

Economic Outlook for the U.S. and Wisconsin 2006

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Top 10 Business Stories of 2005

(AP survey of newspaper editors)

10. New bankruptcy law
9. U.S. economic growth continues
8. Corporate fraud trials
7. New Fed Chairman/end of Greenspan era
6. Housing market starts to cool
5. Pension problems
4. Airline woes
3. GM/Ford domestic auto problems

Top 10 Business Stories of 2005

2. Katrina and the clean-up

1. **ENERGY PRICES**

Oil closed 2005 @\$61 barrel up 40% over the year.

Natural Gas ended @ \$11.33/mbtu up over 80% over the year.

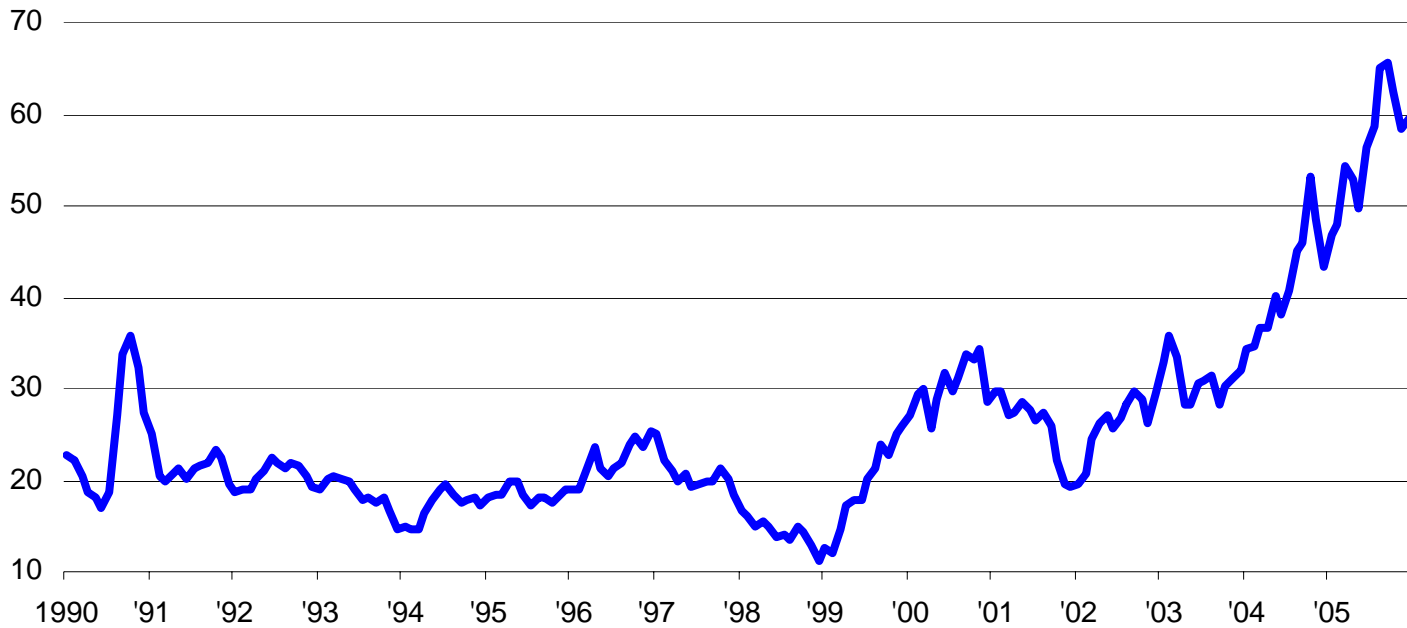
Preview of 2006

- If you liked 2005, there are a lot of similarities
 - Risks
 - energy—best case, relatively high but less volatile prices. Worse case, super spikes
 - Domestic autos and the Midwest
 - Housing slowdown
 - The inverted yield curve
- Evidence.....

Oil prices have been rising for the past four years

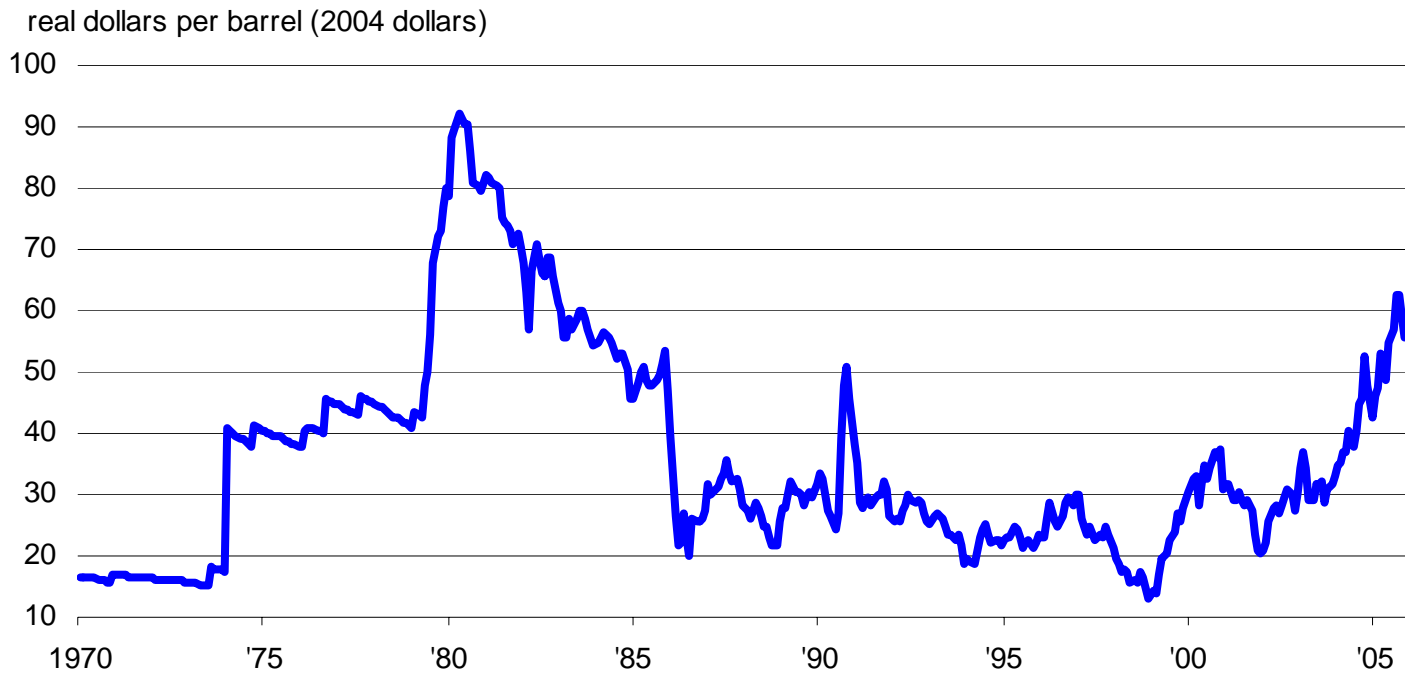
West Texas Intermediate oil price

dollars per barrel



**Adjusted for inflation -
current oil prices are below early 1980s prices and just above the peak
that occurred during the
Iraq invasion of Kuwait in 1990**

