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CURRENT ECONOMIC COMMENT BY DISTRICT

Prepared for the
Federal Open Market Committee
by the Staff

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Summary*

The overall impression that emerges from the individual District Red Book reports is one of continuing improvement in the economic outlook. Consumer spending is apparently on the rise, with indications of heightened interest in nonessential or postponable goods and in both big ticket and higher priced items. New orders, shipments and backlogs of industrial goods are reportedly strengthening, while business confidence is improving noticeably. These favorable developments, however, have not as yet been translated into a significant turnaround in the cautious inventory policies of businesses, and are still reflected only to a moderate extent in actual or planned increases in outlays for plant and equipment. Similarly, the increase in sales and production has not as yet found its counterpart in a sharp rise in the demand for labor, although it has reportedly led to a limited improvement in the unemployment picture.

With respect to consumer spending for goods and services, evidence of strengthening of consumer confidence can be discerned in reports to the New York Bank of increased purchases of nonessential goods and of big ticket items, and the fact that sales of durables are much more vigorous than those of nondurable goods in the Chicago area, with recreational vehicles such as motorcycles, golf carts, snowmobiles and similar items leading the field. In addition, several banks report a sharp uptrend in passenger airline traffic and Atlanta reports booming tourist business in Florida. And while sentiments were mixed in the Philadelphia District, retailers are expecting sales of home furnishings to be strong as a result of the high level of housing completions in the area. A note of caution, however, was sounded by some San Francisco

*Prepared at the Federal Reserve Bank of New York.

bank respondents who questioned whether consumer spending would become much stronger.

Concerning construction outlays, most District reports referring to activities in that industry and/or related industries, indicated that residential, and in some cases (Atlanta) nonresidential construction, continues to be a strong element in the current economic recovery. Some banks, however, including San Francisco, Chicago and Boston, report some feeling among their respondents that a levelling-off in the industry is probably in the offing.

As for industrial activity, manufacturers participating in the Philadelphia monthly Business Outlook Survey report a further pickup in new orders and shipments in February, which is expected to accelerate in March, while Chicago manufacturers of TV sets, furniture and home appliances are said to be very pleased with the trend of sales. Increases in varying degrees in orders, shipments and backlogs--often linked either to a rise in consumer demand or to strong construction activity--are also mentioned by several other Banks, including Richmond and St. Louis. The Dallas Bank notes that the Texas industrial production interest rose to a record level in January.

Despite the apparent strengthening of the economic recovery, District reports, however, generally note that businessmen are still maintaining cautious inventory policies at this juncture, and that no significant turnaround in such policies is indicated for the near future. The current inventory picture is well summed up by the results of the latest Minneapolis Industrial Expectations Survey, which indicate that nearly three quarters of the responding manufacturers considered their inventory positions to be satisfactory, with the balance equally divided between those who considered their inventories too high or too low. Similar sentiments were expressed by several other banks, although Chicago reported that an increasing number of firms showed concern over the adequacy of their inventories to meet rising demands.

Concerning business outlays for plant and equipment, Philadelphia reports that an increasing number of area manufacturers are planning to boost capital outlays, with firms contacted that planned increases outnumbering those planning cut-backs 10 to 1. Atlanta reports that previously postponed capital improvements at airports and other nonresidential projects will now be implemented. Cleveland notes that truck production and sales were at record levels, while both the Chicago and New York Banks saw evidence of a sharp rise in agricultural capital spending. On the other hand, St. Louis notes that capital expenditures are being delayed as long as possible, as its business respondents express reluctance to make major investments in view of the uncertainties surrounding profit prospects, and San Francisco reports a conservative attitude by local businessmen toward new capital investment.

