The KC Chamber’s Economic Forecast

Friday, October 28, 2016

Welcome
Joe Reardon
President and CEO, Greater Kansas City Chamber of Commerce

Economic Update
Frank Lenk
Director of Research Services, Mid-America Regional Council

Introduction
Brad Smith
Regional President, BMO Harris Bank

Domestic and International Economics, Trends and Insights
Jack Ablin, Executive Vice President and Chief Investment Officer, BMO Private Bank

Introductions
W. Perry Brandt
Managing Partner - Kansas City, Bryan Cave

Election Outlook
Jack Oliver, Senior Policy Advisor, Bryan Cave
Miguel Rodriguez, Partner, Bryan Cave

Audience Q&A

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Status of the U.S. Economy

The recovery from the Great Recession continues and so far has lasted one year longer than the recovery following the 2001 recession and longer than the average U.S. expansion. Employment growth during the current recovery has been solid. Since it began in July 2009, job growth in the U.S. economy has averaged about 150,000 jobs a month, and since 2011, average job growth has been running roughly 200,000 jobs a month. This compares to the approximately 100,000 jobs per month average during the recovery from the 2001 recession. (Chart 1)

Chart 1: U.S. Non-Farm Payroll Employment Change, quarterly

![Chart 1](image)


While employment growth during the current recovery has outperformed the prior one, GDP growth has not. After the 2001 recession, U.S. GDP grew an average of approximately 2.8 percent. This compares to a 2.1 percent average growth rate since the end of the Great Recession. More worrisome is that over the last year, GDP growth has averaged only 1.2 percent. (Chart 2)

Chart 2: U.S. GDP Percent Change, quarterly

![Chart 2](image)

Data are seasonally adjusted at annual rates. Source: Bureau of Economic Analysis (BEA), retrieved from FRED, Federal Reserve Bank of St. Louis.
If employment growth has been stronger than following the 2001 recession but output growth has been weaker, this necessarily implies that the rate of growth in labor productivity has declined post-Great Recession relative to the earlier period. This conclusion is borne out by the data. Whereas GDP per employee grew an average of nearly 2% per year during the recovery from the 2001 recession, it has averaged only three-quarters of one percent growth during the current recovery. Even more troubling is that productivity growth appears to have downshifted further in recent years, as it has averaged only about one-quarter of one percent growth since the beginning of 2011. Even more troubling, labor productivity was fallen 0.5 percent over the last year. (Chart 3)

Low growth in labor productivity typically occurs in the later stages of a recovery, and it may be that is what is occurring here. However, with employment growth showing few signs of abating, this explanation doesn’t quite square with the facts.

### Chart 3: U.S. GDP/Employee, Percent Change from Same Quarter One Year Ago

![Chart showing GDP/Employee growth from 2000 to 2016](chart3)

Data are seasonally adjusted. Source: BEA and BLS, retrieved from FRED, Federal Reserve Bank of St. Louis.

In the short-run, lower productivity means increases in demand for goods and services must be met by hiring more workers rather than by substituting capital for labor, which has helped lower the nation’s unemployment rate. At 5.0 percent in September 2016, it is 5 percentage points below its peak during the Great Recession, and only one-half percentage point above its pre-recession low. The broader U-6 unemployment rate, which includes discouraged workers and part-time workers who desire full-time work in addition to the officially unemployed, also continues to decline in roughly parallel fashion, reaching 9.7 percent in September. This is still 1.6 percentage points above the pre-recession low, which is equivalent to 2.6 million people. (Chart 4)

This seems to suggest there remains considerable slack in the labor market. Yet, that the pace of progress in reducing the unemployment rate has slowed down significantly in 2016 despite relatively constant growth in jobs seems to suggest the economy may be approaching an unemployment rate floor for this business cycle. Such a floor might arise from a combination of successfully pulling people into the labor force who were not working previously as well as labor supply constraints resulting from skill shortages in certain occupations.
The potential growth rate of the overall economy is basically the sum of the productivity growth rate plus the labor force growth rate. Unfortunately, the potential growth of the labor force has also slowed markedly in recent years, principally the result of members of the post-World War II baby boom generation beginning to retire in large numbers. This can be seen in the slowing growth of the working-age population, traditionally defined as that between the ages of 15 and 64 years. (Chart 5) From 2005 to 2010, monthly growth of the working-age population averaged less than 100,000 per month, the slowest rate in the last 60 years. This is why any job growth in excess of 100,000 per month would be expected to reduce unemployment. On average, the working-age population is growing about ½ percent per year, significantly limiting the overall growth potential of the labor force and possibly the economy as a whole due to rising labor supply constraints.

Organization for Economic Co-operation and Development (OECD), retrieved from FRED, Federal Reserve Bank of St. Louis

However, in the short-term, there appears to be some capacity to satisfy potential labor shortages, given the still relatively low labor force participation among prime-age workers, defined as those between the ages of 25 and 54.
Despite relatively strong and consistent employment growth, the current (third quarter 2016) employment to population ratio of 77.9 percent for this age group still remains 2.3 percentage points below its prior peak and nearly 4 percent below its all-time high. In fact, the prime-age employment to population ratio is still about three-quarters of a percent below the prior trough, despite seven years of relatively continuous increases from the low-point created by the Great Recession. If the prior trough in the ratio of employment to population for prime-age workers were again achieved, this would represent the addition of another 1 million workers into the labor force. Achieving the prior peak would represent the addition of 3 million more workers.

In combination, higher than normal U-6 unemployment rates plus lower than normal employment to population ratios indicates there is still additional capacity in the labor market to meet current job growth demands despite low growth of the working-age population. It is unclear, however, how long this can continue, especially since job demands are changing, such that some people who want to work find that jobs are simply unavailable for people with their complement of skills. Should the portion of the working-age population that no longer has the skills required by employers be rising rapidly, this may mean it is unreasonable to expect discouraged workers or those seeking full-time work to be able to participate in the workforce at the same rate as existed in the past. As a result, the estimates of worker availability from still-existing slack in the labor market must be considered upper bounds.

If there were skill gaps occurring, one should see employers expending more effort to find appropriate workers. Indeed, this seems to be the case. The net of 200,000 job gains each month is generated by the difference between the millions of people who are hired each month and the millions who are separated from their current employer, either voluntarily by quitting or involuntarily through layoffs and other discharges. It is this continual job churn that allows employers to gradually shift the skill mix of their workforces by laying off those whose skills no longer match requirements and hiring those whose skills better match.
The search for people with new skills is often signaled by advertising a job opening, and since February of 2015, such openings have generally exceeded hires. This indicates employers have become more aggressive in seeking workers, as well as that the available supply of workers worth hiring isn’t currently able to keep up with their demands.

**Chart 7: U.S. Job Churn – Openings, Hires, Quits and Layoffs, quarterly**

If there is an increasing shortage of workers with the right mix of skills relative to demand, then wages should be improving. This also appears to be occurring, at least for full-time workers. Real median earnings increased 2.1 percent over the past year ending second quarter 2016, which was the eighth consecutive quarter of positive growth in worker earnings after adjusting for inflation. **(Chart 8)** This growth is occurring after years of stagnation or decline, resulting in real median earnings for full-time workers now being at their highest level since the data collection began in 1979.

