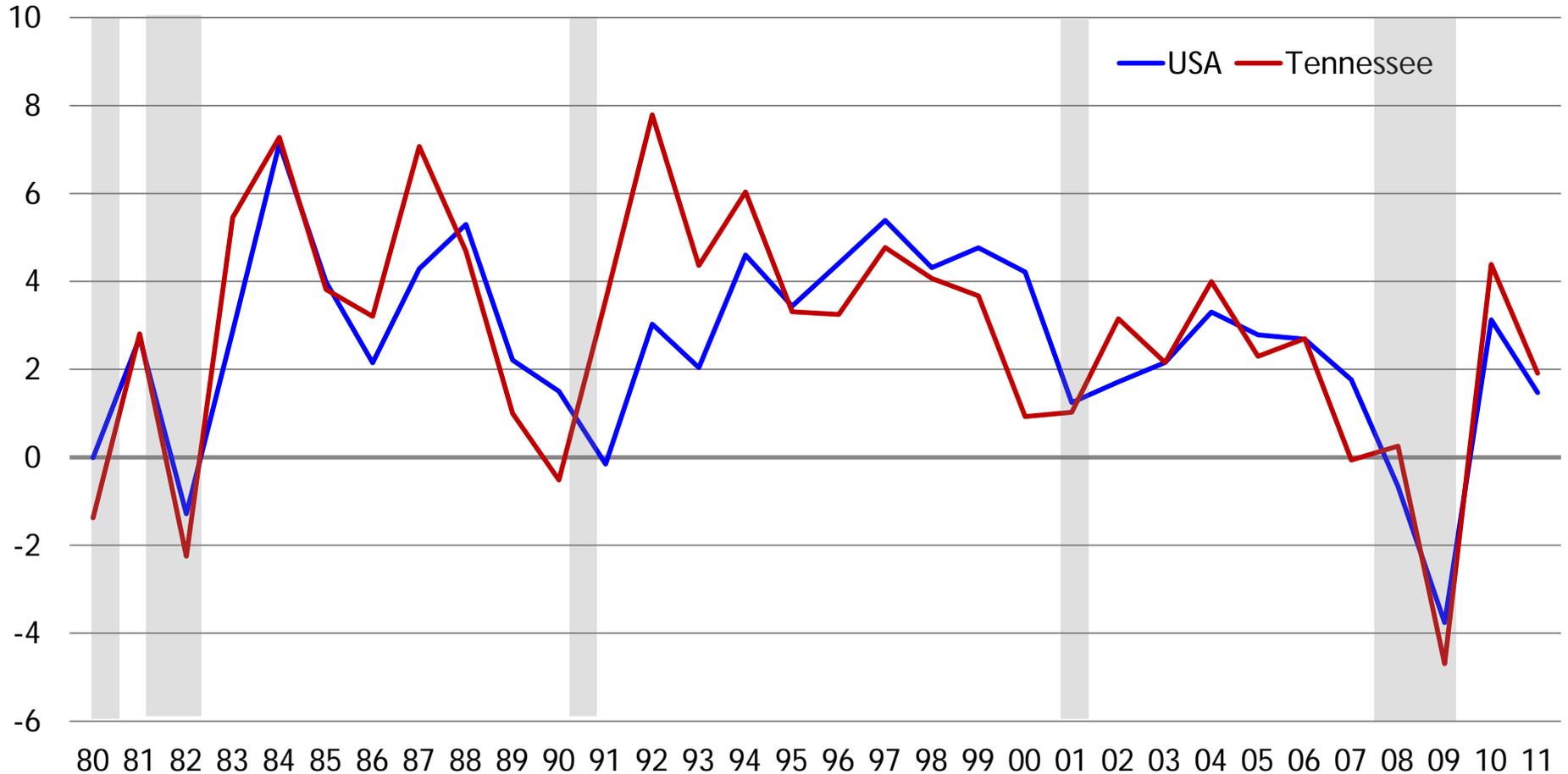
Regional Executive - Tennessee

The views expressed are mine and not necessarily those of the Atlanta Fed or the Federal Reserve System.



The overall economy in Tennessee generally moves in tandem with the US economy.

Economic Growth in Tennessee and the US, 1980 - 2011
Year over Year Percent Change



Where we are today: A Bumpy, Apprehensive Recovery for the nation.

The economy has been operating at a pace of growth of around 2 percent since the recovery began 40 months ago.

There have been quarters of faster growth and certainly quarters that clocked in below 2 percent, but the summary trend rate approximates 2 percent.

Simply said, the economy is stuck in a slow-growth mode.

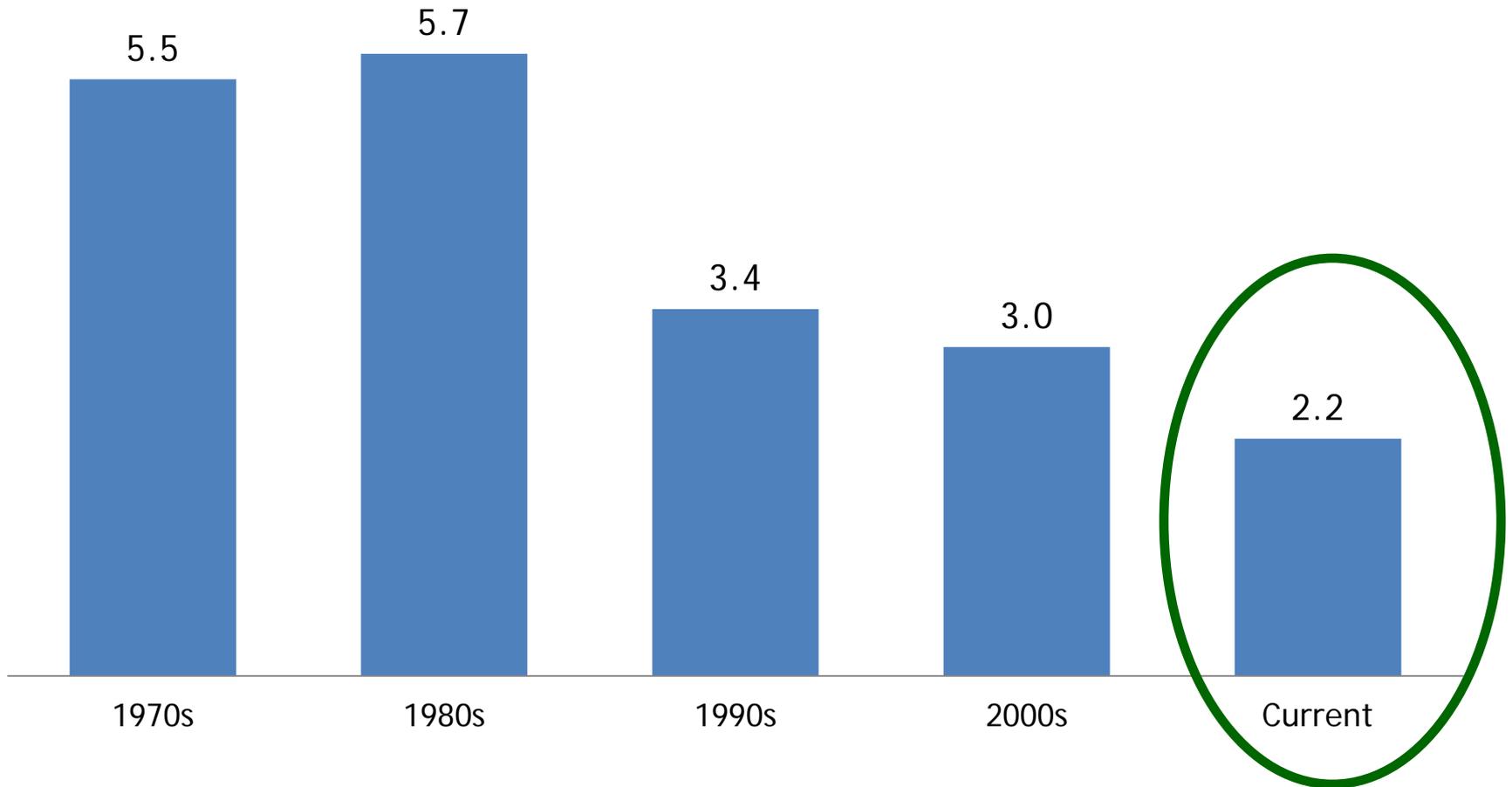
By the end of the third quarter both the economic data and anecdotal reports from business and community contacts indicated that businesses and workers had resigned themselves to an environment where growth is likely to remain modest.