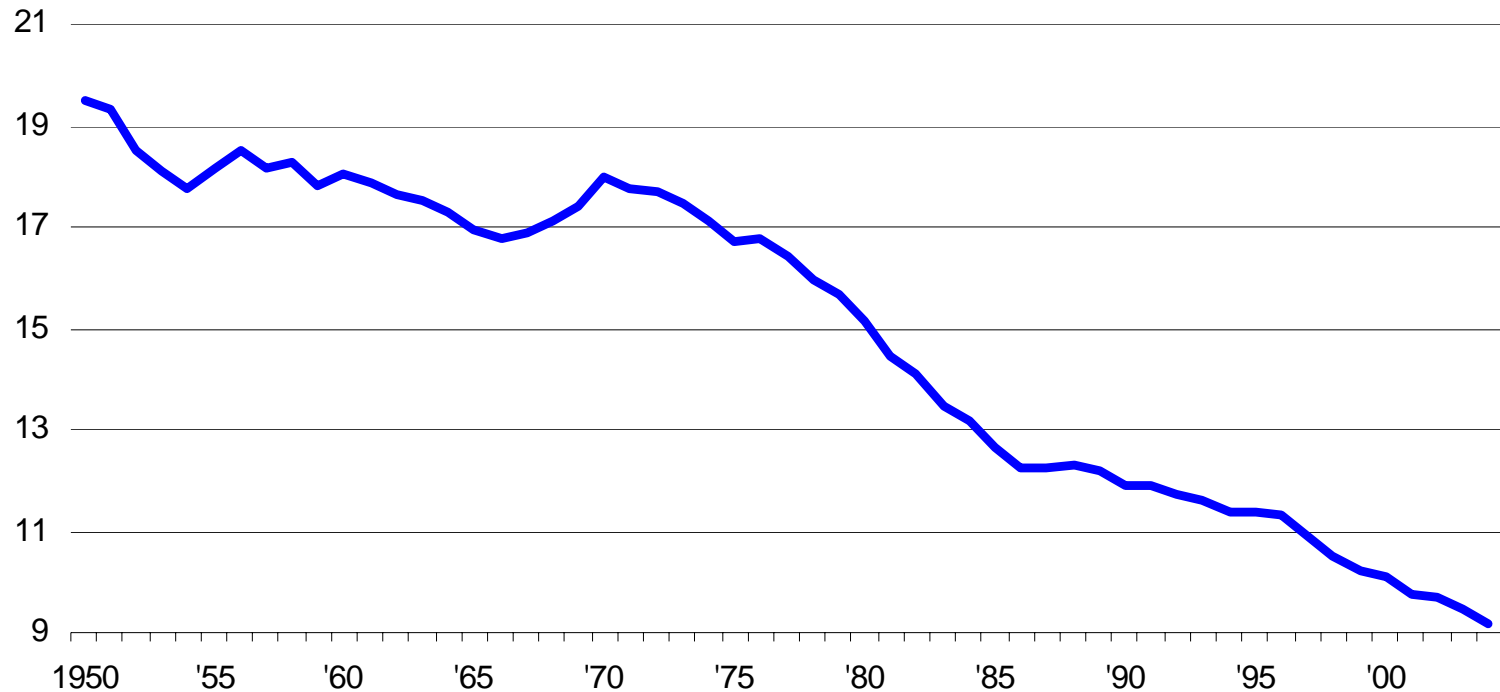
Real West Texas Intermediate oil price



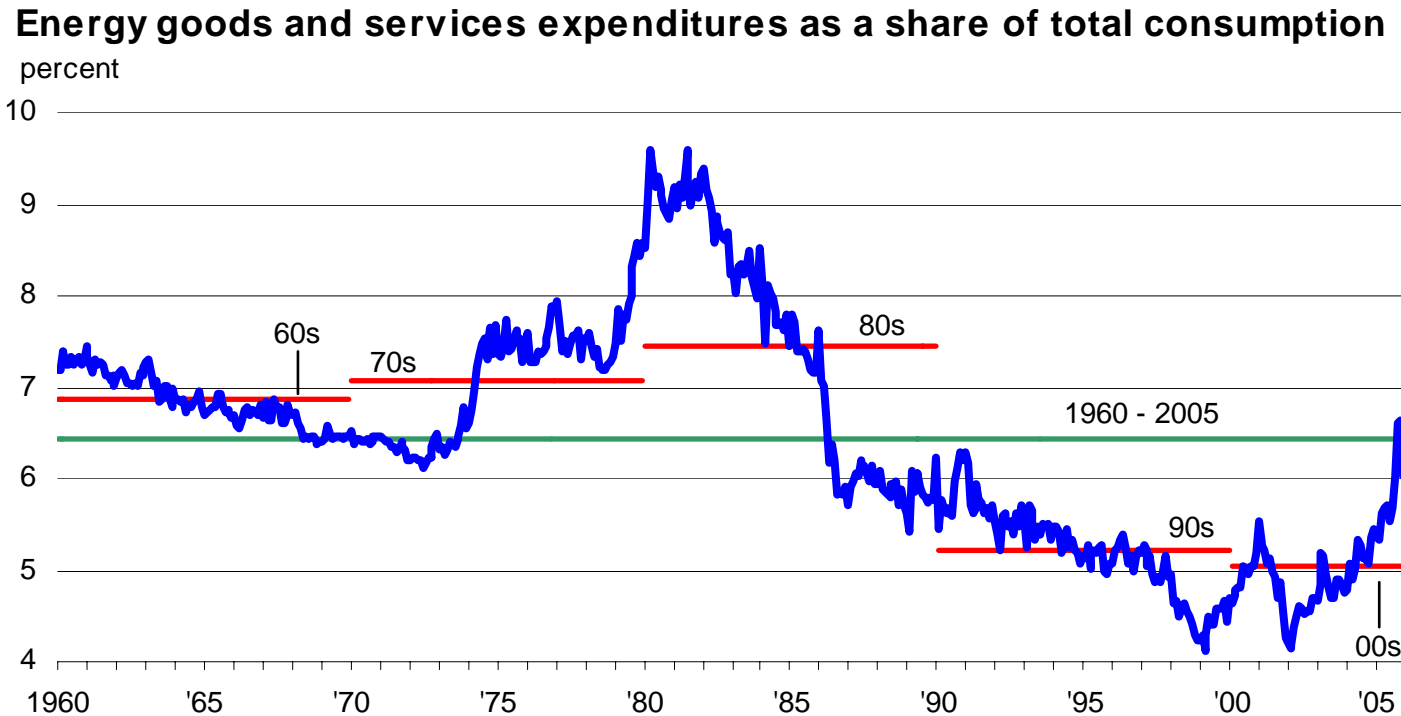
The United States has become more efficient in the use of energy over the past 50 years

Energy consumption per dollar of GDP

Thousand Btu per chained (2000) dollar



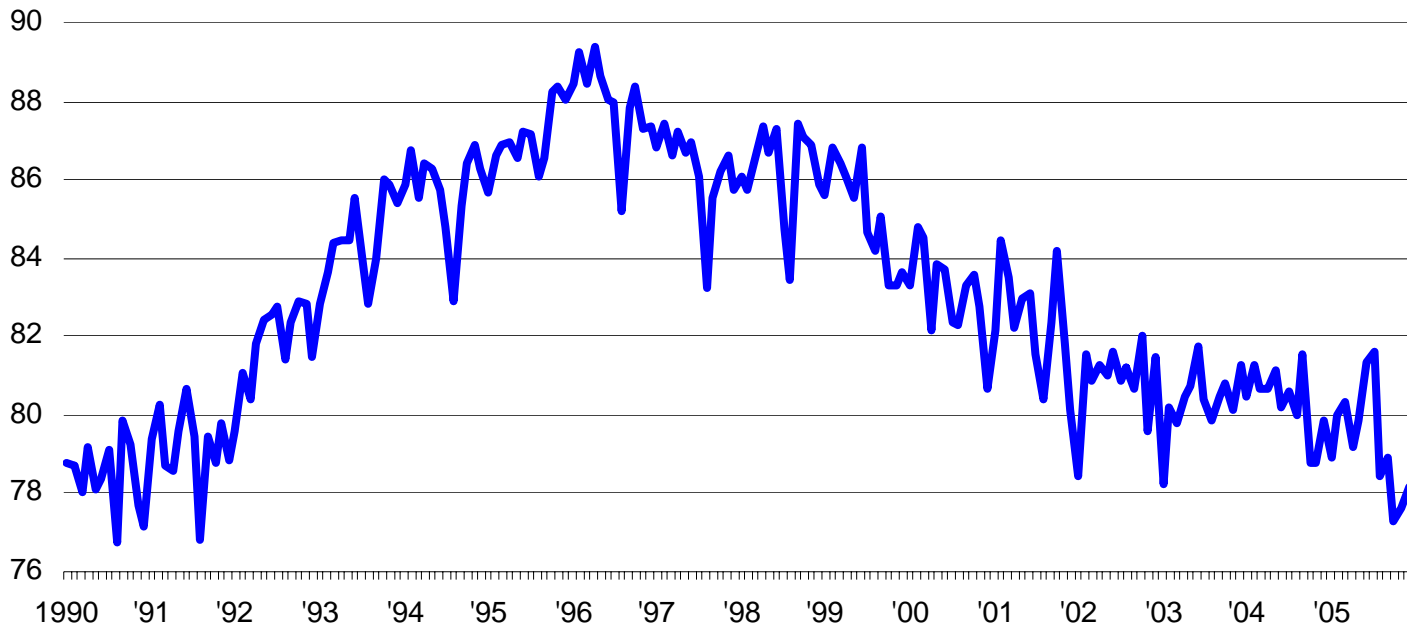
Expenditures on energy increased over the past few years, however they remain just slightly above historical rates



The decline in domestic light vehicle production share

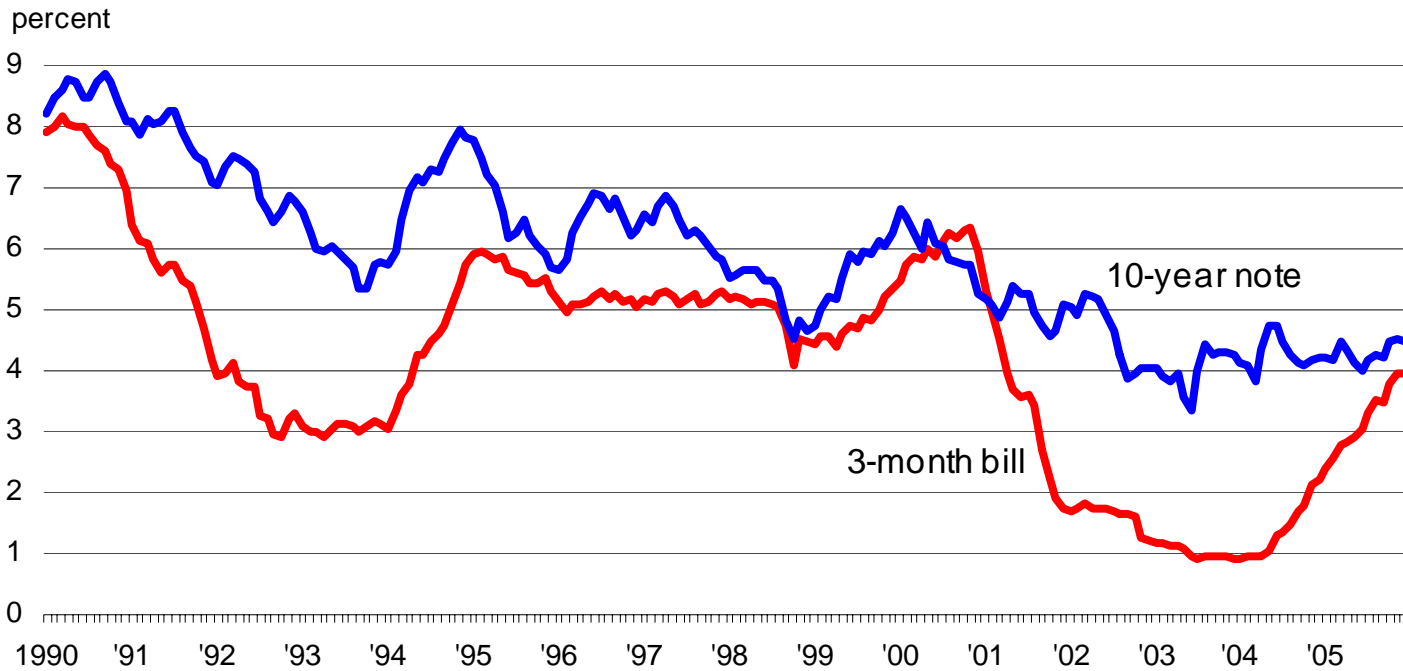
Domestic production share of light vehicles