**Chart 8: U.S. Real Median Earnings Growth, Full-Time Workers, Percent change from 1 year ago, quarterly**

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Data are seasonally adjusted. Source: BLS, retrieved from FRED, Federal Reserve Bank of St. Louis.
That real incomes have finally begun rising more generally is also seen in the recent release of the 2015 American Community Survey. Not only did real median household income jump by 5.3 percent nationally between 2014 and 2015, the biggest gains came at the lower end of the income distribution. According to calculations by the New York Times\(^1\), the inflation-adjusted median household income of those in the lowest 10 percent of income rose 7.9 percent over the period, while the median income those in the 10th to 20th percentile rose 6.3 percent.

These real income increases reflect, in part, the low rates of inflation the nation has experienced in recent years. (Chart 9) Subtracting out the volatile food and energy sectors, overall inflation since the Great Recession has generally been running under 2 percent, as measured by the Personal Consumption Expenditures Index. This measure is similar to the more familiar Consumer Price Index, but does not maintain a fixed market basket of goods like the CPI. Instead, it more closely mirrors the behavior of consumers, allowing substitution of lower-priced for higher-priced goods and services as prices change.

\[\text{Chart 9: U.S. Inflation Rate: Core PCE – Personal Consumption Expenditures Price Index, Less Food and Energy}\]

Data are seasonally adjusted. Source: BEA, retrieved from FRED, Federal Reserve Bank of St. Louis.

This low rate of inflation has allowed the Federal Open Market Committee (FOMC) of the Federal Reserve Board to keep its policy interest rate, the Federal Funds rate, extraordinarily low by historical standards. After announcing in December of 2015 they would increase this rate from near zero to a range of ¼ to ½ percent, the FOMC has so far not voted to increase the Federal Funds rate again in 2016. (Chart 10) Sluggish GDP growth at home, uncertainties abroad, and as yet no significant observable acceleration of inflationary pressures have combined to produce a significantly slower path toward monetary policy normalization that originally anticipated.

**Chart 10: Federal Funds Rate, quarterly**

Such highly accommodative monetary policy has been instrumental in generating the economic recovery from the Great Recession and maintaining the current relatively solid employment growth. Yet, the economy’s ability to sustain or accelerate its rate of growth over the medium- to long-term is uncertain given its slow growth in productivity and potential labor force. As a result, the recent strength in income gains may become jeopardized, as rising productivity increases the value of labor and enables both businesses and workers to experience income growth. While demography may be destiny, productivity has typically been more responsive to policy. Historically, productivity gains occur when long-term investments in infrastructure, education and research combine with increased innovation and entrepreneurship in businesses. The former requires public dollars and the latter requires optimism about the possibility of future gains. Unfortunately, both have been in short-supply in recent years, to the detriment of the U.S. economy’s long-run growth potential.

**U.S. Economic Forecast**

After their September 2016 meeting, the FOMC released their economic projections for the U.S. economy going forward. The median forecast of members was that U.S. GDP would grow 1.8 percent between the fourth quarters of 2015 and 2016, rebound slightly to 2.0 percent growth in 2017 and maintain that rate through 2018. However, the median expectation for the longer-run growth rate of the economy is 1.8 percent, down from the 2.0 percent rate from the June FOMC economic projection.

The range of projections from members reflects current levels of uncertainty regarding the path of the economy over the next eight to twelve quarters. (Chart 11) The range is widest in 2017, when some see an acceleration of growth to 2.5 percent while others see a continued slow decline in the economy’s overall growth rate to 1.6 percent. The range narrows slightly in 2018, with 2.3 percent GDP growth projected at the high end and 1.5 percent at the low end.
Overlaid on the FOMC projections is the U.S. GDP forecast from the University of Michigan’s Research Seminar in Quantitative Economics (RSQE). This is the source of the U.S. forecast used as input into the local forecast, and is a change from prior years’ forecasts that have used the U.S. forecast from Moody’s Analytics. In recent years, though, the Moody’s forecast has been overly optimistic, exceeding the upper end of the FOMC range as it called for a period of GDP growth near 3 percent. That optimism has not been borne out by the actual performance of the economy, however. RSQE has a reputation of being an accurate forecast. It is also one that works well with the model used to make the local forecast, Policy Insight from Regional Economic Models, Inc. (REMI), and for these reasons, this economic forecast adopts RSQE to serve as the U.S. driver from the REMI model of the Kansas City metropolitan area economy. The RSQE forecast was prepared in September 2016.

Though it is more conservative than the Moody’s forecast has historically been, it mostly falls on the optimistic side of the FOMC median and, in 2017 comes close to exceeding the FOMC range. Measured on fourth-quarter to fourth-quarter basis, RSQE expects U.S. GDP to grow 1.9 percent in 2016, 2.4 percent in 2017 and 2.1 percent in 2018.
The FOMC projections also provide information concerning the anticipated future path of monetary policy. The so-called “dot plot” reproduced below (Chart 12) captures individual participants’ projections. There is clearly a wide range of views represented concerning the appropriate level of the Federal Funds rate going forward. However, it is still instructive to examine the central tendency of the views.

In September the vast majority of the Committee expected the Federal Funds rate to be at least ¼ percent higher by the end of 2016 than it now. Going forward, the median projection is for the rate to increase ½ percent in 2017 and another ¾ percent in 2018, reaching a level between 1.75 and 2.0 percent at that time. In the longer run, the median projection is for the Federal Funds rate to settle at 2.9 percent. The longer-run Federal Funds rate represents the level at which Committee members believe monetary policy is neither expansionary nor contractionary. The current projection is a slight reduction from the June FOMC projection of 3.0 percent, consistent with the lowering of projected longer-run GDP growth.

Chart 12: FOMC Participants’ Assessment of Appropriate Monetary Policy Expected Federal Funds Rate at end of year

Consistent with its generally higher forecast for GDP growth, RSQE anticipates the Federal Funds rate will increase at a slower rate than the median view of the FOMC. They expect the Funds rate to remain unchanged in 2016, then to increase ½ percent in 2017 and another ½ percent in 2018. This results in a forecast Funds rate of 1.4 percent by the end of 2018, about ½ percent lower than the median estimate of FOMC members.

Status of the KC Economy

While many of the Kansas City area’s peer metropolitan areas have bounced back from the Great Recession, the Kansas City region had not been keeping up. In response, leaders from the business, civic, philanthropic, education and local government communities launched KC Rising to help the region regain its competitive edge. KC Rising, developed as a partnership between the Civic Council of Greater Kansas City, the Mid-America Regional Council, the Kansas City Area Development Council and the Greater Kansas City Chamber of Commerce, is designed as a 20-year strategy focused on improving the key drivers of regional economic prosperity – globally competitive economic sectors, innovation and entrepreneurship, and human capital. This initiative has adopted the goal of becoming a top-10 metro among our peers along three key metrics: GDP, quality jobs, and median household income. Peer metros were defined as the 15 immediately larger and 15 immediately smaller by population. Quality jobs were defined as those typically requiring a post-secondary degree or certificate for entry, or that paid above the median wage.

Based on the latest available data, the Kansas City area, the 16th largest metropolitan area among its peers by definition, is currently ranked 15th in GDP, 12th in quality jobs and 12th in median household income. As such, it is punching above its weight. However, to break into the top 10 and remain there, the regional economy must consistently grow faster than its peers. If it were to regularly achieve a top-10 growth rate in each of the key metrics, this would be sufficient to move
into the top 10 over time. Assessing whether the Kansas City area economy is growing tenth-fastest or better along the key metrics then becomes a way of determining if the region is on track to achieve the ambitious goal set by KC Rising. Unfortunately, between 2014 and 2015, the last years for which historical data is available, metropolitan Kansas City’s real GDP growth rate ranked 25th among the 31 peer metros, at 1.5 percent. (Chart 13) As such, the region is at risk of seeing its rank fall rather than increase. By contrast, the 10th fastest growing metro, Richmond, Virginia, saw its GDP grow nearly 4 percent.