Recent (and projected) data suggest the US economy remains on about a 2% growth trajectory.

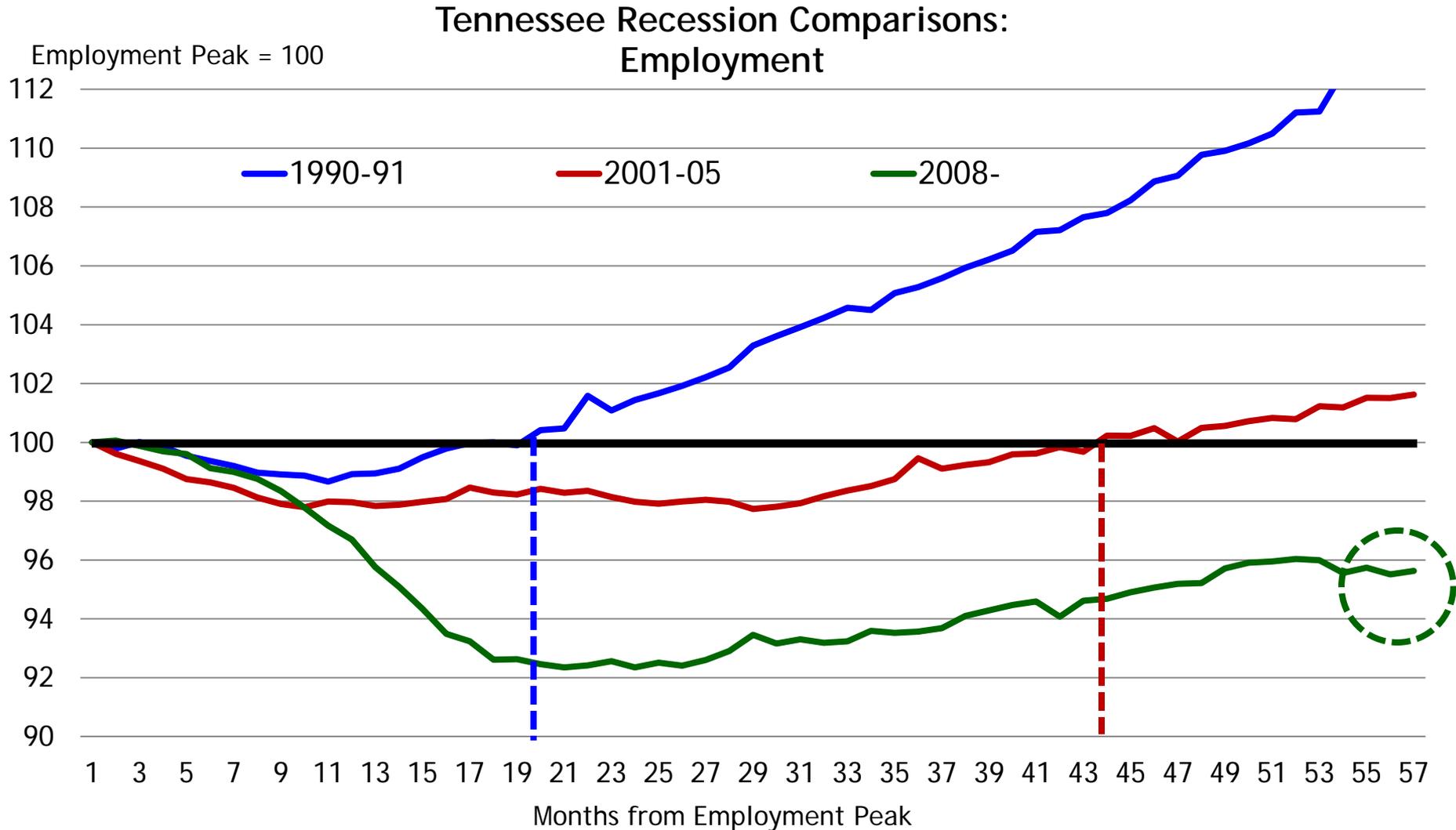
Period	GDP Growth (in percent)
2010	2.4
2011	1.8
2012	2.2*

Nationally, the economic recovery has been frustratingly slow.