Regarding the unemployment picture, reports vary among the District banks, but on balance suggest some limited improvement. Richmond thus reports sharp increases in manufacturing employment, as well as a substantial rise in the trade and services industries. The Philadelphia and New York Banks both had evidence that some firms were adding to their payrolls, while the Dallas Bank indicated that a rise in employment, notably in the construction industry, had lowered the jobless rate in the District to its lowest level in more than a year. According to reports to the Atlanta Bank, unemployment was "very low" in East Tennessee, and scattered improvement was seen elsewhere in that District. There has also been some increase in employment in the lumber industry in the San Francisco District. The Cleveland Bank notes a continued small recovery into January in non-farm employment, but expects no major improvement at this time. Similarly, Chicago notes that employers have been very cautious in increasing their work force, and St. Louis reports that apart from some gains in the construction and service trades, additions to payrolls are being delayed.

FIRST DISTRICT -- BOSTON

Reports from our directors indicate a continuing improvement in business activity. Savings flows remain unusually strong, but demand for funds outside residential construction has not yet picked up. In general, no significant price increases from suppliers were noted.

None of our directors indicated that their firms had either increased employment or overtime in the past month. One bank director, whose bank does the payroll for area firms employing 30,000 workers, stated that overtime work at these firms has been increasing steadily during the last month.

Savings flows in February and early March continue to be very strong. A large Boston bank cut its rate on savings accounts over $100,000 but reports that large institutional deposits (mainly universities) have not slackened, since savings deposits rates are still above short-term market rates. Demand for single-family mortgages is still excellent. A New Hampshire bank reported a 1/4 percentage point drop in mortgage rates. Within the last two to three weeks, there has been a noticeable slowing in the demand for apartments in the greater Boston area due to an oversupply, but contractors are continuing to borrow and build. In southern New Hampshire, Manchester still has an apartment shortage, but Nashua is experiencing a "sticky" market. While business loan demand is reported stable, businesses are "dusting plans from the shelf" and coming to Boston banks to discuss financing, but there is still little interest in increasing inventories.

Our business directors indicated that new orders in 1972 have been better than in the fourth quarter of 1971, especially those tied to consumer spending. Despite this, one business director indicated no plans to raise capital spending because of continuing excess capacity, and another director indicated that recent increases in capital spending were tied to cost increases, not larger planned capacity.

The four academic respondents contacted this month, Professors Eckstein, Samuelson, and Wallich and Dr. Shapiro, agreed unanimously that the Federal Reserve should permit short rates to drift up, though each had a different reason for doing so. Expressing some concern over the international position of the dollar, Wallich felt the Europeans need some evidence that we are cooperating. The recent rise in the money stock presents a good opportunity to allow an "upward drift" in short rates "for a short period of time". Over the next quarter or two, Wallich would ignore the money stock as a policy target, even if it were to shoot up considerably, and concentrate upon interest rate behavior.

Samuelson would encourage an "operation twist" policy even though it would be limited in what it could accomplish over a long time period. He felt there is a serious international "war of nerves" going on and fears capital controls abroad are a dangerous possibility. At the same time, he warned that the foreign exchange problem cannot be overcome by the amount of adjustment the United States will be willing to make in an election year. Samuelson took an 8 percent to 9 percent rate of monetary growth as "par" for the year--maybe more between now and Labor Day and less afterward. Even then, there may be some increase in short rates. Open market operations should be used to prevent this rise from being translated into the long end of the market. Since the middle of 1971, the dynamics of the economy have meant that following only aggregates or only interest rates as targets would lead to unpredictable effects in the other variables. Samuelson inferred from this that one must "look at both all of the time".

Eckstein and Shapiro welcome a continuation of the upward drift in short rates, which they had been expecting, since it will get short rates back in line with fundamental factors and not because of international considerations. Shapiro finds little evidence that short money flows are sensitive to interest differentials rather than to the expectation of devaluation. He argues further that the loss of short money is of little consequence. Shapiro expects short rates to continue to move up and long rates to move down more, with AA utility new issues at 6 1/2 percent to 7 percent by the year-end. Shapiro thinks the Fed should continue to pursue a 5 percent to 7 percent monetary growth target but not be concerned by very large gyrations over a few months.