**Chart 13: Percent increase in real GDP 2014-15, KC relative to 30 peer metros**

Similarly, the region’s performance with respect to creating high-quality jobs also was insufficient to put it on track to break into the top 10. (Chart 14) The region’s expansion of the number of quality jobs by 1.6 percent between 2015 and 2016 unfortunately only ranks 21st among its peers. Sacramento, the 10th ranked metro in quality job growth rate, added jobs nearly twice as fast as the Kansas City area at 2.9 percent.

**Chart 14: Percent increase in quality jobs 2015-16, KC relative to 30 peer metros**

On the other hand, real median household income in the Kansas City area shot up 6 percent between 2014 and 2015. This ranks second among its peer metros behind Nashville which, at 10 percent real growth in income, appears to be something of an outlier. (Chart 15) If the region is able to maintain its relative performance in median household income growth with respect to its peers, it is likely to break into the top ten over the next several years.

**Chart 15: Percent increase in real median household income 2014-15, KC relative to 30 peer metros**

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_Shaded dots represent the top 10 metros. The first and tenth ranked metros are labeled for reference. Source: BEA._

_Shaded dots represent the top 10 metros. The first and tenth ranked metros are labeled for reference. Source: JobsEQ._

_Shaded dots represent the top 10 metros. The first and tenth ranked metros are labeled for reference. Source: Bureau of the Census, 2015 American Community Survey (ACS), 1-year data._
KC Rising identified several key sectors of the region’s economy important to the region’s capacity to trade goods and services with the rest of the world, such as manufacturing, wholesale trade, information (which includes telecommunications), finance and insurance, transportation and warehousing, and professional, technical and scientific services (which includes the engineering, architecture, design and IT industries, as well as portions of the life sciences industry). In addition, portions of the health care industry and the construction industry are both exporters of services and tightly tied to the prior sectors, so they are also included as priorities for examination.

These traded sectors bring outside dollars to the metropolitan economy where they are recirculated to generate additional economic growth. As such, these traded sectors form the base of the regional economy, and their performance largely determines the region’s overall competitiveness relative to its peers.

Unfortunately, only two of these sectors have seen strong employment growth over the last 14 years in the Kansas City region, health care and professional, scientific and technical services. (Chart 16) The good news is these two sectors are also the largest traded sectors in terms of their number of jobs, with health care currently employing about 147,000 workers and professional services about 88,000.

Employment in the wholesale trade and the finance and insurance sectors have been stable over the period. The construction, manufacturing and transportation and warehousing sectors all have fewer employees in 2015 than they did in 2001, but have been stabilizing and rebounding since the end of the Great Recession. Only the information industry has seen steady and steep declines, losing nearly two-thirds of its jobs over the period.

**Chart 16: KC Employment by Industry, 2001-2015**

Examining trends in these key sectors since the Great Recession in more detail, the following sequence of charts compares their job growth in metropolitan Kansas City to that occurring in the nation as whole, quarter by quarter, measured on a year-ago basis. The charts are ordered from best-performing to worst-performing sectors relative to the nation, left-to-right and top-to-bottom, based on relative growth over the most recent year.

In 2012 and 2013, the region’s total employment generally grew on par with the nation’s. Since then it has grown slightly faster. As of the fourth quarter of quarter of 2015, the last period for which data is available, the region’s total employment was growing at a rate of 2.3 percent compared to 2.1 percent growth for the U.S. (Table 1 on page 16)
Professional, scientific and technical services has been the Kansas City area’s best-performing sector relative to the nation. (Chart 17) Throughout most of the period since 2012, employment in this sector locally has grown significantly faster than it has nationally. During the most recent year ending fourth-quarter 2015, the professional services sector in metropolitan Kansas City grew 7.6 percent, more than twice as fast as the nation as a whole.
Table 1: 2014Q4-2015Q4 Job Growth

<table>
<thead>
<tr>
<th>Sector</th>
<th>U.S.</th>
<th>KC</th>
<th>Difference</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total Employment</td>
<td>2.1%</td>
<td>2.3%</td>
<td>0.2%</td>
</tr>
<tr>
<td>Professional, Scientific and</td>
<td>3.3%</td>
<td>7.6%</td>
<td>4.3%</td>
</tr>
<tr>
<td>Technical Services</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Health Care</td>
<td>2.9%</td>
<td>4.1%</td>
<td>1.2%</td>
</tr>
<tr>
<td>Manufacturing</td>
<td>0.6%</td>
<td>1.6%</td>
<td>1.0%</td>
</tr>
<tr>
<td>Finance and Insurance</td>
<td>2.1%</td>
<td>2.8%</td>
<td>0.7%</td>
</tr>
<tr>
<td>Construction</td>
<td>5.0%</td>
<td>5.2%</td>
<td>0.3%</td>
</tr>
<tr>
<td>Transportation &amp; Warehousing</td>
<td>4.6%</td>
<td>2.1%</td>
<td>-2.4%</td>
</tr>
<tr>
<td>Wholesale Trade</td>
<td>0.8%</td>
<td>-2.2%</td>
<td>-3.0%</td>
</tr>
<tr>
<td>Information</td>
<td>1.3%</td>
<td>-28.6%</td>
<td>-29.9%</td>
</tr>
</tbody>
</table>

Source: Quarterly Workforce Indicators (QWI), Bureau of Labor Statistics

Growth in health care employment generally tracked national trends until 2015 when local employment in this sector accelerated relative to the nation. By the end of the year, the regional health care industry was adding jobs at a 4.1 percent rate, compared to 2.9 percent job growth in the national health care industry.

The region’s manufacturing industry also experienced an acceleration of employment growth relative to the nation in 2015. However, this occurred after generally posting sub-par employment growth through most of the post-recession period. By the end of 2015, though, local manufacturing employment was growing at an annual rate of 1.6 percent, a full percentage point higher than the 0.6 percent growth rate experienced nationally.

Growth in metropolitan Kansas City’s finance and insurance employment has been quite volatile since the end of the Great Recession, at times growing significantly faster and at times significantly slower than the nation as a whole. In 2015, it has been growing faster than the nation, though its growth advantage slipped throughout the year. By the end of the year, jobs in the Kansas City area’s finance and insurance industry were growing at an annual rate of 2.8 percent, compared to 2.1 growth in the U.S.

Local construction employment has generally tracked very closely with national trends post-recession. In the most recent period ending fourth-quarter 2015, construction jobs in the metropolitan area were growing barely faster than in the U.S. generally, at an annual rate of 5.2 percent compared to 5.0 percent nationally.

The remaining key sectors – transportation and warehousing, wholesale trade and information – have all been underperforming the nation on job growth recently. Wholesale trade appears to have seen a sudden deceleration in job growth in 2015 after years of either tracking with or exceeding national trends. Transportation and warehousing, on the other hand, has been adding jobs at a slower rate locally than nationally throughout most of the post-recession period. Job growth has been consistently positive, however. This is not the case for the information sector. Nationally, this sector has barely added any jobs since 2012. Locally, the declines in employment have been significant and they accelerated sharply in 2015.
In part because the Kansas City economy has been growing slightly faster than the U.S. economy in recent years, the region’s unemployment rate is lower. (Chart 18) In second quarter 2016, the official unemployment rate for the metropolitan area stood at 4.1 percent, significantly below its pre-recession low of 4.8 percent. By comparison, the second quarter unemployment rate for the U.S. was 4.8 percent, still significantly higher than its pre-recession low of 4.2 percent.