Average Growth Rate for the National Economy During Recovery



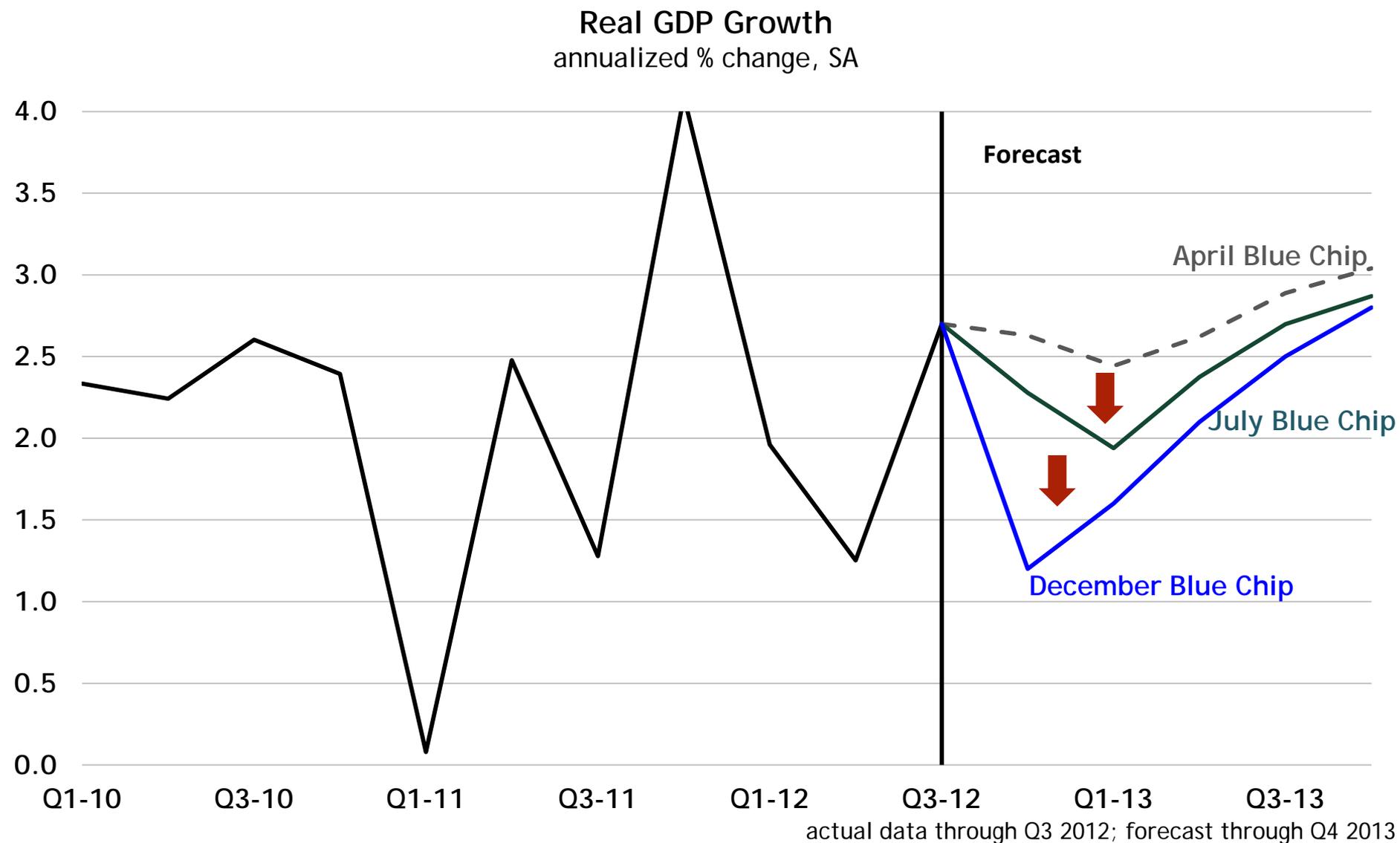
Similarly in Tennessee, economic activity has not returned to the level needed to create sustained job growth.



Overview of the economy and the policy environment.

1. Economic growth remains subdued.
2. Recent employment trends are a bit more favorable than thought a few months ago. Still, many measures of labor market performance remain near recessionary levels, and the prospect for a significant drop in joblessness any time soon appears somewhat small, particularly if labor force participation increases.
3. The housing market is stabilizing and appears to be moving toward recovery at a slow but steady pace.
4. The fiscal cliff remains a large downside risk to the outlook.
5. Inflation indicators are holding steady at target-consistent (~2%) levels.

The economic outlook, as judged by private forecasters, shows an economy slowing to around a 1.5% pace for the next two quarters and only approaching a 3% path by the end of 2013. This is a decidedly more subdued growth pace than private forecasters were envisioning earlier in the year.

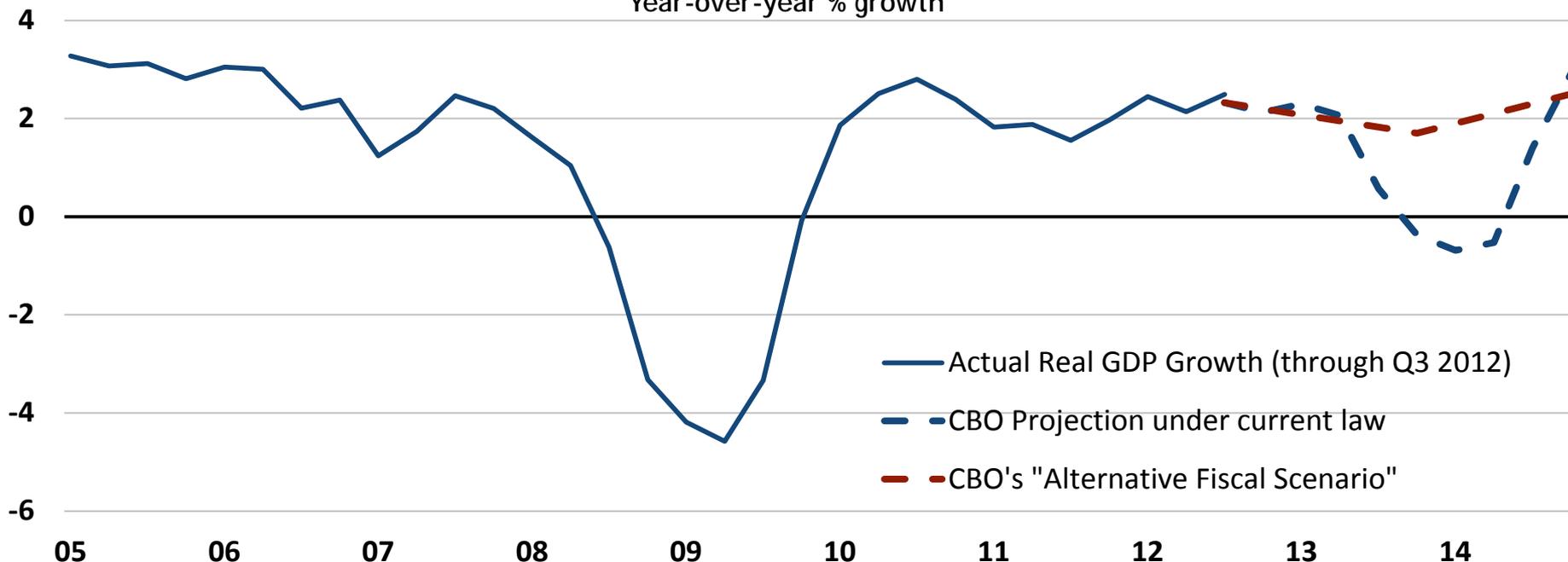


Sources: BEA; Blue Chip Consensus Forecast April, July, and December 2012

A major, lingering uncertainty is the potential for a sharp fall-off in business activity should the economy go over the fiscal cliff. The CBO's baseline scenario (which is a fiscal cliff scenario) cuts GDP growth a little more than 2 percentage points in 2013 and raises unemployment by a bit more than a percentage point. Other estimates are broadly similar in magnitude.

Real GDP Growth under various CBO fiscal scenarios

Year-over-year % growth



Economic impact of fiscal cliff in 2013:		Real GDP Q4/Q4	Unemployment Rate
CBO baseline scenario		-0.5	9.1
CBO alternative scenario		1.7	8.0
		<i>GDP Impact</i> ‡	
Moody's		-2.8	9.2
Fitch		-2.0	N/A
JP Morgan		-1.0	N/A

‡percentage point reduction in real GDP growth relative to baseline forecast

Note: "Alternative Fiscal Scenario": Expiring tax provisions are extended; AMT indexed for inflation; Medicare payment rates held constant; and automatic spending reductions required by Budget Control Act do not take effect in January 2013.

