

## Market Power?

BY DOUG CAMPBELL

“Can Feedback from the Jumbo CD Market Improve Bank Surveillance?” R. Alton Gilbert, Andrew P. Meyer, and Mark D. Vaughan, Federal Reserve Bank of Richmond *Economic Quarterly*, Spring 2006, vol. 92, no. 2, pp. 135-175.

Bank examiners spend a lot of time on the road. They drive around the country dropping in on financial institutions of all sizes, meeting with managers and inspecting the books. It's an expensive way to mind the banks, but necessary.

The other way that bank examiners keep tabs is through a model which summarizes a depository institution's financial condition. It's useful so far as it goes, but in recent years economists have been considering whether there might be other, more effective ways of supervising banks that complement on-site visits.

One of the leading candidates for how this might be accomplished is through financial market information — everything from stock prices to bond yields. Under one proposal, large banks would have to issue a special debt offering, with the idea that the market performance of this debt issue would flag problem banks perhaps sooner than traditional bank surveillance techniques.

In a new paper, economists in the supervisory units of the Richmond and St. Louis Feds size up the surveillance properties of jumbo certificates of deposit (CDs). Jumbo CDs are a cheap and stable source of funding for banks, and supply ample data to mine. Equally, jumbo CDs are used by even the smallest banks, which are the sort historically most likely to fail and the ones that experience the widest time lags between on-site examinations.

The authors build a model that aims to mimic surveillance practices used by bank supervisors. Then they compare how jumbo CD signals fare as a predictor of bank problems with the standard capital-adequacy model.

It turns out jumbo CDs aren't so good at providing early warnings about problem banks. Even though it costs almost nothing to add jumbo CDs to a model of bank surveillance, doing so produces little in the way of valuable information.

It may be that the jumbo CD results were less than fruitful because they were produced through a model that tracked the healthy economic period of 1992 to 2005. This could mean that other market data could produce meaningful information for different time periods. At the same time, the findings on jumbo CDs suggest that no single source of market information can replace existing bank monitoring techniques. The authors conclude, “Our findings — when viewed with other recent research — suggest the supervisory return from reliance on a single market signal through all states of the world may have been overestimated.”

“A Leaner, More Skilled U.S. Manufacturing Workforce.” Richard Deitz and James Orr, Federal Reserve Bank of New York, *Current Issues in Economics and Finance*, February/March 2006, vol. 12, no. 2.

The U.S. manufacturing sector continues to shed jobs, but a growing number of the remaining ones require relatively high skills and, as such, they come with higher pay.

Manufacturing employment fell 9.3 percent in the United States between 1983 and 2002. But economists at the New York Fed found that during the same period, the percent of high-skill manufacturing jobs rose 36.6 percent. Among the biggest-gaining regions in this regard was the South Atlantic (which includes the entire Fifth District); it saw a 63.4 percent gain in high-skill manufacturing jobs, countering the region's overall 8.8 percent loss of manufacturing positions.

These results are in keeping with economic theory. Global trade has combined with technological advances to lower demand for the least-skilled U.S. workers, whose jobs can be done cheaper by workers overseas or by machines. Meanwhile, high-skill jobs are being created in engineering research and development, and export industries. As a result, the authors conclude, “a manufacturing workforce is emerging that is at once leaner and more skilled.”

“The Decline in Teen Labor Force Participation.” Daniel Aaronson, Kyung-Hong Park, and Daniel Sullivan, Federal Reserve Bank of Chicago *Economic Perspectives*, 1Q 2006, pp. 2-18.

In the late 1970s, the labor force participation rate of working-age teenagers (16 to 19 years old) peaked at about 59 percent. It's been downhill almost ever since, including a steep 7.5 percentage point fall between 2000 and 2003. Are teens hanging out the mall and playing video games, or are they devoting themselves to their studies as never before?

The answer may be important for the economy and its future productivity. Investments in human capital — be they in the labor market or in schooling — ought to increase teens' future earning power. The authors find that the long-term decline in teen labor force participation is “a supply-side development,” triggered principally by “the significant increase in the rewards from formal education.”

There remains a possibility that demand has also dropped for teen labor, but the authors note that the recession ended four years ago and labor force participation among 16- to 19-year-olds still hasn't picked up. More to the point, today's teens simply aren't looking for jobs. They appear to be hitting the books instead. **RF**