Chart 18: KC vs. U.S. Unemployment Rate

As the unemployment rate has continued to push downward after the Great Recession, it has finally reached a point where nominal wages are beginning to show an upward trend. (Chart 19) The region’s average weekly wage in the fourth-quarter 2015 was 4.5 percent higher than a year ago. Nationally, wages grew at an even faster pace, 6 percent, helping to maintain Greater Kansas City’s reputation as a low-cost place to do business.

Chart 19: KC vs. U.S. Average Weekly Wage, Percent change from 1 year ago

Source: Quarterly Census of Employment and Wages (QCEW), Bureau of Labor Statistics
**KC Economic Forecast**

The prior trend information along with the RSQE forecast was input into the REMI model in order to produce a forecast for how the regional economy will change between 2016 and 2018, measured on a fourth-quarter to fourth-quarter basis. *(Chart 20)*

Overall, the regional economy is expected to mostly track the national economy. After growing slightly slower than the U.S economy in 2015, the recent acceleration in job growth is expected to push the regional economy slightly faster than average in 2016, growing 2.0 percent compared to the nation’s 1.9 percent. In 2017, regional growth in GDP is expected to remain steady at 2.0 percent. However, RSQE’s forecast suggests the national economy will accelerate to 2.4 percent GDP growth, though this forecast is admittedly at the high end of the range anticipated by most economists. By 2018, the growth of both the local and national economies is expected to ratchet down a notch, with metropolitan GDP forecast to grow 1.9 percent while U.S. GDP is forecast to grow 2.1 percent.

**Chart 20: KC vs. U.S. Real GDP Growth, 2015-2018, Annual change, fourth-quarter to fourth-quarter basis**

![Chart 20](image)

Source: Mid-America Regional Council (MARC), as forecast by the REMI model. Note that REMI estimates GDP using different methodology than the figures from BEA, one that better takes into account differences in inter-metropolitan costs of living.

Overall, the region’s employment is expected to expand at rates similar to those of the past couple of years. Total employment in metropolitan Kansas City is expected to climb by 20,100 in 2016, measured on a fourth-quarter to fourth-quarter basis. Total job growth is expected to slow slightly in 2017, to 19,300, in part reflecting the difficulty in finding employees for high demand occupations in STEM-related fields. In 2018, as the overall economy begins to cool, job growth downshifts further, to a still-respectable 17,300 jobs.

Examining the region’s projected job growth by sector reveals a familiar pattern. *(Chart 21)* Medical services and professional, scientific and technical services lead the way. Medical services is expected to add about 5,000 jobs annually over the forecast period, while professional services is expected to add nearly 4,000.

Other traded sectors also are expected to add significant jobs over the projection period. Construction is expected to grow as home-buying continues to recover. It will add roughly 1,300 jobs annually between 2016 and 2018. Transportation, finance and wholesale trade are also expected to grow in employment, adding annually an average of 700, 400 and 400 jobs respectively over the projection period.

Two traded sectors are expected to lose jobs, manufacturing and information. Manufacturing is a bit of a surprise given its recent rebound, but it may be that a combination of productivity improvements and a strong dollar caused by international uncertainty conspire to hold hiring down, resulting in a small loss of 200 jobs annually, on average, from 2016 through 2018. The loss of about 1,500 jobs annually in information is not unexpected but, at some point, those losses should diminish and employment should stabilize. Large recent losses, though, are undoubtedly weighing on the forecast.
Sectors that serve the local population more than external markets tend to be more labor-intensive industries, and several of these are expected to add a significant number of jobs. This includes retail trade, which is expected to average a gain of 2,100 jobs annually from 2016 through 2018. Retail trade employment growth diminishes over this period, however, partly in response to rising Internet sales. The accommodations and food services industry and the administrative services, also are expected to add an average of over 2,000 jobs annually, but growth in these local-serving industries remains more stable throughout the projection period.

Chart 21: Kansas City Employment Change by Industry, Measured fourth-quarter to fourth-quarter

Source: Mid-America Regional Council (MARC), as forecast by the REMI model.

Conclusion

The current recovery from the Great Recession is already longer than average. While there are signs of a tightening labor market, so far this has led to rising wages without rising inflation without major labor supply constraints hindering overall growth. This is a rare combination of events, and should be celebrated.

Going forward, there is little sign that the recovery is in danger of running out of steam. It is likely more vulnerable from external events than internal frictions. It appears that GDP growth around 2 percent is the new normal. Even at this pace, prosperity is nonetheless beginning to rise for all.

The principal storm clouds on the horizon relate to the current slow growth – and even negative growth – of labor productivity. In the long-run, rising productivity is what pays for rising standards of living. To ensure the hard-fought gains to achieve a more inclusive prosperity are not short-circuited will require investments that improve the capacity of workers to produce higher-valued goods and services. Such investments include not only physical capital – infrastructure, plant and equipment – but the investments in human capital required to ensure greater access to, and greater ability to create, opportunity.
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North American Outlook: Election Uncertainty Clouds Outlook

Sal Guatieri, Senior Economist, BMO Capital Markets

BMO Harris Bank

With time running out on one of the most unusual elections in U.S. history, the race is still up for grabs. The only thing we know for sure is that the economy could look a whole lot different depending on who wins. Under a Clinton presidency, increased spending on infrastructure, education, health care and renewable energy will largely be offset by higher taxes on the wealthy, resulting in a modest increase in the budget deficit and a similarly small lift to the economy.

Under a Trump presidency, the range of possible economic outcomes is much wider. While Trump has scaled back his personal income tax cuts, they (along with lower corporate, capital gains and investment income taxes) still amount to $4.4 to-$5.9 trillion over a decade, according to the Tax Foundation. While that’s about half the original estimate, even the lower end of the range works out to more than 2% of GDP per annum. Congressional concerns about the budget deficit could rein in Trump’s ambitions, even if the Republicans hold both chambers. But not all of the tax cuts are needed to give the economy a boost. As well, his favorable treatment of energy producers could unleash new investment spending on pipelines and drilling. However, it’s his other proposals—on trade (with import tariffs on Chinese and Mexican goods possibly leading to retaliatory actions on U.S. exports, disruptions to supply chains and higher inflation) and on immigration (as plans to deport up to 11 million illegal migrants will shrink the work force when qualified workers are in short supply, resulting in higher inflation)—where the challenges begin to mount. Throw in concerns about a rising budget deficit (which could drive up interest rates) and plans to replace the Fed Chair (when her term expires in early 2018), and businesses and investors could face more uncertainty.

Unlike actions that affect the budget, the President has some unilateral control over immigration and trade. The President does not need congressional approval to withdraw from NAFTA after six months’ notice. While Congress would need to sign off on a 45% tariff on Chinese goods, Trump could unilaterally impose a tariff of up to 15% for 150 days.

While the U.S. economy is poised for a better second half of 2016, the outlook for next year is fogged up by election uncertainty. Depending on whom you believe, if Donald Trump wins, the economy is either poised to accelerate on massive tax cuts and deregulation, or is headed for a downturn due to increased protectionism, less immigration and greater uncertainty. The Fed could either lean more heavily against his stimulative fiscal policies, or be forced to ease if growth goes into reverse.