Because of the sharp deficit reduction that will occur under current law, the CBO projects that the unemployment rate will rise to 9.1 percent by Q4 13. An alternative scenario (no fiscal cliff) leads to a gradual decline in the UR.

Unemployment Rate

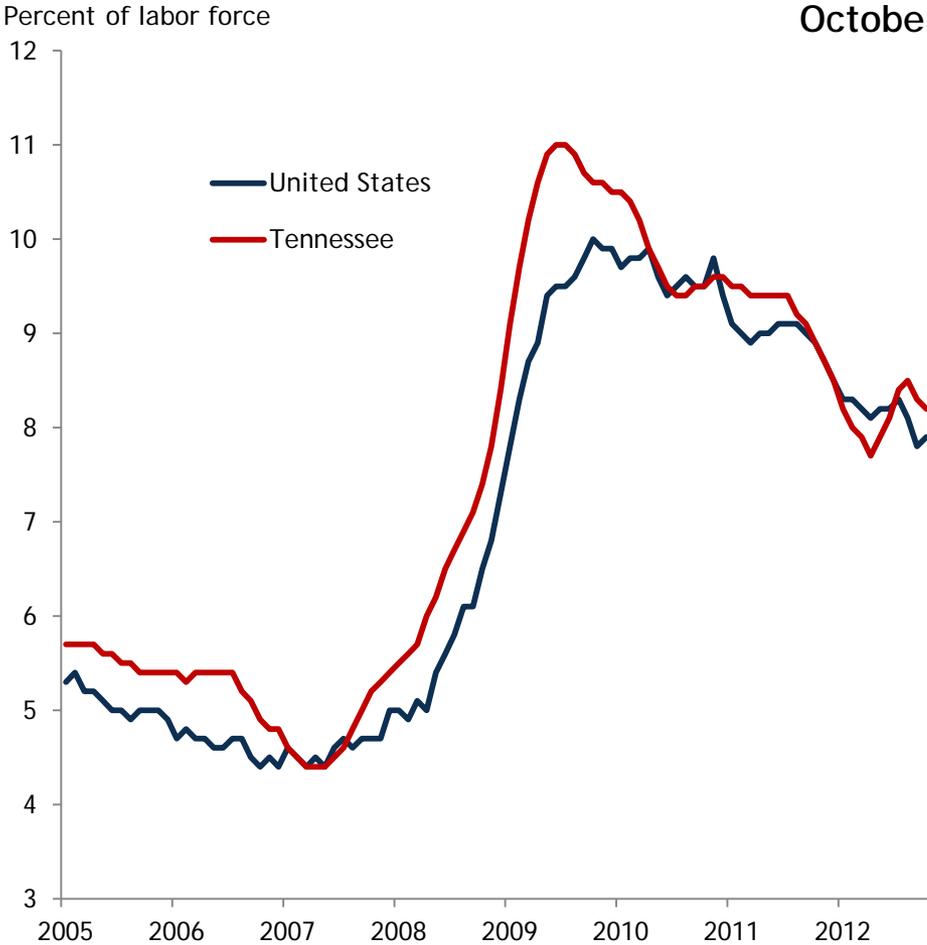
(Percent)

August 2012
<http://go.usa.gov/7QY>



The unemployment rate for Tennessee dipped slightly in September and October, but remains higher than the national rate.

Unemployment Rates October 2012

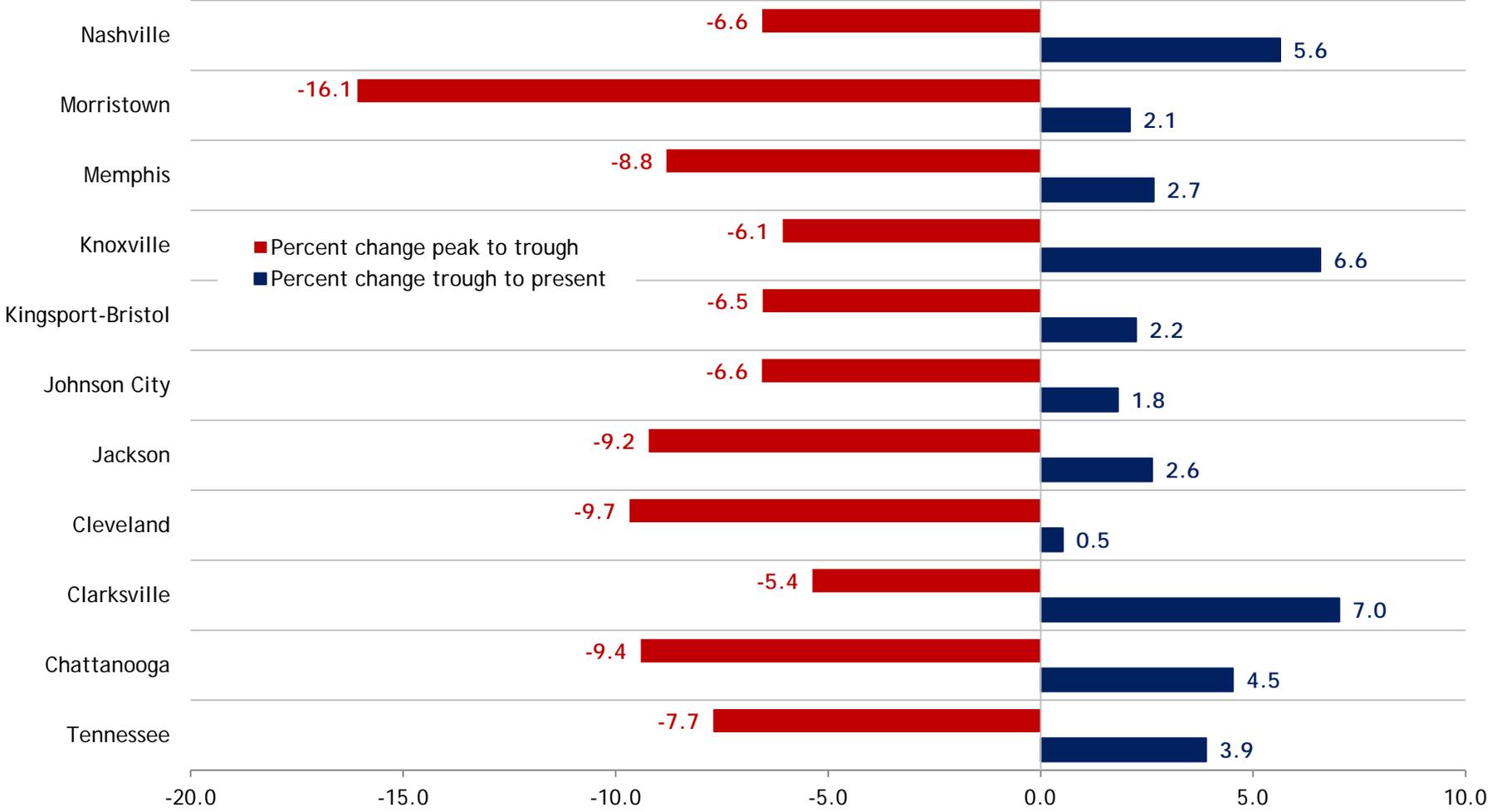


Unemployment Rates			
	Current	Year Ago	Jan 2007
United States	7.8	9.0	4.6
Tennessee	8.3	9.1	4.6
Chattanooga	7.1	8.3	4.4
Clarksville	8.3	9.8	5.7
Cleveland	7.8	9.3	4.9
Jackson	7.9	9.5	5.6
Johnson City	6.9	8.1	4.8
Kingsport-Bristol	6.9	8.1	4.8
Knoxville	6.1	7.3	4.1
Memphis	8.4	10.0	5.8
Morristown	9.3	10.8	6.1
Nashville	6.4	7.9	4.2

Source: U.S. Bureau of Labor Statistics, Haver Analytics

Employment losses in Tennessee metro areas were significant during the downturn. Most metro areas are slowly regaining jobs. Clarksville and Knoxville have regained and slightly exceeded jobs lost while Nashville is inching closer.