percent



While short term Treasury yields have risen, longer maturity notes have not

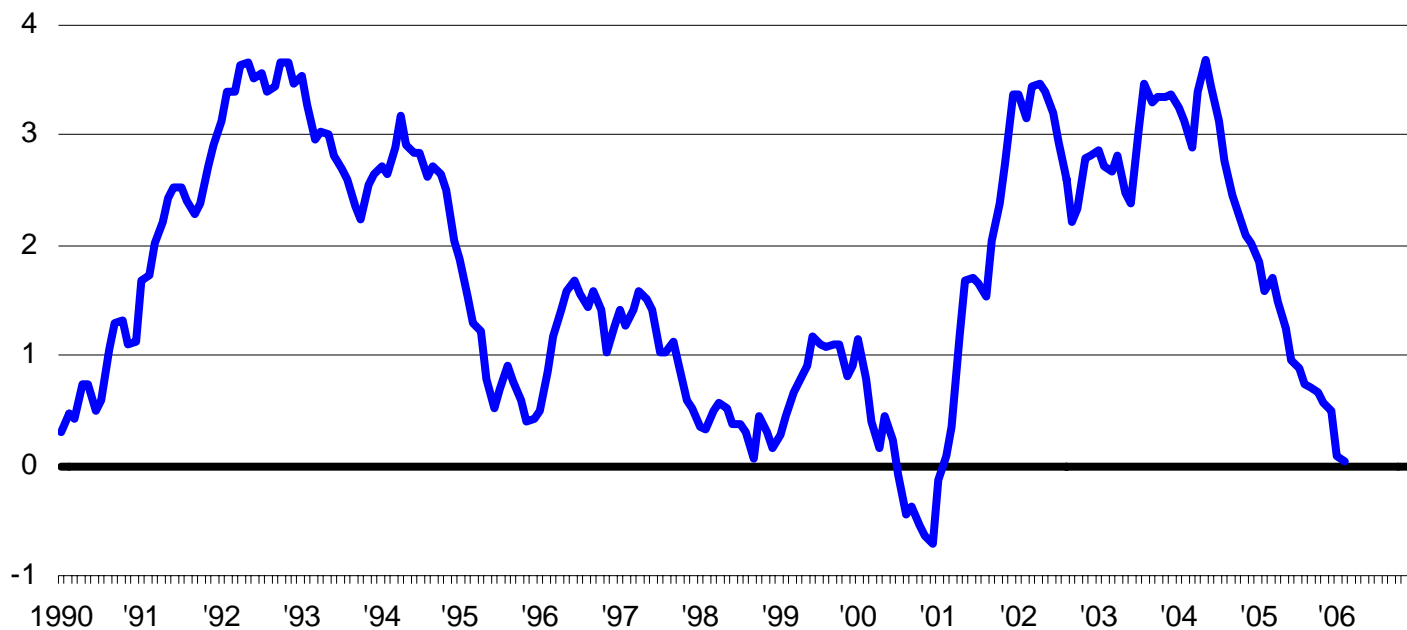
Treasury yields



The yield curve is flat

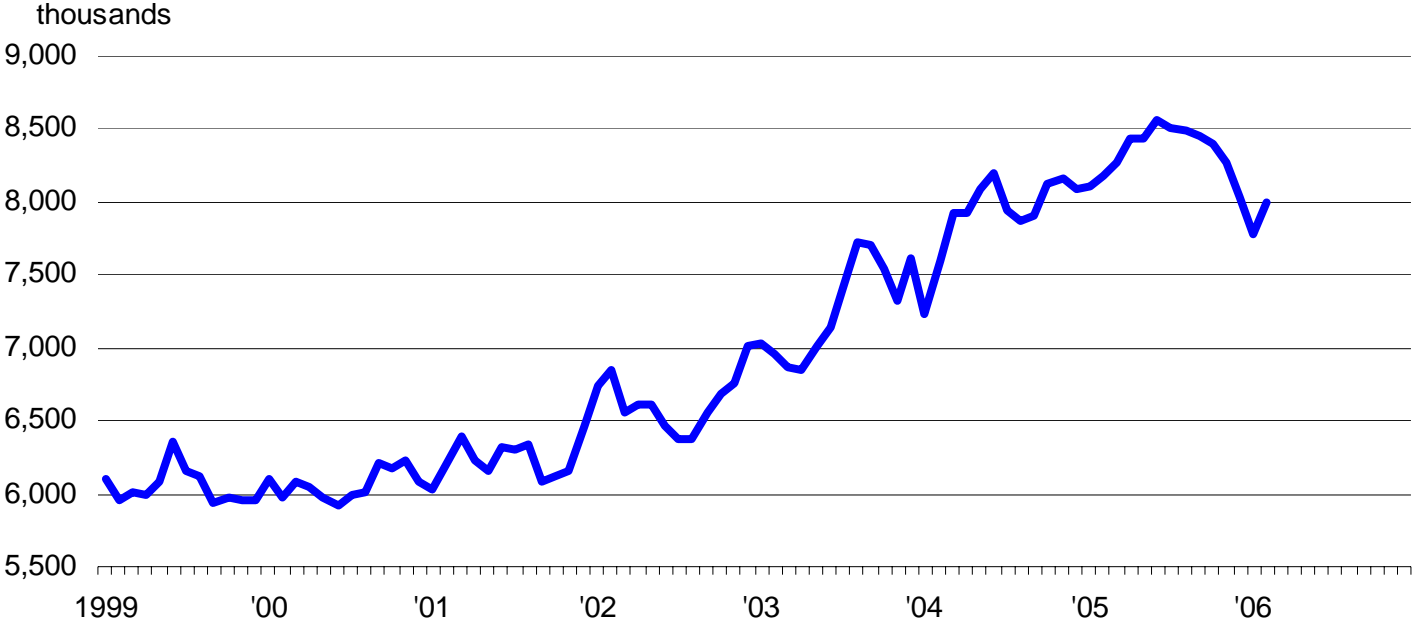
Yield curve - 10-year Treasury note yield minus 3-month Treasury bill yield