Our base-case is that U.S. economic growth improves from an estimated 1.6% in 2016 to 2.2% in 2017. Consumers are still spending at a healthy rate, housing markets are creeping forward and business investment appears to be turning the corner. Auto sales seem to have plateaued, albeit at record highs. Surprisingly, exports have risen three months in a row, after sagging 9% in the previous two years as the dollar soared 20%. Although most indicators weakened in August, many rebounded in September. GDP growth looks to have popped to around 3% in Q3 after averaging 1.1% in the first half of the year. The FOMC wants to normalize policy but remains divided on the time and pace. We lean toward a December rate increase, assuming no economic hiccups or post-election fireworks. We expect an additional two moves in each of the next two years, a slightly slower pace than anticipated by the FOMC.
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US Economic and Business Environment

By Clay Nickel

Director of Investment Strategy, Arvest Wealth Management/Investment Management Group

The U.S. Economy Plods Along: The sure-footed, slow moving economy continues to grow at an inflation adjusted rate of approximately 2% per year. We anticipate this to continue through 2017. On balance, a number of forward looking indicators continue to point to a low probability of recession over the next 12 months, although slightly elevated from last year. It is important to point out that the six year old economic expansion is now “late cycle,” or long in the tooth, and at this stage we see increasingly mixed economic data. While we continue to monitor the mosaic of leading indicators, we are especially attuned to ISM survey data and Initial Jobless Claims. Should the ISM index fall into the mid-to-low 40s, or should weekly jobless claims increase above 300,000, we would treat them as early warnings of an increased likelihood of a U.S. recession. Absent these developments, we maintain that recession risks are low.

Inflation Nation: While we have been unconcerned about inflation for the last few years, we do anticipate inflation to normalize. The current 2% inflation rate (or less, depending on your preferred inflation measure) should lift towards 2.5% over the next year—still below long-term average inflation rates, yet starting a trend that should continue beyond 2017 without becoming problematically high. Inflation could rise more rapidly should nationalism and trade protectionism, espoused to a greater or lesser degree by both major party Presidential candidates, become policy and not just campaign rhetoric. The potential for less trade could not only dampen already low growth rates, but the reduction in global competitive forces could further pressure U.S. inflation.

Inflation pressures could be further exacerbated by the abysmally low productivity levels. Productivity in the US continues to hover near zero while unemployment rates are at levels economists consider to signal full employment. Historically, during periods of full employment, inflation has been mitigated with improvements in productivity. Given the dearth of capital investment in the US, productivity gains are unlikely.

The Workers’ Share: Labor market data are somewhat mixed. The common unemployment measure is at 5% while a broader measure that also includes discouraged workers, those who want to work but are not actively looking, and those working part time but desire full time employment is at 9.8%--a level consistent with labor market slack. At the same time, the Bureau of Labor Statistics JOLTS report shows record/near record levels of open, unfilled job postings. The demand for qualified labor is outpacing the supply of available qualified workers. This will likely fuel increases in wages. We are already witnessing increasing wage gains. This trend is likely to continue. Business profits will be pressured by higher labor costs, especially if investments in productivity enhancements are not made.

The Four Year Itch: We are loath to discuss the impact of Presidential election outcomes given two major party candidates with historically high unfavorability ratings and our general predisposition that Presidents have less economic impact than ascribed by most investors and small business operators. Nonetheless, it appears highly likely that Secretary Clinton will handily win with roughly 300 electoral college votes (of the 270 required). At the same time, we currently anticipate that the Republicans will retain control of the House of Representatives, making potentially economically impactful initiatives such as tax increases and sweeping regulatory legislation unlikely, especially since it is anticipated that she may have less than 50% plurality of the popular vote, precluding a governing mandate. However, should the election evolve into a Presidential landslide, which is increasingly probable, House control will be in question.

With political gridlock and the heightened use of Presidential Executive Orders, there is still the chance that small business growth and formation, which is inordinately affected by increased bureaucratic regulation, may be negatively impacted. While the risk is not immaterial, it is largely anticipated that a Clinton Administration would generally see a continuation of President Obama’s policies instead of a dramatic shift or increase, resulting in an environment similar to the current situation.
Carry On: In last year’s KC Chamber Economic Forecast publication we closed with the following:

“Think like a man of action, act like a man of thought.” –Henri Bergson. Economic data is best utilized to inform decision making and action. While reticence has reigned for many small and mid-sized businesses, since 2013 we have advocated that decision makers take advantage of the plodding, improving US economic environment, as well as the concurrent low interest rates and favorable lending environment, to continue to employ growth oriented investment in their business. Although the shining sun is moving towards sunset, it appears that there is still time to prudently make hay.

To that we would add Reinhold Niebuhr’s Serenity Prayer: God, grant me the serenity to accept the things I cannot change; Courage to change the things I can; And wisdom to know the difference.

We wish you the best of success in 2017.

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2016 has proven to be a decent year for markets despite all of the distractions. Of course, that could change in an instant, but in spite of so many headwinds, markets have produced reasonable returns.

Gains in employment are the best economic news of the year, actually good since 2009. From a peak of 10% in 2009, the unemployment rate has been consistently at or below 5%. Lower weekly unemployment claims support the expectation that job gains will continue, at least for the immediate future. Consumer confidence has been on an upswing this year. This is particularly good news because consumers drive GDP growth in the U.S. There are many reasons for the GDP improvement, including more jobs, less unemployment, low mortgage rates, gasoline prices are still low and wages have started to improve...slowly. Consumers haven’t been overspending though. The new “smarter” consumer has been saving more and been cautious with mortgage debt. American consumers seem to be more focused on balance sheet repair since the recession of 2008-2009. Good news for the long-term, but something of a headwind in the near-term for an economy built on consumer consumption.

New single family home starts have improved this year and new home prices are up. However, existing home sales are weaker, impacted by the lack of inventory...which has led to higher prices, significantly higher in some markets. Those higher prices make it more difficult for buyers to qualify, thus causing slower sales.

Leading economic indicators are up, but the pace of improvement has started to slow. This implies that growth over the next six to nine months may show some softness.

All in, U.S. economic news is mixed.

The U.S. presidential election is just around the corner. A few things look highly likely to me. First, both candidates are emphasizing the need for infrastructure spending. The only way to finance a significant increase in spending is to borrow more. So, it seems likely that government debt, which is already high relative to GDP, will move higher. Because of incredibly low interest rates, the government has been able to keep our debt problems out of the headlines. That may not be the case for long, even if interest rates move up only a small amount. Secondly, defense spending is going to move higher. We live in a precarious world. Regardless of who is elected President, we are going to need to spend more on defense. Again, additional spending will enlarge the U.S. deficit. Finally, it seems likely that the U.S. will experience a recession some time during the first term of the new President. Recessions cause tax receipts to decline and government spending to increase. I am a broken record on this topic thus far, but U.S. government spending is set to jump and the deficit will return as a major political debate in the next few years.

Central banks around the globe face a number of challenges in maintaining stimulus and trying to keep expectations higher for longer due to stubbornly weak inflation. The comment about stubbornly weak inflation may be slowly changing. The 10-year Treasury started 2016 with a yield of 2.27%, reached a low of 1.37% in early July and is now at 1.75%. There has been small, but noticeable increases in average hourly earnings and the employment cost index. Interest rates have probably seen their lows. The Federal Reserve’s preferred measure of core inflation is the personal consumption expenditures price index. Through August, the year over year increase had moved up to 1.7%,
still below the Fed’s goal of 2.0%, but now slowly gaining ground. Should overall economic growth remain modest, a sustained increase in inflation will create stress in markets and the economy.