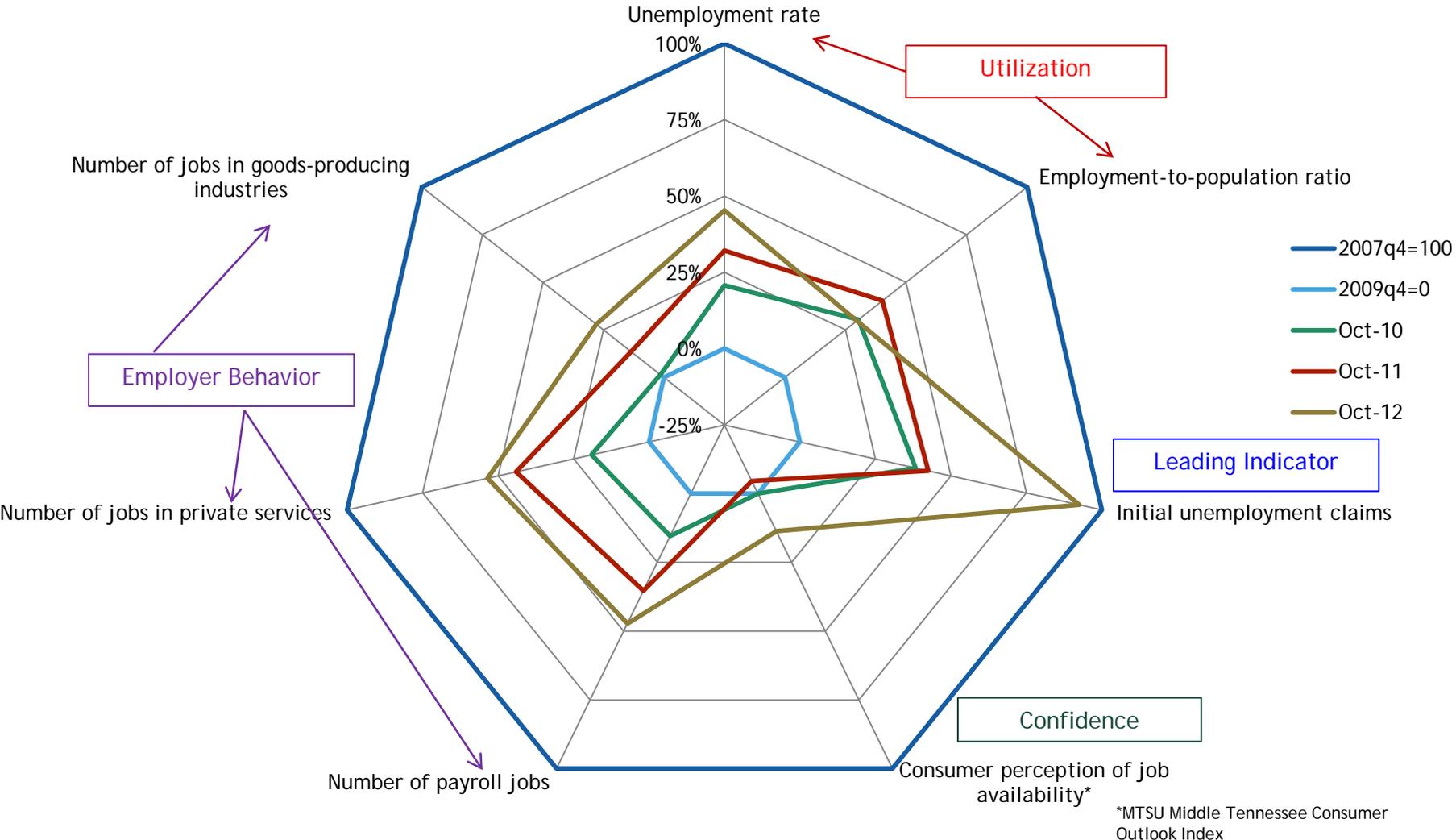
Employment Loss and Gain by Metro Area: Tennessee
October 2012



Sources: U.S. Bureau of Labor Statistics, Haver Analytics, Federal Reserve Bank of Atlanta

Judging the state of the Tennessee labor market from a variety of perspectives reveals a decidedly mixed picture of recovery. Bottom line, the labor market has a long way to go to recover to pre-recessionary levels in many key measures.