percent



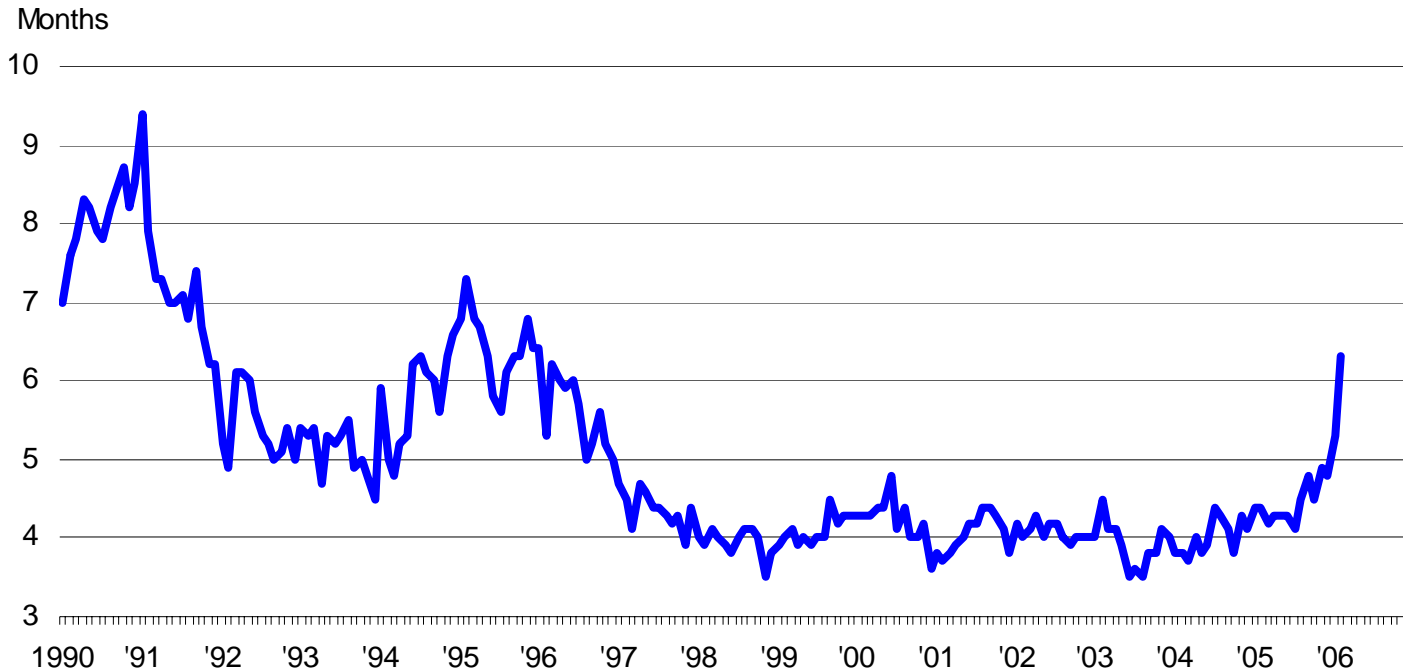
Home sales have been falling

New and existing home sales



The months supply of single family homes has been rising

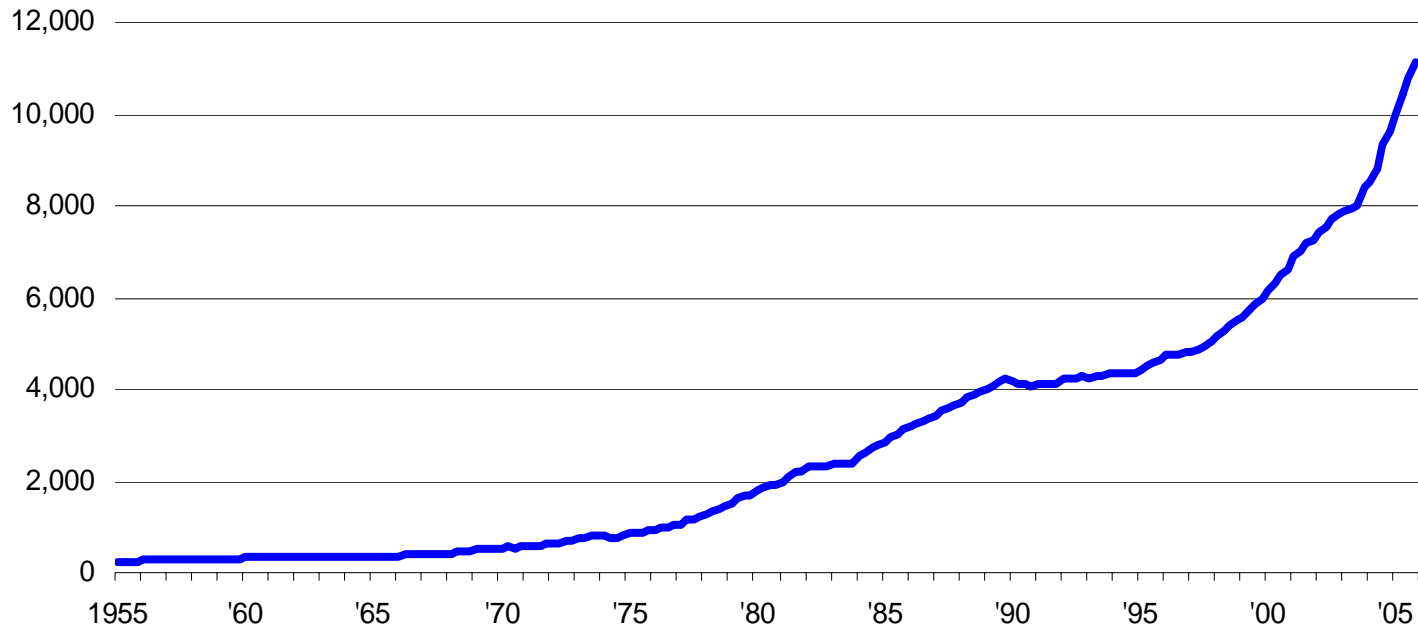
Months supply of new single family homes



However, there has been an impressive rise in real estate equity over the past ten years

Households equity in real estate

Billions of dollars



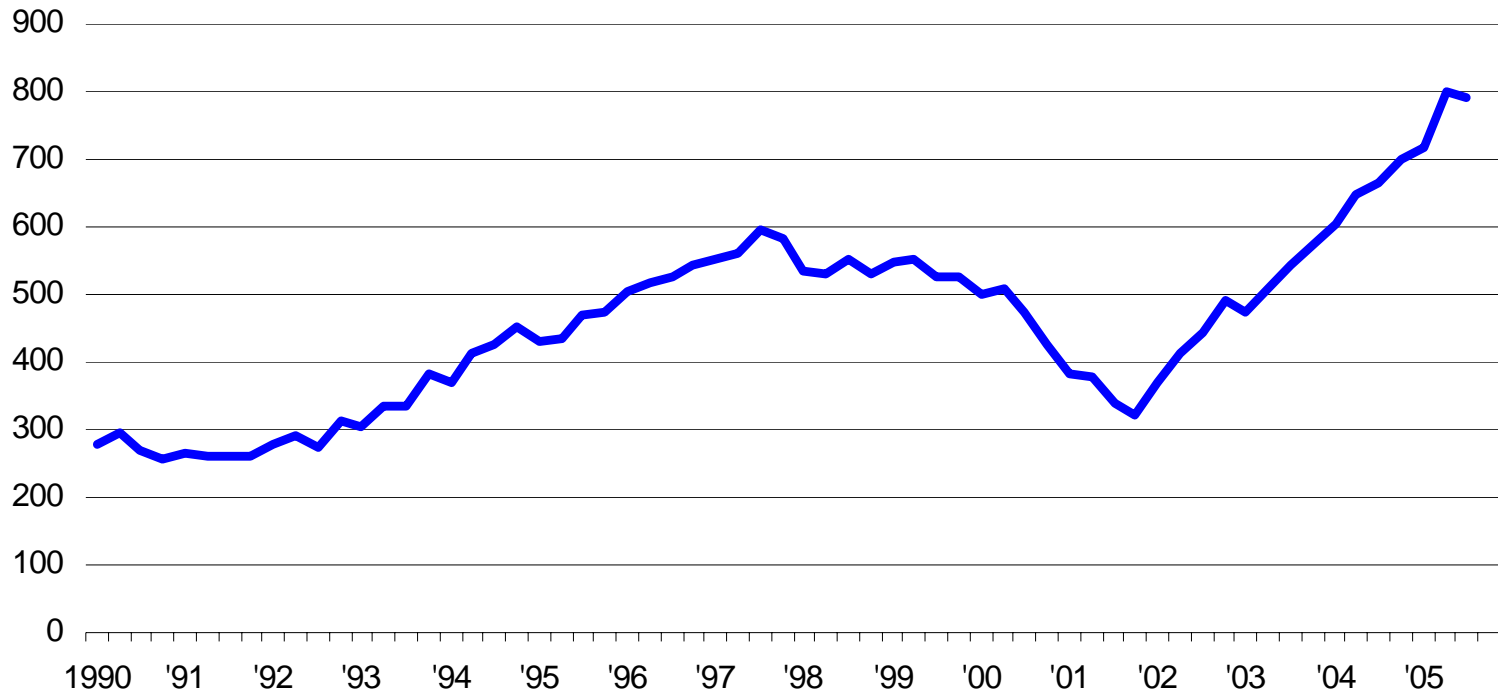
Preview of 2006 continued

- Pros
 - Business spending picks up the slack, companies are sitting on piles of cash
 - Manufacturing (ex. Domestic autos) are seeing good times. Manufacturing output is at a record
 - Productivity numbers are good
 - Neutral monetary policy

Corporate profits are at a record level and have been rising since the fourth quarter of 2001