Eckstein's remarks focused on criticizing monetary authorities for not supplying bank reserves more smoothly over the past six months. After several months of excessive stringency, the Federal Reserve responded in December by producing excessive liquidity in the banking system. Part of the dollar outflow stems from the huge reserve growth since December. For the present, Eckstein urged a smooth growth in reserves with an eye toward preventing increases in long rates. Eckstein cited a simulation experiment in which a 1 percent rise in the bond rate left the unemployment rate, a year from now, over 6 percent and rising.

Respondents' views on the prospects for the economy differ. Wallich stands by his earlier estimate of an $85 billion gross national product (GNP) gain, and Shapiro sticks to his $100 billion forecast. Upward revisions in business fixed investment combine with cuts in consumption, leaving Eckstein with an unchanged GNP estimate of $1,143 million for 1972.

SECOND DISTRICT -- NEW YORK

A moderately more optimistic picture of the economic outlook, as compared to last month, emerged from opinions expressed by the directors of the New York Bank and the Buffalo branch, and other businessmen. Consumer spending appears to have strengthened somewhat, while business confidence was reported to have improved moderately. The unemployment situation continues unsatisfactory, but is apparently a little better than earlier in the year.

Consumer spending, which for the retail industry as a whole had been relatively sluggish in February, seems to have quickened in the very recent past, with scattered indications of increased sales of higher priced items. Among the directors, a senior official of the largest upstate firm felt that the underlying trend of consumer spending has continued to improve, and saw evidence of increased consumer willingness to trade-up in the strong sales of his firm's new movie cameras. A head-office director referred to an across-the-board rise in airline travel and to a "dramatic" increase in domestic television sets sales, while another director, an upstate businessman, noted that, in his area, sales of higher priced automobiles were rising more rapidly than those of cheaper models. Nevertheless, most of the directors at both the head office and the Buffalo branch, did not discern any fundamental changes in consumers' attitudes as yet. Among the retailers contacted, an official of a high-price and high-quality New York City department store with branches in the suburbs reported that, following a rather sluggish performance earlier in the year, sales by his firm had picked up noticeably so far in March, and while he remained cautious, he felt that 1972 would be a good year for his firm. Similarly, the vice-president of a large nationwide chain of department stores reported a strengthening in consumer demand at his firm's stores in the recent past and, notwithstanding the rather slow start earlier this year, looked for a significantly better retail sales performance in 1972 as compared to 1971--both for his firm and the retail trade industry in general. Finally, an official of a medium-price retail store chain, which has experienced a gradual increase in business since last fall, stated that he expects this trend to continue and noted that in the past month there had been a significant increase in his firm's sale of big-ticket items such as furniture and home appliances.

Also encouraging was a report of some firming in business confidence. Among the Buffalo branch directors, the president of a Rochester bank traced this strengthening to the "slightly better" profit outlook, while the chairman of the board of a Buffalo bank felt that the recent stock market strength mirrored an improved mood; he also reported some pickup in machine tool orders in recent months. In addition, another upstate banker pointed to the relatively "ambitious" capital spending plans in his area, while a senior official of a food processing company pointed to a recent sharp rise in farmers' borrowings from agricultural financial institutions which he felt reflected a significant increase in farmers' capital spending. Among the head-office directors: the chairman of a large New York City bank stated that there had been "some general improvement" in business confidence, an upstate banker saw signs of willingness to spend on plant and equipment, while a New Jersey and an upstate New York banker both felt there had been a modest improvement in business confidence in their areas. However, at a meeting of business leaders held at this Bank, a senior official of a large nationwide conglomerate stated that while he looked for a rise in capital spending in certain industries, other sectors such as the space and aircraft industries would not likely increase such outlays. He also noted that most manufacturers are "a bit wary" and more reluctant than in the mid-1960s to embark upon large-scale capital outlays. As in previous months, some businessmen felt that most of the capital outlays would be largely limited to environmental control purposes.