Indicators of labor market's health in Tennessee

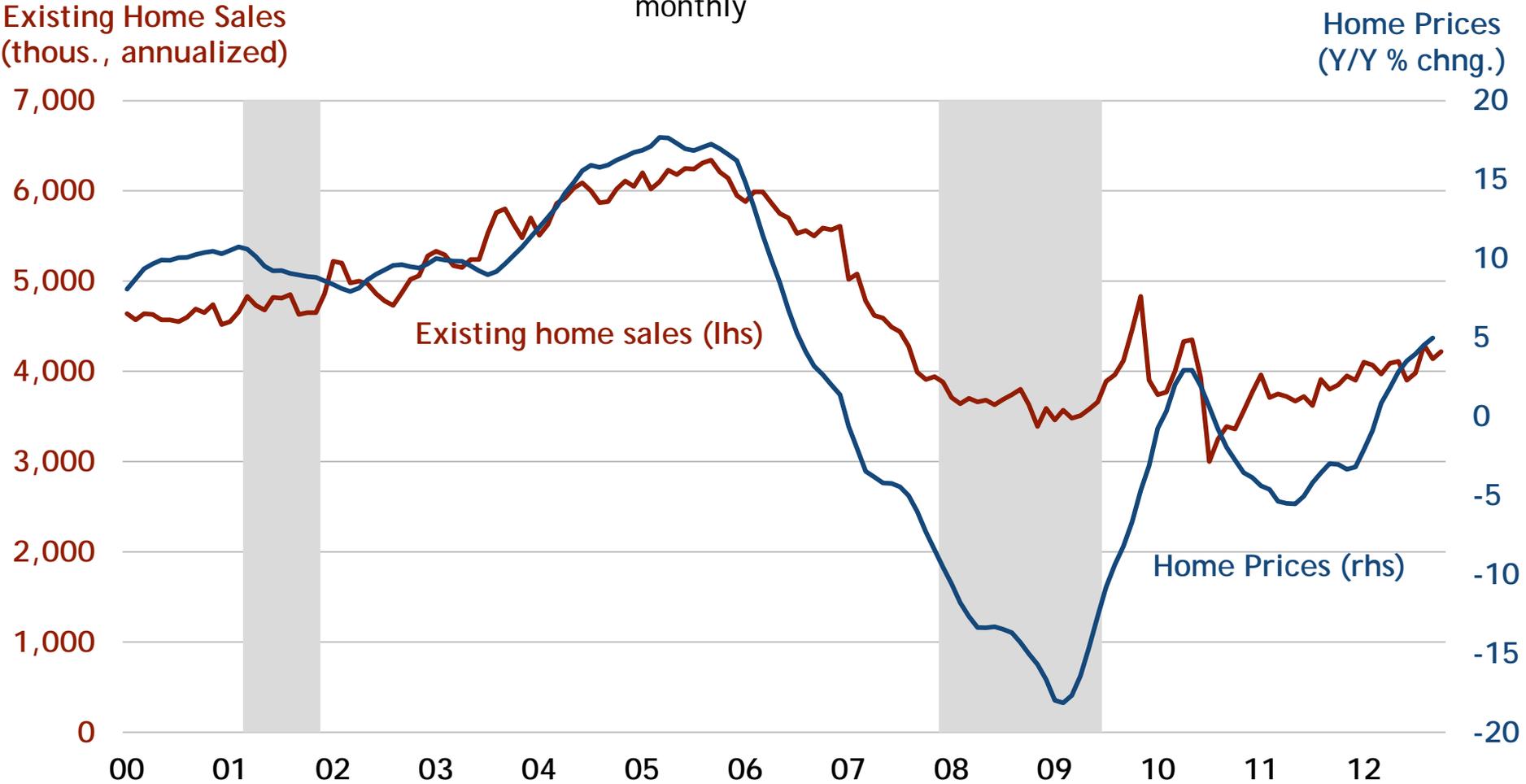


Sources: Haver Analytics, FRB Atlanta calculations

*MTSU Middle Tennessee Consumer Outlook Index

The U.S. housing market is a particular bright-spot for the economy. Home sales are on a gradual up-trend (though still about 20% under the levels posted a decade ago). Home prices are now up 5% on a year-over-year basis.

U.S. Single-family Home Sales and CoreLogic Home Price Index

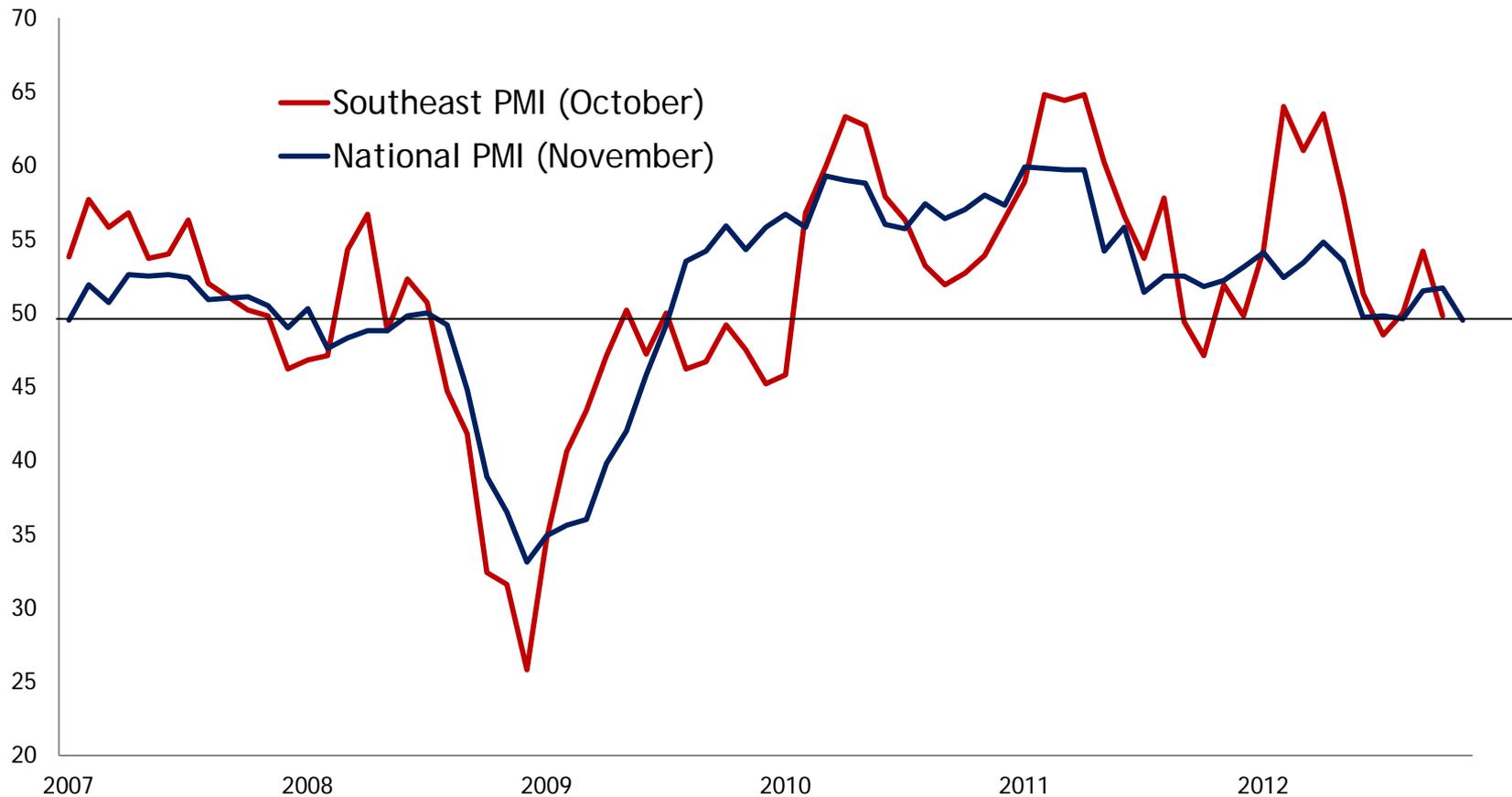


Home sales through October 2012;
Prices through September 2012

Sources: National Association of Realtors, CoreLogic

Growth in the manufacturing sector has flattened in recent months and has become more consistent with a sector that is moving laterally rather than expanding.