Nonfinancial corporate profits

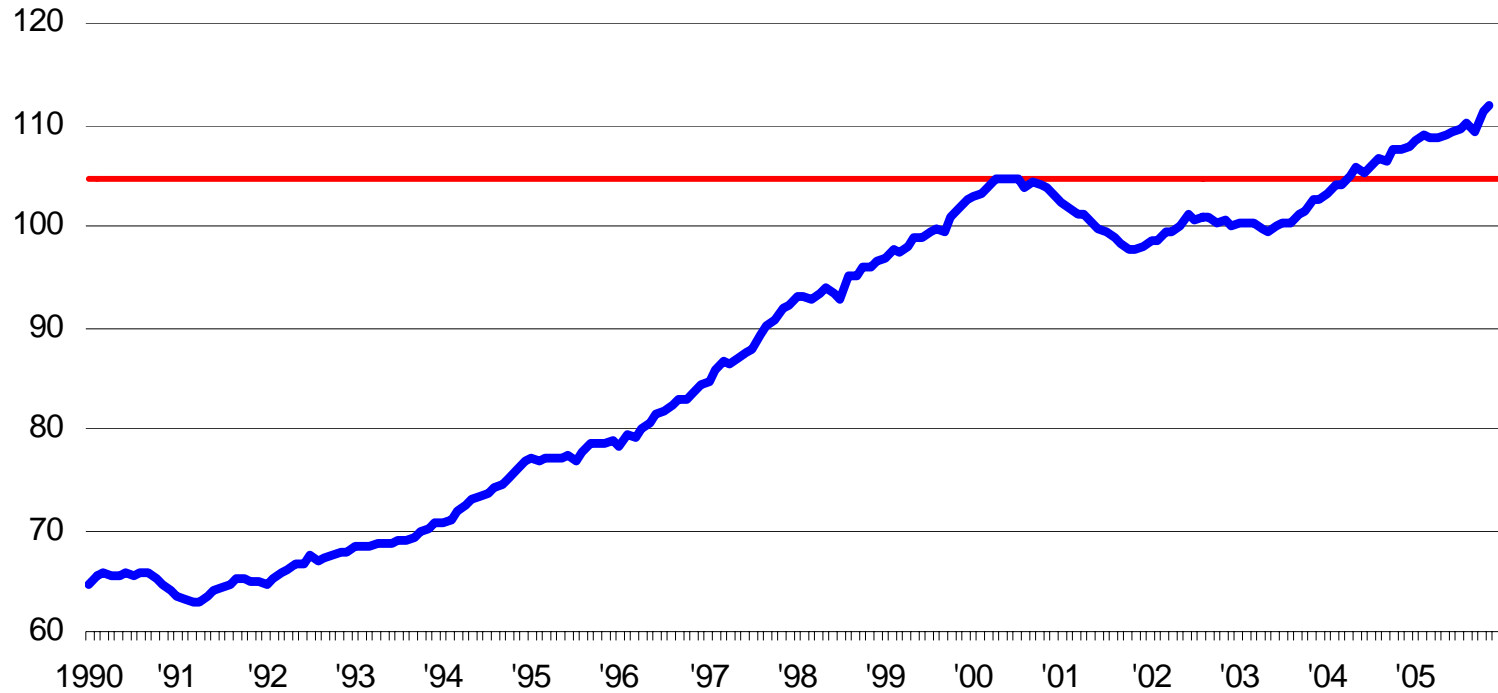
Billions of dollars



Manufacturing output in the United States has never been higher

Industrial production - manufacturing

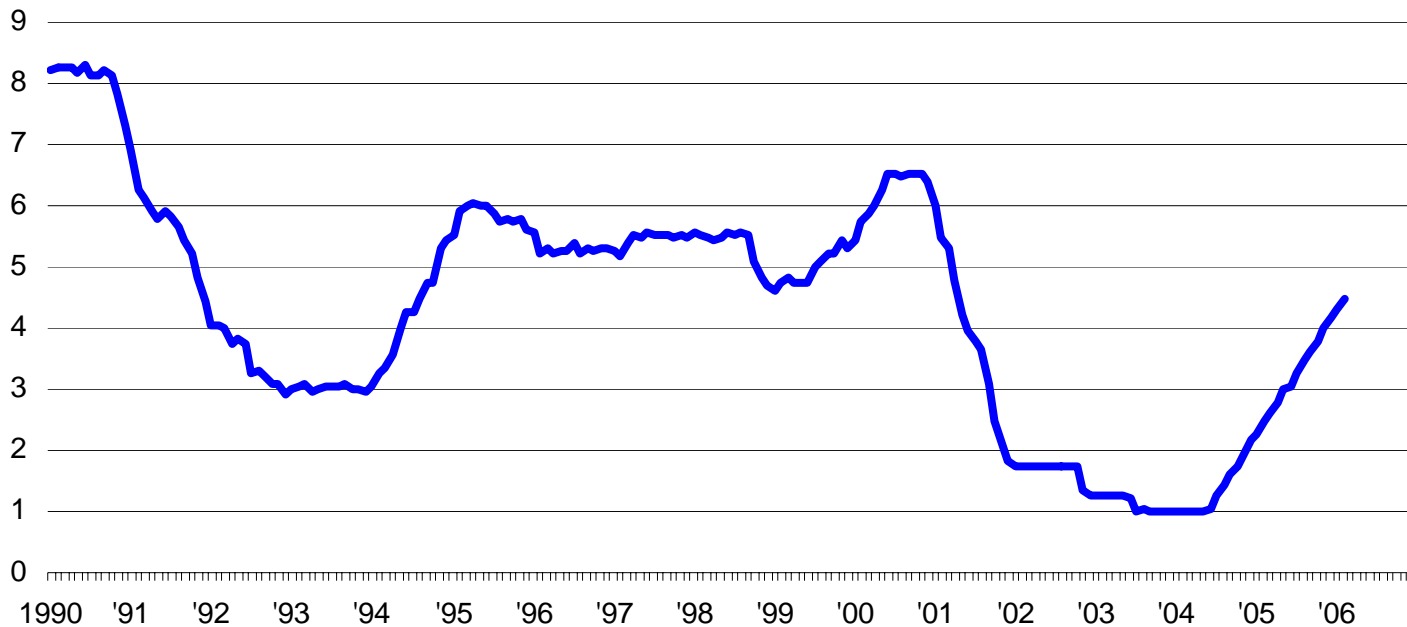
Index 1997=100



The Fed has raised interest rates by 375 basis points (4.75%) and longer-term inflation expectations remain contained

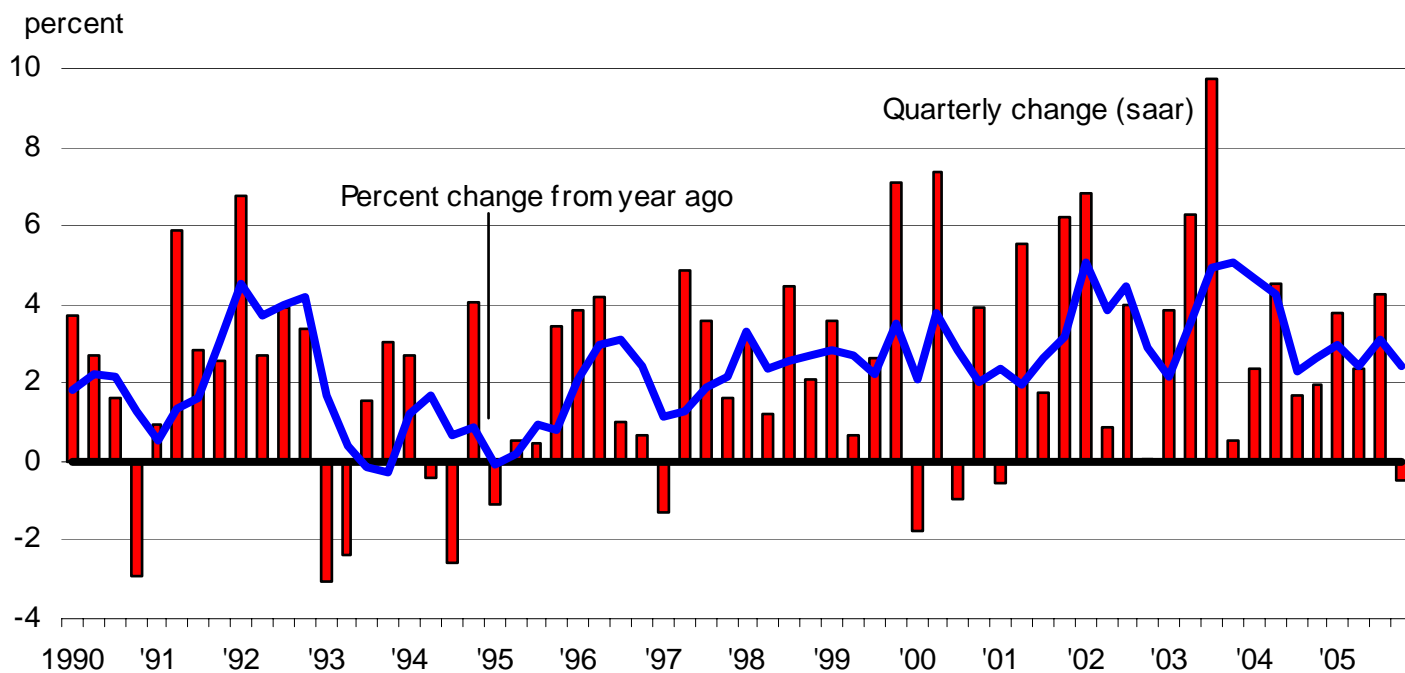
Fed Funds rate

percent



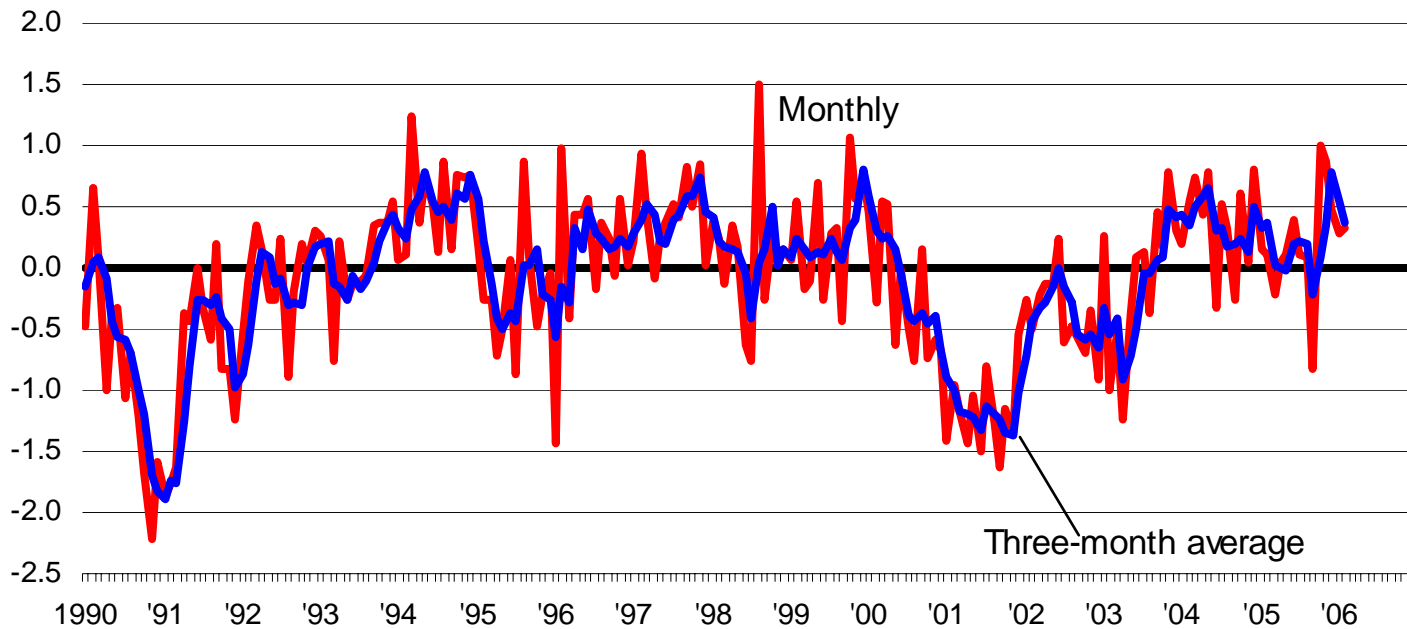
Productivity growth has been steady over the past year

Nonfarm business productivity



The three-month average of the Chicago Fed National Activity Index eased in February to 0.36

Chicago Fed National Activity Index



Look at the numbers

(results from 2006 Chicago Fed Economic Outlook Symposium)

| | 2004 actual | 2005 estimate | 2006 projected |
|------------------------------|-------------|---------------|----------------|
| Real GDP (chained) | 3.8% | 3.6% | 3.2% |
| GDP price index | 2.9% | 2.8% | 2.6% |
| Personal consumption | 3.8% | 3.1% | 3.0% |
| Business fixed investment | 10.9% | 7.0% | 6.4% |
| Net exports | -\$634.1b | -\$629.8b | -\$620.3 |
| Industrial production | 4.3% | 2.4% | 3.2% |

Forecast continued

| | 2004 actual | 2005 estimate | 2006 projected |
|----------------------------|----------------|-----------------|-------------------------------|
| Car/light truck sales | 16.9m | 17.0m | 16.8m |
| Housing starts | 1.95m | 2.04m | 1.9m |
| Unemployment rate | 5.4% | 5.1% | 5.0% |
| Crude oil | \$48.31bbl | \$61.21bbl | \$55.69bbl |
| Treasury constant maturity | 2.47% 4.17% | 4.18%/ 4.60% | 4.70%/ 5.11% |

Bottom line

- A good not spectacular year that will look and feel like 2005.
- Still probably more downside than upside risks
- Real key will be if business spending is able to balance (possibly lower) consumer demand

On Wisconsin

- Outlook is quite sanguine
- Relative to much of the Midwest, Wisconsin will show steady, if not exciting economic growth
- Manufacturing and paper are relative strength, particularly with appreciation of the Canadian dollar
- Madison continues to attract high tech business and ranks high on quality of life index
- Milwaukee's future seems more closely tied to Chicago and that might be a good thing
- Decline of domestic autos is hurting the state less