Jim Huntzinger
Chief Investment Officer
BOK Financial Corporation
October 20, 2016

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25.7% of companies in the SBEI increased staff, 48.1% made no changes and 26.2% decreased employee totals.

**SEPTEMBER AT A GLANCE**

- **25.7%** Increased Staffing
- **48.1%** No Change
- **26.2%** Decreased Staffing

**6 MONTH OVERVIEW**

**TRENDING BY INDUSTRY**

- Agriculture
- Construction
- Education
- Transportation
- Legal & Entertainment
- Insurance
- Non-Profits
- Retail & Wholesales
- Total Trend

**TRENDING BY REGION**

- **0.29%** Increased
- **0.20%** No Change
- **3.78%** Decreased
- **0.22%** Total Trend

*There’s little doubt that small business owners have hit the pause button on hiring as the rhetoric and tumultuous election cycle has left many dissecting tweets and headlines to figure out where the candidates stand on the issues that will affect them. Three months of small business employment count demonstrates a willingness among employers to allow natural attrition to reduce labor costs in advance of greater certainty from the election itself.*

- Philip Morstinger, President of CBIZ Employers Services Organization

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The KC Chamber’s 2017 Economic Forecast

United States Economic Forecast

Pundits and analysts overuse the word uncertainty when discussing the economy, especially during election seasons. Indeed, you’ve likely read a lot about how uncertainty is holding back the economy. But evidence for this hypothesis is surprisingly slim. It’s easy to attribute problems to uncertainty, since it isn’t something that’s easily measured. So it’s hard to know for sure whether businesses have indeed cut back spending as overheated election-related rhetoric, featuring warnings of imminent catastrophe, makes the world more uncertain. But as of August, we do know a few things:

- **Businesses are willing to hire.** After a short lull, US employment growth seems to have jumped back to over 250,000 per month. Businesses would be less likely to add workers if uncertainty were a serious problem.

- **Consumer confidence remains high.** And while consumers and businesses may not think the same way, consumers likely wouldn’t express optimism if they viewed the election as a significant source of potential problematic changes.

- **Household saving has been slowly failing.** While that’s not necessarily for the best in the long run, household members probably wouldn’t willingly cut back on saving if they felt good about the economy. All this suggests that it would be an uphill battle to demonstrate that the recent economic weakness has been the result of presidential-campaign uncertainty.

“While that’s not white-hot growth, it may explain why businesses are hiring so many employees (needed in the service sector) even when overall GDP growth has been relatively slow.”

It’s true that US economic growth has been relatively weak (just 1.2 percent) during the past year. But much of that weakness is concentrated in a few areas: Nonresidential investment (down 1.3 percent) and exports (down 1.2 percent) have been key factors. Both of these sectors face significant negative fundamentals. Investment has been hit hard by the decline in energy investment (which is very capital-intensive), and exports are suffering from weak demand and a strong dollar.

Much of the weakness has therefore been in goods GDP, which grew only 0.5 percent over the past year. Services GDP, in contrast, grew 1.7 percent. While that’s not white-hot growth, it may explain why businesses are hiring so many employees (needed in the service sector) even when overall GDP growth has been relatively slow.

Both major-party nominees have proposed infrastructure spending programs. The likelihood of the US government enacting such a program remains low, considering Congress’s ongoing reluctance to increase spending. And the economy may be nearing full employment, although the Deloitte forecast assumes that there is substantial slack in the labor force.

Nevertheless, the chances of a fiscal stimulus are larger than they were before the campaign got under way. If that were to happen, the United States would join Canada among the G-7 as countries willing to take advantage of low interest rates to stimulate the economy and finance some public works.
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Subdued Economic Outlook Continues
By Tim Laughlin – Director, Investment Management, First National Bank

From an economic perspective, 2016 is looking similar to many of the previous years. After a slow start, evidence indicates the pace of economic activity is picking up. Real GDP growth in the second quarter was a subdued 1.4% SAAR, but we expect third quarter growth will be noticeably better. However, declining productivity and demographic forces are impeding growth. These headwinds will likely keep economic activity below the U.S. economy’s historical average growth rate for the foreseeable future.

The most positive component of the economy is the strength and stability we see with the consumer. Personal consumption was up 2.9% in Q2 and we expect consumption to remain relatively strong over the near-term future due to favorable tailwinds. Undoubtedly, the consumer has benefited from the improving jobs market. Other metrics, such as the rise in average hourly earnings and the lengthening average hourly work week, should also be positives for demand. Rising home values and stock market gains have raised consumer net worth and this “wealth effect” supports increased spending too.

The biggest headwind for the economy has been weakness in private investment. Nonresidential investment spending (which includes the spending businesses make on machinery, factories, equipment and inventory) has fallen for three straight quarters. There are numerous reasons for weak spending, but the main reason for falling investment has been due to the dramatic pullback in spending in the energy sector. As oil prices moved lower over the last two years, oil companies markedly scaled back spending. As oil prices ebb higher, we anticipate the sharp decline in investment spending from this sector to moderate. Moreover, we anticipate inventory adjustments to add to investment spending over the coming quarters. Overall, the drag on growth from the private investment component of GDP should subside.

Our outlook related to inflation is balanced. We have moved away from deflationary fears, while inflationary pressures remain contained. The core inflation rate, as measured by the PCE price index, is below the Fed’s target of 2% which has enabled the Fed to be patient in adjusting monetary policy. Based on current economic data, we believe the Fed will raise rates in December, but the path of future rate changes will be more gradual and the neutral Fed Funds rate is lower than previously believed. The relatively low Fed Funds rate coupled with the Fed’s elevated holdings of longer-term securities should maintain accommodative financial conditions for the economy.

Downside risks for the outlook are related to shocks that would damage consumer sentiment and reduce risk appetite. If inflationary pressures surprised on the upside and the Fed was forced to adjust rates unexpectedly higher, financial market distress would likely reduce domestic demand. Moreover, commodity shocks or geopolitical uncertainties could weigh on growth. In contrast, a better-than-expected global economic environment would likely generate a positive/upside risk for the U.S.

The outlook for modest growth with low inflation creates both opportunities and challenges for the banking sector. After years of relatively stable, but slow, economic activity, bankers have been successful in building loan demand which has helped improve profit and asset quality metrics. However, the yield curve has flattened during the year and this creates challenges for the banking sector. A flat yield curve pressures a bank’s net interest margin and thus profitability. However, due to improved capital ratios, the banking sector should be well-positioned for the future.

Tim Laughlin is a Director and leads the Wealth Management Division in the Kansas market. Tim partners with his Wealth Management colleagues in the Kansas market to provide pragmatic solutions designed to help clients achieve their financial goals in an optimal way. Tim’s job is to craft and manage investment strategies to ensure the strategy is aligned with the client’s goals, situation and risk tolerance. Tim has over 25 years of banking, trust and investment experience. Tim can be reached at tlaughlin@fnbk.com or 913.266.9357.
Industry Update and Outlook

Wealth Management Industry

By: William B. Greiner, CFA
Chief Investment Strategist, Mariner

The Current Industry Landscape

The wealth management business has been expanding, when measured by assets under management (AUM), over the last number of years. Currently, the Scorpio Partnership estimates that wealth managers manage a total of $19.6 trillion of assets for high-net-worth clients globally. It is interesting to note that $15.5 trillion (80 percent market share) is being managed by the 200 largest private managers around the world.