Purchasing Managers Indices

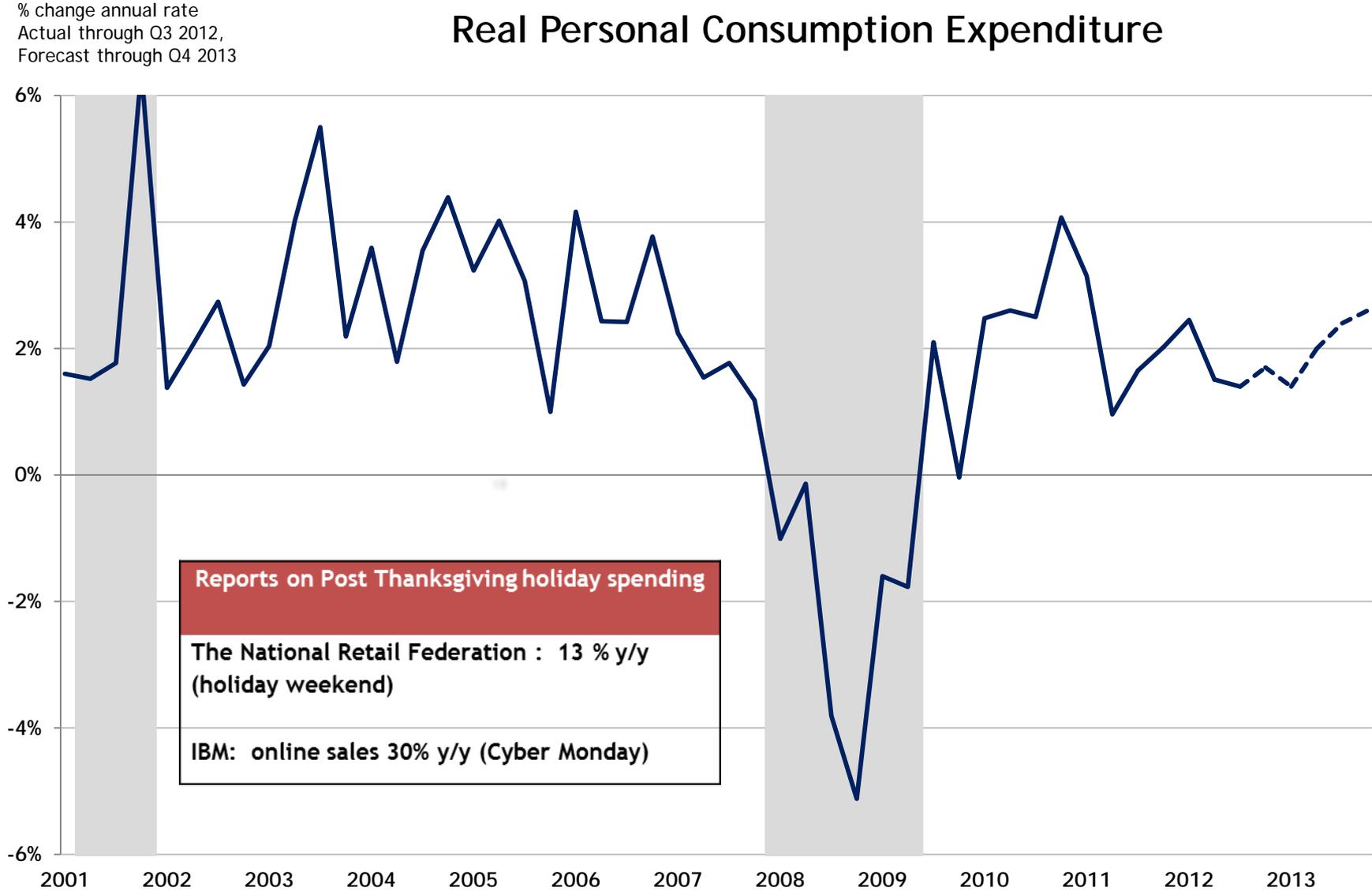


Note: 50+ = Expansion

Sources: Kennesaw State University, Coles College of Business Econometric Center; Institute for Supply Management

Consumer spending has been tracking at a pace of only about 2/3 its average growth of the 2002-2008 period.

Real Personal Consumption Expenditure



Sources: BEA, Blue Chip Consensus Forecast, December 2012

Growth of sales tax revenue in Tennessee has decelerated over the past few months, and MTSU's recent post-election survey of consumer confidence in Middle Tennessee indicted a sharp drop in respondent's overall outlook for the nation's economy.

Tennessee Sales Tax Revenue and Consumer Confidence
October 2012

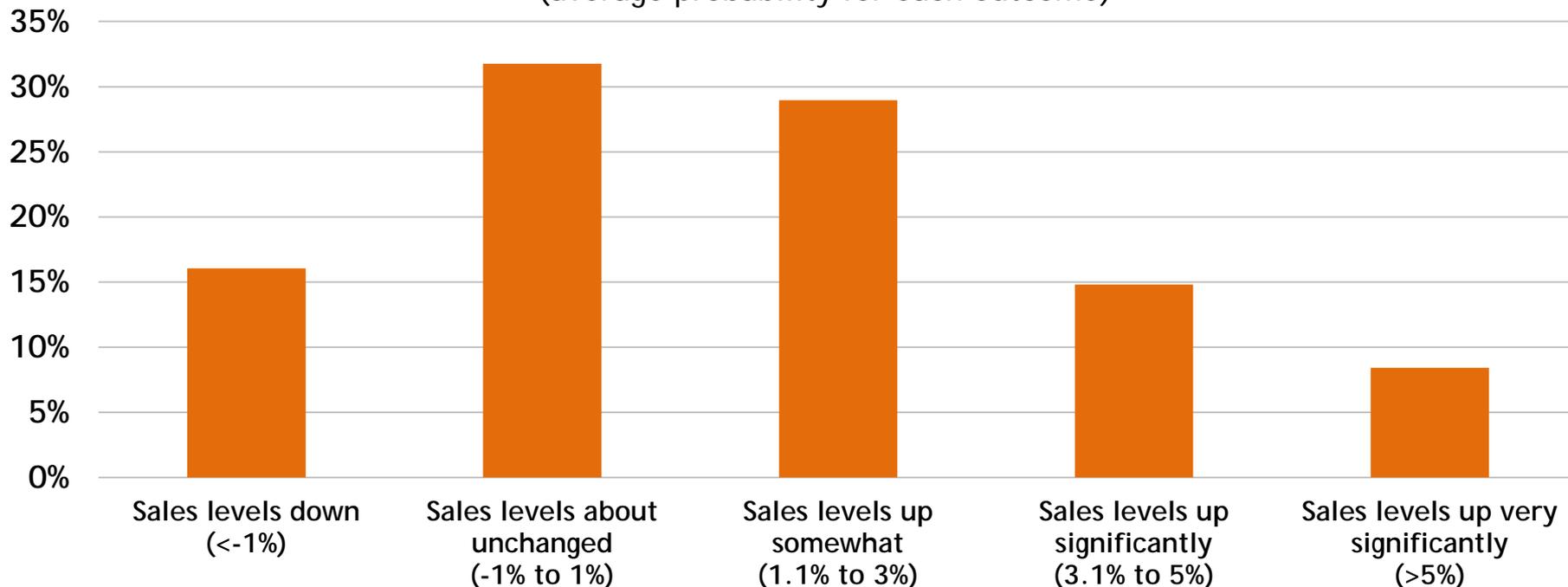
Year-to-year % change,
3-month moving average



Note: Consumer confidence data are through November 2012.
Source: Middle Tennessee State University, Tennessee Department of Revenue

Survey data collected by the Federal Reserve Bank of Atlanta indicate that businesses expect to expand unit sales growth by a little more than 1 percent this year—a somewhat pessimistic projection. However, uncertainty over the outlook appears to be running high, and especially high for firms that report rather optimistic sales growth for the year ahead.