Down Wisconsin

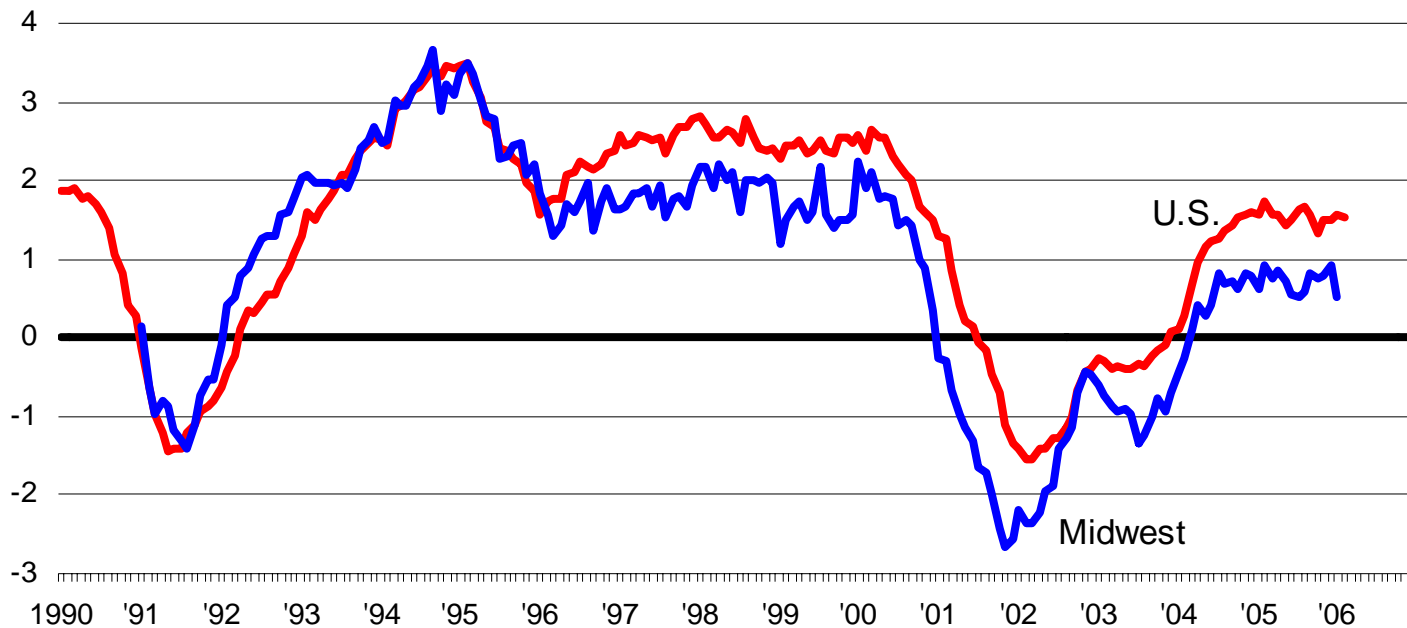
Long-term issues

1. Demographics aren't great
2. Skill mix is an issue (brain drain)
3. Continued perception of Wisconsin as a high cost state
4. Minnesota as a rival
5. Ultimately the issue is the same throughout the Midwest—Can a region grow prosperous without growing big? Suggests that productivity growth is the key to the future
6. What is the role/future of higher education?

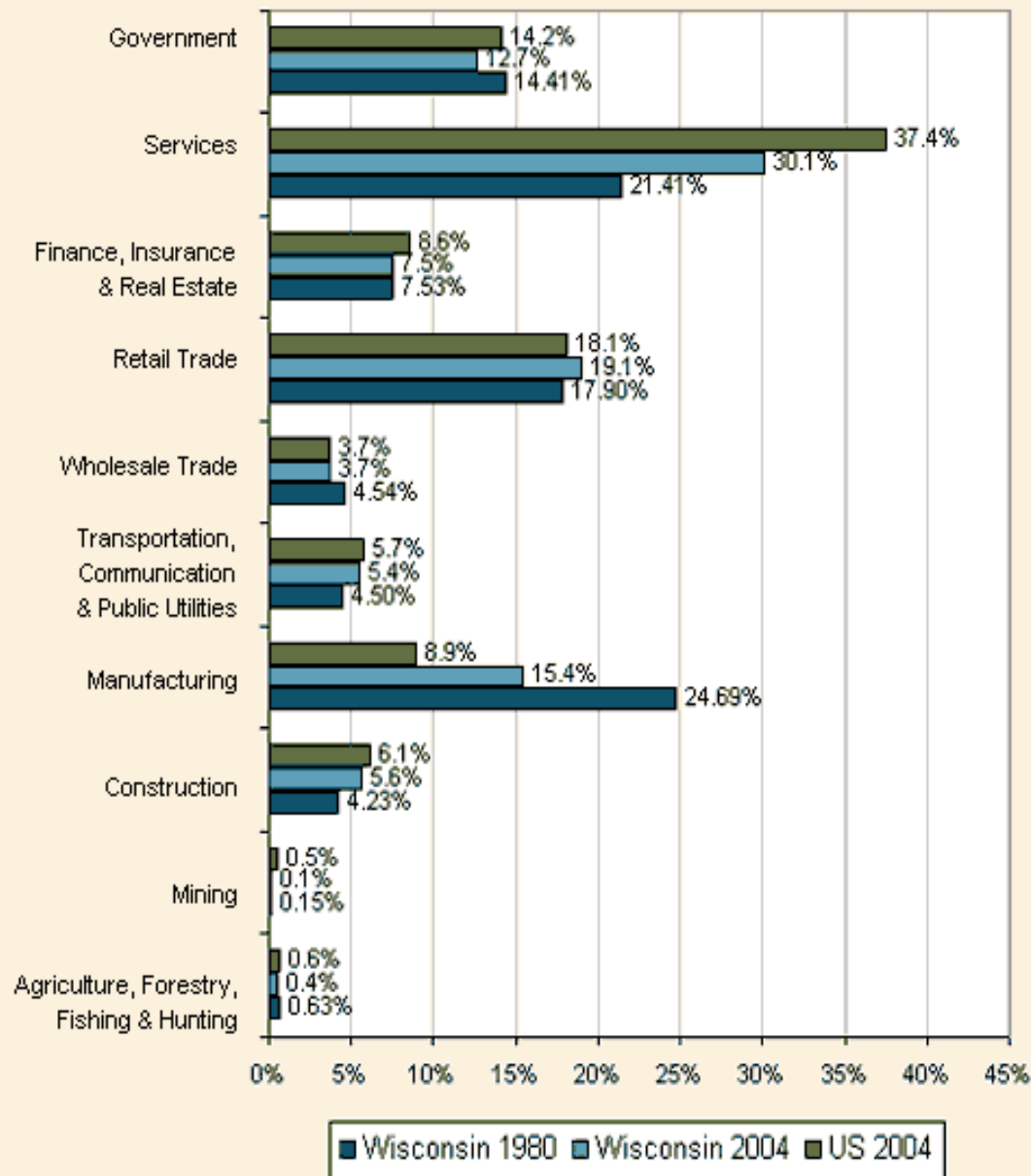
Regional employment growth has been flat for the past year and underperforming national employment growth for nearly ten years