It has been estimated that wealth managers’ AUM contracted by 1 percent in 2015, partially driven by low investment returns from both global stock and bond markets. The slight contraction is probably centered in foreign investors hands, as household net worth in the United States rose by 2.4 percent for the year ending March 31, 2016. Speaking of which, it is interesting to note that household net worth has been rising in the United States by a strong 6.8 percent annual rate, since 1950 (from $1.56 trillion to $88.09 trillion). This is the raw “stuff” of growth in the wealth management industry.

Wealth advisors are naturally an optimistic group. They have to be. The outlook for the industry in 2016 has been positive, with most participants believing returns the public capital markets provide will be positive. This positive bias continues as more than 60 percent of those recently polled consider themselves bullish in their views toward asset returns in general.

That being said, public markets are offering minimal “safe” returns. More than 50 percent of sovereign bonds being offered in today’s marketplace are yielding less than country-specific inflation. Indeed, up to 35 percent of the world’s government-backed bonds are now yielding negative returns. Perhaps Karl Marx was right – capital has no value!

It probably goes unsaid that I, and the capitalist world, do not support Karl Marx’s concept. So, the search for reasonable returns with a manageable level of risk continues. That search has never been more difficult than it is today, as “base” or “risk free” returns are currently minimal. But, if the search for the proper risk/return customized mix for investors was easy, investors wouldn’t hire wealth managers for their advice.

A Penny Saved is a Penny Earned

Per the advice of Benjamin Franklin, wealth advisors tend to be focused today on issues which they can control with their clients. These factors include:

- **Investment management fees.** Growth in index or passive investment alternatives continues. While an investor cannot control their returns in various public markets, they can control the fees which they pay. Index ETF’s and mutual funds have gathered serious capital over the last number of years...I suspect that trend will continue.
The tax man cometh. Tax rates are uncontrollable, but an investor's exposure to those tax rates can be controlled in most cases. Upwards of 40 percent of an investor's total return can vanish due to levied taxes. Wealth advisors know this, and attempt to bring value to clients through the structure of portfolios and trading activities. The goals is for investors to keep the returns their capital earns.

Wealth transference. Wealth managers are focused on helping with estate planning procedures and ideas, with taxes not being the sole driver behind recommendations. A generational shift in wealth is, and will be, occurring over the next 20 years as baby boomers pass wealth on to their heirs. Planning is the key which helps drive the fulfillment of family desires.

During a time of low public market returns, reducing “cost” drag be it taxes or fees, has never been so important.

Future Drivers – Demographics and Other Challenges

Customer count within the wealth management industry is driven by many factors, among which demographics is key. The BLS (Bureau of Labor Statistics) estimates that by 2024 the United States will see an increase of 16.98 million additional people above the age of 65, as compared to those in that age bracket in 2014. That represents an addition of 47,000 new 65-year-olds every day over that 10-year period. This obviously represents a tremendous opportunity for the industry as a whole as many of these retirees will need serious financial planning services.

Other issues which are currently being addressed within the industry include:

- **“Robo” advice.** Affecting mainly smaller relationships, it is a technology-based service which helps people decide what asset allocation mix is most appropriate for them to meet their financial needs. “Robo” services tend to be lower in price than fully customized solutions. This type of advice is starting to find its way into the service lineups of larger, traditional wealth management firms. One question firms are attempting to currently answer: Do technology-based allocation solutions empower current wealth teams, replace them, or a little of both?

- **The Department of Labor’s ruling.** The DOL ruled to designate investment advisors as fiduciaries under ERISA. The real fulcrum of this ruling is the criteria for who qualifies, based on what kind of advice they give, how often, for what purpose and for what kind of compensation. There is a higher standard of proof that advisors are acting only in the best interest of their clients as fiduciaries.

- **Younger generation expectations.** Younger investors, while typically less wealthy than older generations, will eventually inherit wealth and also create their own wealth. It is estimated that Gen-Xers and Millennials, who currently control about 20 percent of the nation’s wealth, will control 50 percent of the nation’s wealth in 15 years. Younger people have a different expectation set as to what they may be seeking when hiring a wealth advisor. They typically wish to engage in new methods – communication through both digital and human-based mediums. Socially-conscious investment alternatives tend to be more sought after by this age group than others.

- **Holistic advice.** Traditional Wealth Management clients will look for further holistic offerings from firms, including advice on achieving various life goals like healthcare, relocation, education and leisure alternatives.

It is an exciting time to be involved in the wealth management industry. Change is happening rapidly. At Mariner, we embrace this change and look forward to a strong future with our clients.
Construction Industry Outlook

By Pat McCown, CEO, and Nancy Whitworth, VP, Human Resources

Construction Growth is Positive, Although Not Spectacular

Overall
The overall construction outlook for the Kansas City metropolitan area looks positive, with somewhat steady but not spectacular growth over the next five years. From 2016-2020, the industry is expected to experience an average annual growth rate of 6.1% for the combined categories of residential, non-residential buildings, and non-building structures. Of the three major categories, non-residential buildings will enjoy the strongest average annual growth rate of 7.4%, followed by residential buildings at 5.7%, and non-building structures at a lower rate of 4.5%. The Kansas City forecasted average annual growth rate is higher than the national average of 3.7%. It seems the diverse mix of business and industry has led to a certain amount of resiliency in our local market, and provides a solid foundation for continued steady growth.

Non-Residential Buildings Will Enjoy Moderate Growth
The non-residential buildings market (commonly known as the commercial construction market) makes up about 46% of construction dollars in the Kansas City metropolitan area, with a projected spend forecast of $14.31 billion from 2016-2020. The diversity of markets in Kansas City continues to bode well for its future, including education, office, manufacturing, commercial, healthcare, transportation, lodging, communications, amusement/recreation, public safety, and religious. No single market sector accounts for more than 20% of the total; however, education and office combined are one-third of the expected spend from 2016-2020.

Every market sector can be expected to grow, ranging from 1.5%-10.9% average annual growth from 2016-2020. Office and Healthcare can expect above-average annual growth rates of 10.9% and 10% respectively, followed closely by Commercial at 9.0%. Lodging and Manufacturing continue to enjoy steady growth at 7.8% each. For the most part, sectors have been on a good path to recovery over the past three-to-four years from the recession low point and will continue on that trajectory, with the exception of the minor sectors of religious and public safety construction, which remain almost flat.

In summary, the Kansas City area can look forward to a moderate increase in non-residential building construction over the next five years. It seems that economic factors are returning to relative “normalcy” without the extremes of some previous periods. Office construction will be the largest market sector in the area, followed by educational, manufacturing, commercial, and healthcare.

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1 FMI Construction Outlook, 2Q 2016
KC, MO-KS MSA 3Q 2016 forecast based on 2Q 2016 actuals
In Millions of Current Dollars
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PUBLIC POLICY UP CLOSE SPEAKER SERIES
WHAT TO EXPECT WITH THE NEW POTUS AND THE 115TH CONGRESS IN 2017

Just two days following the November 8 elections, former US Congressmen, John Shadegg of Phoenix, AZ and Alan Wheat of Kansas City, MO, now with Polsinelli, will take the stage at this Chamber event to discuss what we can expect when the new Congress and President take office in January and what the lame duck congressional session might accomplish. Is the landscape ripe for a tax overhaul? Will we have a wall? What new committee leaders are emerging? Save the date and plan to attend this important briefing.