Expected Change in Unit Sales Levels over the Next Twelve Months (average probability for each outcome)



	Unit Sales Expectation (mean)	Unit Sales Uncertainty (variance)
Total	1.20%	2.77%
Top Quintile for expected sales	3.60%	3.20%
Bottom Quintile for expected sales	-0.59%	1.70%

What we're hearing: While the timid economic expansion continues, some bright spots emerged.

There was an unexpected increase in overall optimism among our directors and business contacts in November.

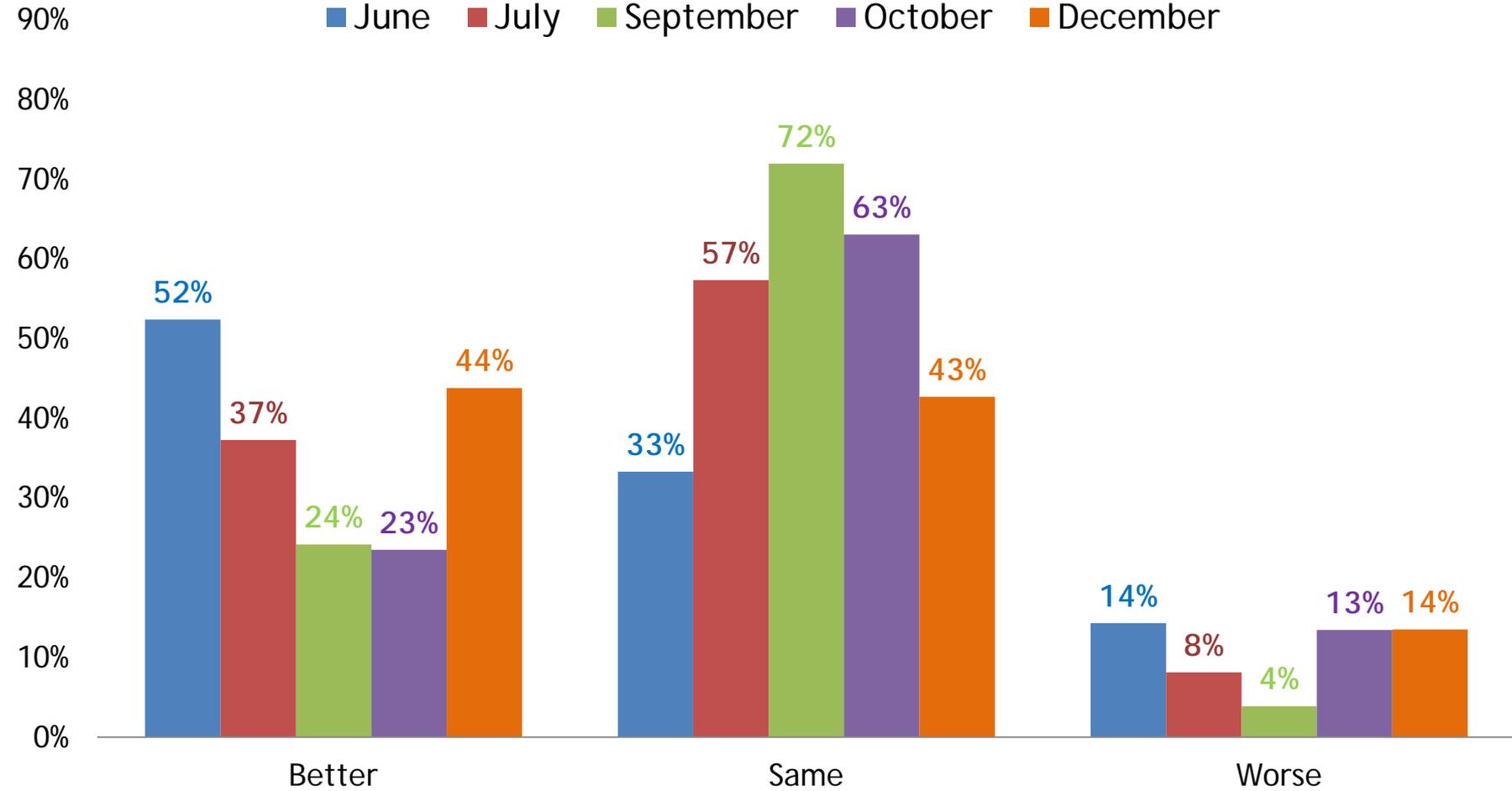
Examples:

- Reports of increasing activity in residential construction and of rising optimism among firms with ties to this sector positioning for additional growth.
- Many firms feel there is pent up demand that could be unleashed if fiscal uncertainties are removed.

However, we continue to hear concern about how the litany of cost-related uncertainties - taxes, healthcare, regulation - could negatively impact businesses growth and hiring plans for 2013 and beyond.

Our Directors' short-term outlook improved in December, but most noted apprehension regarding fiscal policy uncertainties and the unclear healthcare and regulatory cost environment.

Do you expect the growth in your business over the next 3 to 6 months to be better, about the same or worse than they were over the previous 3 to 6 months?



Where we are headed: More of the same kind of bumpy, apprehensive recovery?

“I think the most plausible forecast is continued modest growth with gradual employment gains.”

“Around this more-of-the-same forecast are downside risks of economic shocks as well as chances of somewhat better economic performance if certain risk elements are eliminated or attenuated.”

-- FRB Atlanta President Dennis Lockhart

2013 Outlook



Continuing accommodative monetary policy...until mid-2015, or until “substantial” improvement in the labor market “is achieved in a context of price stability.”

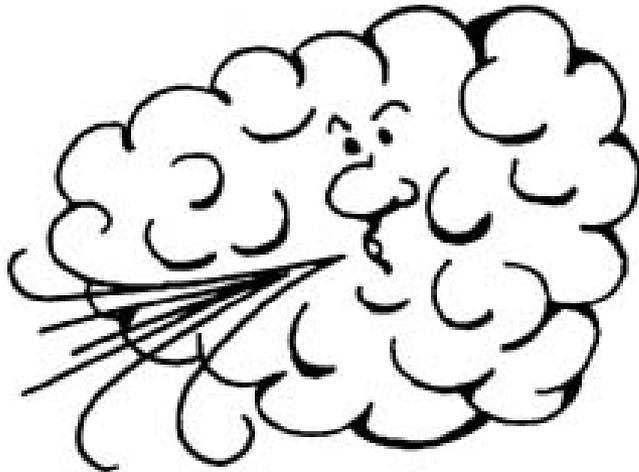
Real GDP growth only modestly above a 2% annual trend.

Moderate inflation close to the Federal Open Market Committee’s target of 2%.

Gradual improvement in the employment picture.

Note: This outlook does not take into account major potential sources of downside risks (e.g., fiscal cliff threats in early 2013).

Looking Ahead: Tailwinds and Headwinds



Fiscal Cliff

Longer-term Fiscal Policy Challenges

Un- and underemployment

Slow Global Demand

Europe



Housing

Energy

Autos

Low Interest Rates (Transmission?)

Improving Business and Consumer

Balance Sheets

(but still a long way to go for consumers)

Thank You . . . Questions?