Total employment

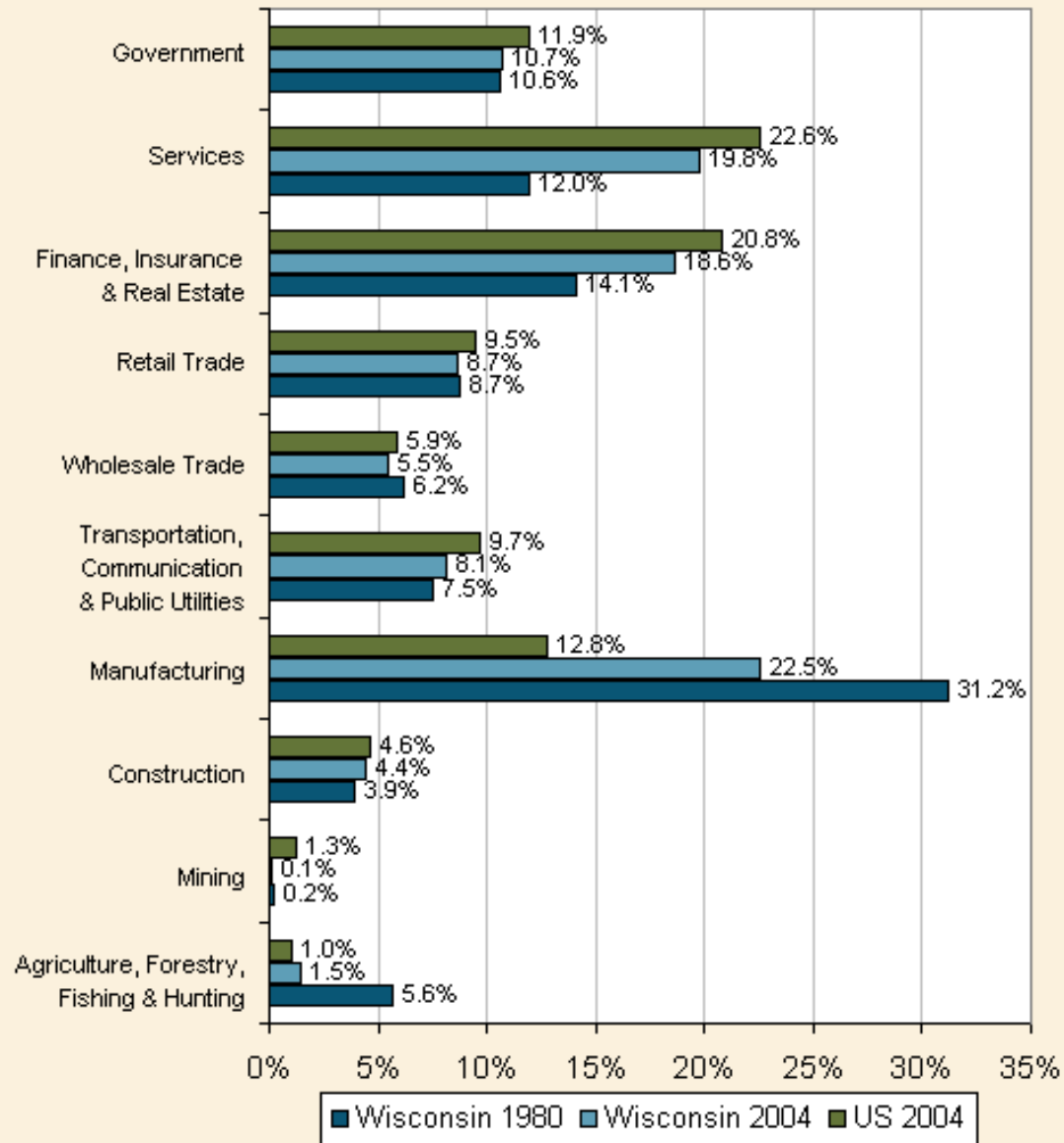
percent change from year ago



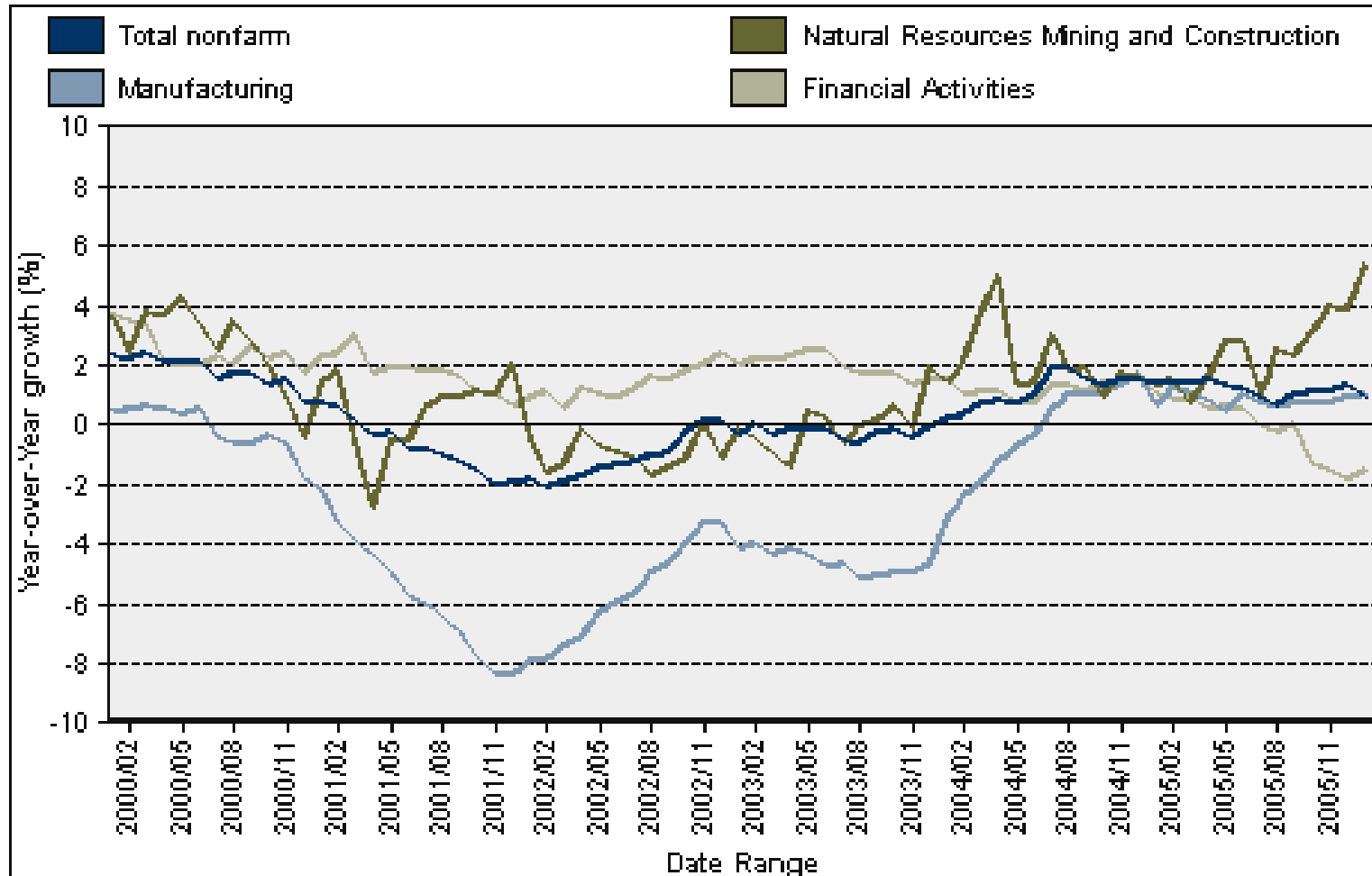
Wisconsin: Percent of Total Nonfarm Employment by Industry and Comparison to the US



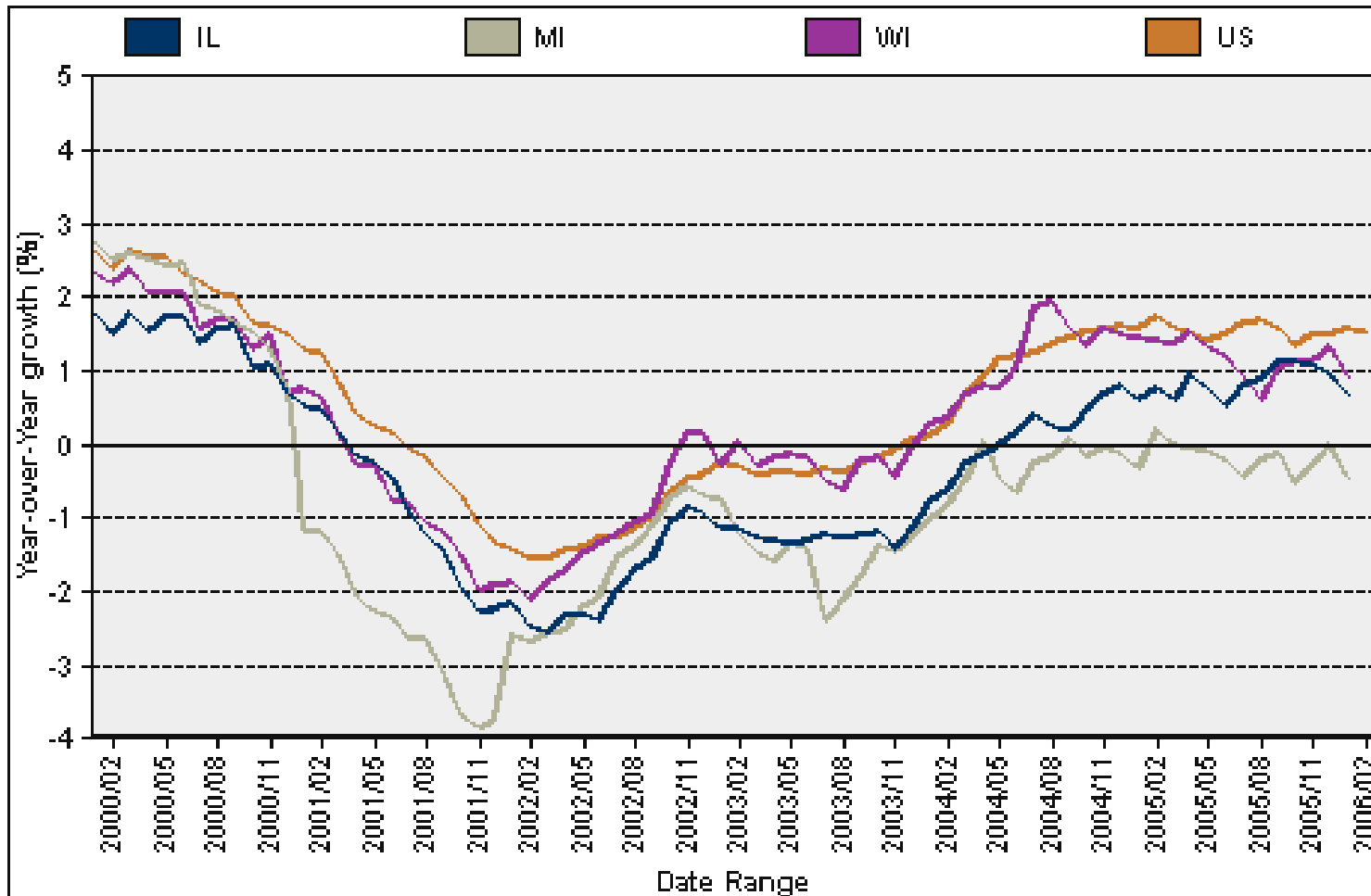
Wisconsin: Percent of Total Gross State Product by Industry and Comparison to the US