THURSDAY, NOVEMBER 10
InterContinental Kansas City at the Plaza Rooftop Ballroom
7:30-9:00 a.m. breakfast and program
PPC members get up to 2 complimentary seats with RSVP
Email Shavon Brown for details, brown@kcchamber.com
Shipping is vital to the everyday life of the average consumer and in the ever changing world of commerce. As technology evolves at rapid rates, the transportation industry must change and adapt as well in order to meet increased demand for faster delivery times. eCommerce continues to grow as more and more people elect to shop online from the comfort of their own home or on mobile devices while they are on-the-go. This trend has led to the need for innovation by companies and shippers to ensure their supply chains are able to meet the time and place expectations of their customers.

2017 should prove to be an interesting year in the realm of transportation as technology continues to play an increasingly critical role in the day-to-day operations of companies all over the world. The Internet of Things (IoT) is on its way to providing the world with more connectivity than ever before, and the effects are being felt in the transportation industry with the increased usage of technologies like RFID tags. The importance of high quality and efficient inventory and communications systems continues to rise as companies seek to optimize supply chains and minimize lead times.

Looking ahead, 2017 has a great chance of being a prosperous year full of growth and innovation that will most likely set a new precedent for speed and quality in the transportation industry. The following sections take a look into the expectations for 2017 in the various modes of transportation in the industry on a national and global scale as well as a specific focus on the Kansas City region.

Global

2016 has proven to be an interesting and eventful year economically, politically, and socially. Geopolitical tensions are high all over the world with a high concentration in the Middle East. The European Union has seen a shake up as the United Kingdom voted to leave the EU. World economies reacted immediately as a result of the uncertainty following the British exit (Brexit).

According to World Economic Outlook, growth in emerging markets slowed for the fifth consecutive year, but still accounts for more than 70 percent of global growth. Meanwhile, advanced economies have continued to modestly recover and financial conditions in those economies remain consistent. Despite political tension and economic uncertainties around the world in 2016, global growth is still projected at 3.6 percent for 2017, a .2 percent increase over the 2016 projection. Emerging markets will play a key role in this growth as they continue to develop higher quality infrastructure and can participate more actively on a global scale.

Global trade has been given a massive opportunity with the opening of the expanded Panama Canal. As vessel size has increased a great deal in recent years and an enormous amount since the Canal opened in 1914, the expanded canal will revolutionize the speed and efficiency with which cargo can be moved from the Atlantic to the Pacific and offer new route options for the larger ships that have previously been unable to use the canal.

The World Trade Organization released a World Trade Outlook Indicator in July 2016 that was at a reading of 99.0, which signifies that the WTOI is slightly below trend and predicts sluggish growth in the coming months. Heading into 2017, the general growth trend can be expected to pick up as a new year often brings renewed optimism. Despite the slowdown in certain areas, the recovery in developed markets as well as the certainty in key emerging markets should bring an uptick in growth in 2017.

One of the greatest challenges faced by shippers is how to optimize last mile delivery. Silicon Valley is thriving as a test market for new last mile delivery techniques that seek to improve the speed with which consumers receive their online orders. According to supplychain247.com, Amazon has been testing same-day delivery service in San Francisco as well as using bike messengers in New York City, specifically in Manhattan. Another last mile delivery trend is the use of independent drivers competing with established courier firms. This follows the explosive popularity of people using services like Uber instead of taxis. As customers demand faster delivery times, shippers are taking a hard look at final delivery strategies and revamping strategies as far upstream as their distribution networks.

According to the U.S. Bureau of Labor Statistics, the U.S. unemployment rate halfway through 2016 was 4.9 percent, down 0.4 percent year over year. Both Kansas and Missouri have unemployment rates below the national average at 3.7
percent and 4.3 percent, respectively. While the national unemployment rate dropped, it has not been as a result of job creation which has been disappointing in 2016. Many people dropped out of the labor force because they chose to stop looking for work. Until June 2016, many were sure the Fed would raise interest rates because of generally positive job reports until a dismal 38,000 jobs were created in May 2016. However, the New York Times reported that worries were put at ease when jobs roared back in June with a gain of 287,000. The gains were widespread across sectors, although a significant portion were service related jobs. While there have been ups and downs during 2016 and a with new president to be inaugurated in 2017, the U.S. should be in store for continued job growth and economic recovery as most have agreed that there have been improvements since the 2008 crisis.

**Kansas City Region**

The Kansas City region has decidedly put itself on the map as a transportation and logistics hub for North America, and continues to see development that will allow it to sustain that distinction. Four major modes of transportation support the region in the form of four major interstate highways, five first class railways, an international airport, and a port on the Missouri River that is beginning to see investment for revitalization and growth.

Kansas City’s transportation advantage is a result of its access to this variety of transportation options as well as its geographic location. Kansas City is home to the largest rail center in the United States by tonnage positioned at the crossroads of four major national highways (I-29, I-35, I-49, and I-70). Early discussions are taking place around the development of Kansas City International Airport stages that could increase the amount of air cargo that passes through Kansas City.

Woodswether Terminal at the Port of Kansas City on the Missouri River reopened in August 2015 and has had a stellar 2016 thus far. Currently perceived as an unreliable form of transportation, the Port of Kansas City has been working to change this mindset and increase the usage of the river. Port KC has stated that advantages such as environmental friendliness, lower cost than land shipping, and alleviation of traffic on rail lines and highways are just a few of the major ways that the Port can serve the region. Increased usage of the river and Port could lead to job creation and private investment in the coming years as well.

The advantages of Kansas City as a transportation hub give the region an extremely positive outlook for 2017 and the real estate market in the region has proven that Kansas City will continue to grow in the next year and beyond. In the past five years, the KC region has seen an average of 4 million sq. ft. of speculative space added annually with more than 5.8 million sq. ft. of industrial speculative space added in 2015. Additionally, there is currently 6.3 million sq. ft. of speculative space currently under construction. The Kansas City region is poised to be a national leader as a transportation hub in 2017 and for many years to come.

Amazon announced in July that it will open a third fulfillment center in the Kansas City Region with a new 855,000 sq. ft. building in Kansas City, Kansas and bring over 1,000 new jobs to the area. The footprint of the building is only part of the story as Amazon has plans calling for 2.3 million sq. ft. of usable space. Amazon is dominating traditional retailers in the ECommerce market. According to Fortune, Amazon has digital sales of $71,844,000,000. At second place, Wal-Mart is a seemingly insurmountable distance back at $13,188,000,000. Amazon has demonstrated through its investment in the region that it sees the value of locating its fulfillment centers in a region that can reach 85 percent of the United States in two days or less. According to a 2016 Q2 Market Report from Newmark Grubb Zimmer, Kansas City has an industrial vacancy rate of 6.3 percent which was an increase due to deliveries of 1.3 million of sq. ft. during the quarter. Kansas City has a great deal of activity currently in development for industrial real estate and is positioning itself to be an elite region in the transportation industry.

Generally, the transportation industry should continue to see growth in 2017. The U.S. economy is continuing to recover and add jobs. The inauguration of a new president could change the direction that the world is moving in entirely. Transportation is always necessary in commerce, so while the market may change, the industry will find a way to be successful. The Supply Chain industry is on the rise and the number of jobs in logistics is swelling. By and large, 2017 should continue trucking onward and upward.