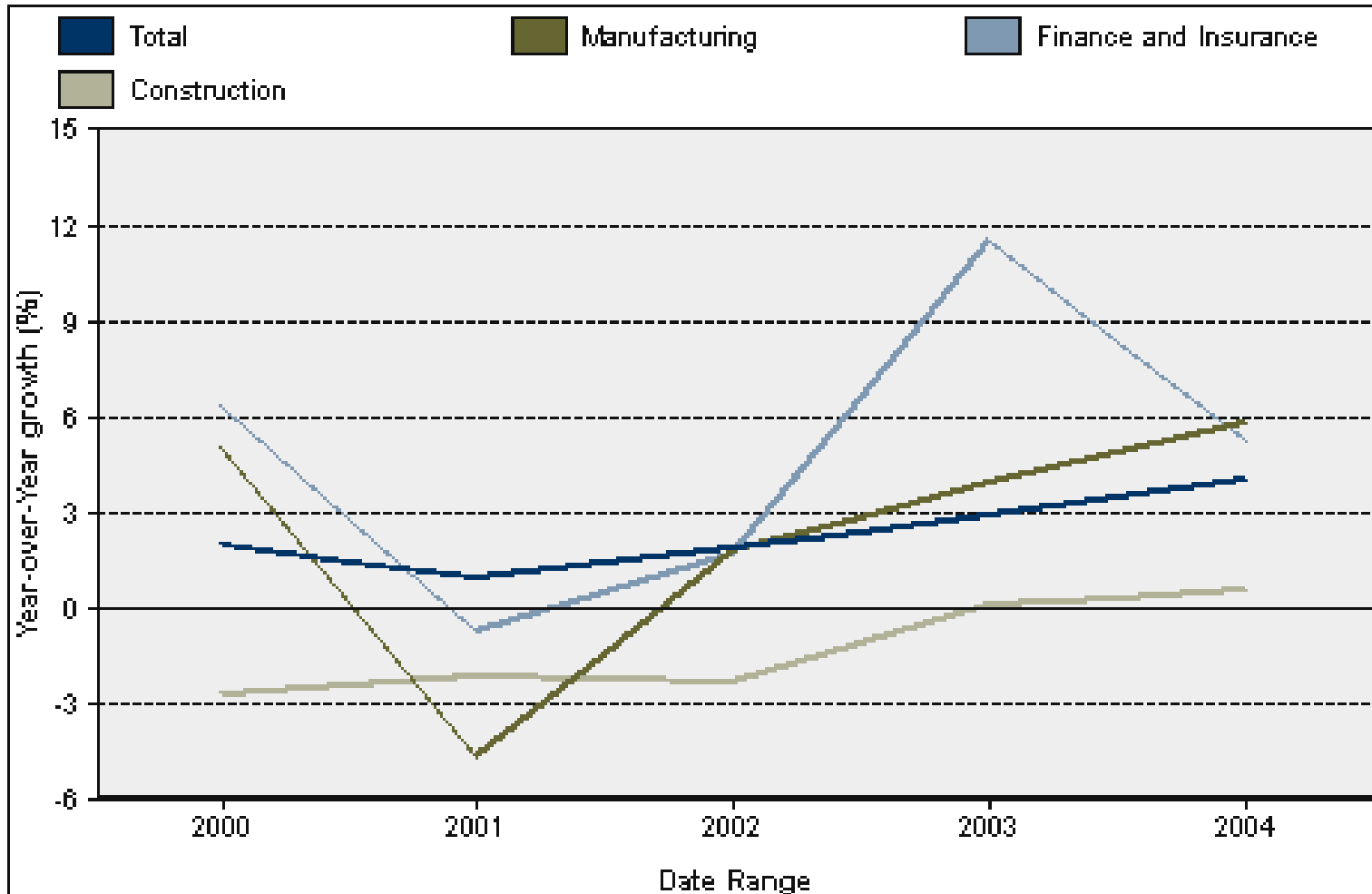
Wisconsin employment growth major sectors



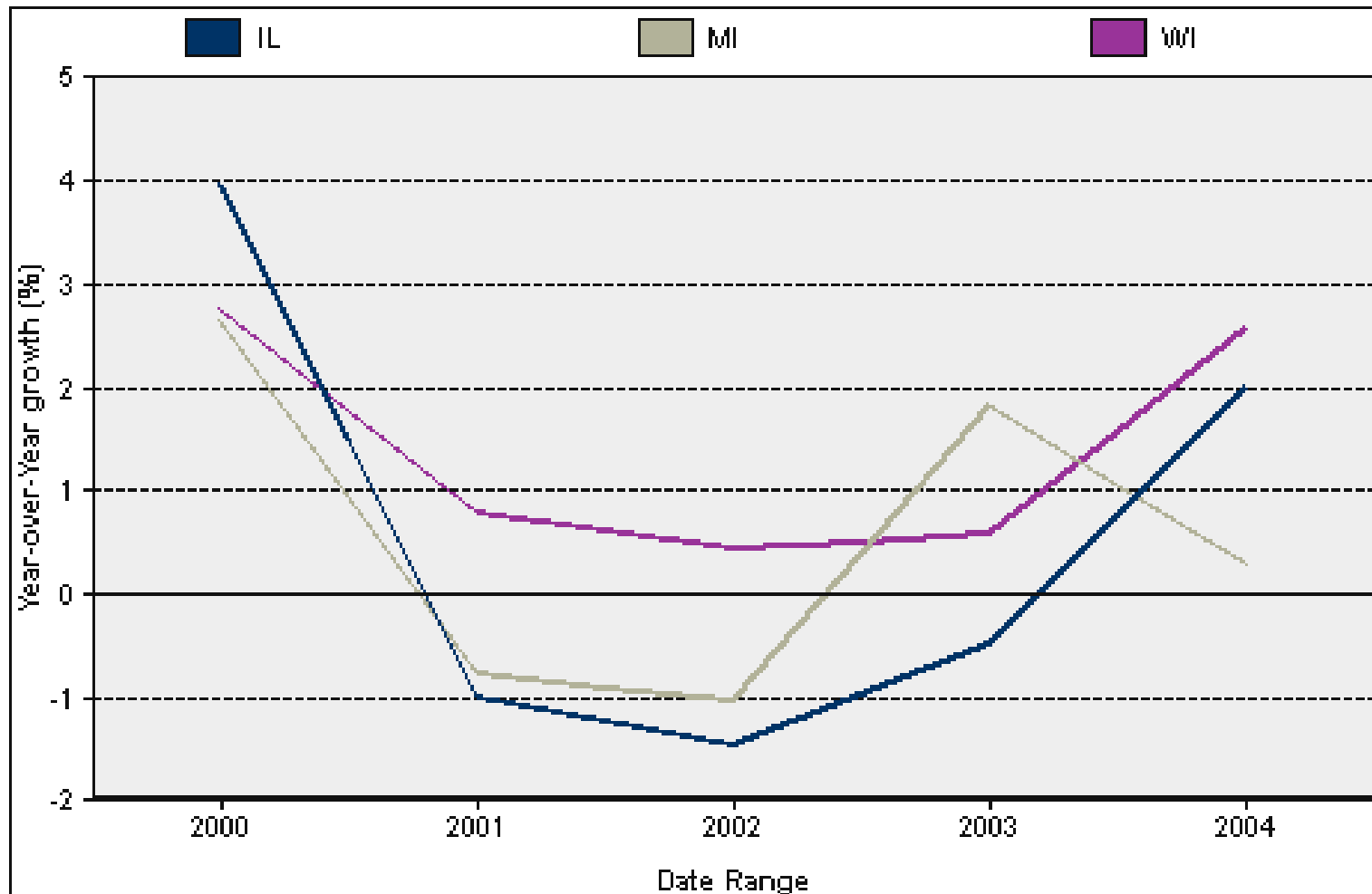
Employment growth state comparisons



Wisconsin output growth

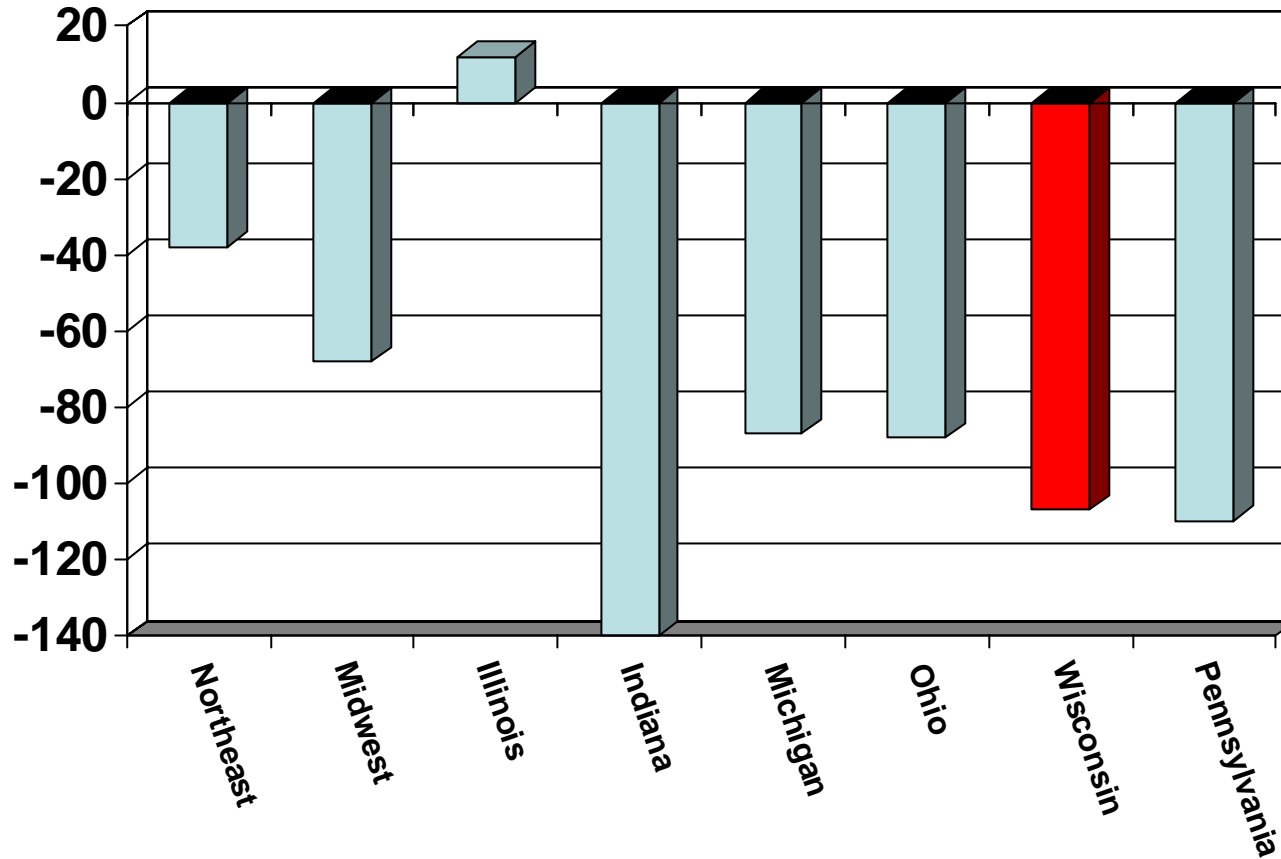


Personal income growth



Net migration rates for college educated 25-39 year olds, 1995-2000

(U.S. Census 2000, inflow/outflow per 1000 inhabitants)



Wisconsin outlook

- Relatively strong performance in a weak region
- Historical strengths still exist, hard working state with excellent education resources
- Pressure is the future—grow strong without growing big