There was some evidence at this time of an upturn in inventory outlays. The president of a large metal processing corporation reported some inventory buildup in the metal industry, but primarily as a hedge against expected price increases in copper. Another director referred to a rebuilding of inventories in computer related lines. The retailers that were contacted, however, all reported that while their firms were increasing inventories somewhat in view of their expectations of increased sales, such outlays were being kept under tight control. The current inventory outlook was perhaps best summed up at the Buffalo branch directors' meeting where it was noted that businesses had "learned to live" with lower inventories, and are becoming less concerned about the occurence of "stock-outs".

Although the respondents saw no dramatic changes in labor market conditions over the past month, there were no further reports of cost-cutting layoffs and in fact several respondents saw some strengthening in the demand for labor, particularly skilled workers. Some improvement thus was noted in the Rochester area, while a senior official of the largest upstate firm observed that unemployment rates for experienced workers were trending down. The New Jersey banker stated that there had been a "fair" improvement in the job market in his area, and that it was harder to get qualified workers. A similar sentiment regarding skilled workers had also been expressed by a senior official of the country's largest communication firm. Finally a director reported that his company's efforts to improve productivity through reductions in production workers had been "somewhat overdone" and that his firm was now increasing its work force by a few hundred workers. On the other hand, a number of respondents looked for little change in the unemployment picture in the near future. The official of the large manufacturing conglomerate did not expect a quick rebound in manufacturing employment, while the chairman of a large department store chain expressed the belief that unemployment benefits and high welfare payments are "geared to keep the unemployment rate high".

THIRD DISTRICT -- PHILADELPHIA

Economic conditions in the Third District continue to show some signs of strength and optimism. Area manufacturers report further pickup in new orders and shipments during February along with added employees on the work rolls. The increased activity is expected to continue at least through the next six months. Plans for capital expenditures are strengthening as well. Bank loan demand remains sluggish but increased activity is expected in the next two months. Retailers find the consumer is still bargain hunting, but they also expect more activity in the near future. Prices in the manufacturing sector seem to be under less pressure and the near-term outlook is for more of the same.

District manufacturers polled in this Bank's monthly business outlook survey reported a continuation of the increased economic activity experienced in January. Over a third of the respondents reported increases in new orders and shipments for February, while more than 13 percent added employees. Also during February, the average employee workweek was increased by 13 percent of the firms. This pickup is expected to accelerate in March. Over 45 percent expect increases in new orders and shipments, and nearly 18 percent plan to add employees.

Moreover, the area manufacturers remain optimistic about the longer run future of the regional economy. Three out of four forsee an increase in general business activity at least through the next six months, and two thirds of the respondents expect new orders and shipments in their own firms to be rising six months from now. An increasing number of area manufacturers also are planning to boost capital outlays. The proportion of firms intending to increase capital expenditures outstrips those planning cutbacks by a margin of over 10 to 1--the highest in over two years.

Encouraging signs are appearing on the price front as well. Over three fourths of the responding manufacturers reported prices were steady during February, and the same number expects them to be unchanged in March. Furthermore, the proportion of manufacturers anticipating price increases for March was about half the level of those that predicted increases for February.

Area bankers report sluggish loan demand but expect at least a seasonal pickup in the next few months. A representative of one large Philadelphia bank noted a decided change in tone among area businessmen. He believes that businessmen are finally convinced the recovery is for real, and he thus expects loan demand will be rising by the end of April. One banker on the board of directors expressed several concerns of small bankers. He noted they are currently worried about declining deposit activity, especially in the wake of deposit rate cuts. In addition, lack of loan demand has caused many small banks to become rather liquid and thus threaten bank profits. As an example, he cited some banks that have 20 percent to 25 percent of their assets in Federal funds.

On the retail front, area business economists report some strength in autos but little encouragement elsewhere. Department store sales have shown little improvement over the last month. One store representative says the consumer is still bargain hunting but reacting to both price and quality. He cited that budget store sales have been in the doldrums for many months. Customers wait for sale prices on regular items rather than settle for budget items. Retailers are expecting some help, however, from the spring weather. Also, home furnishings are expected to be strong as a result of housing completions in the area.

CLEVELAND -- FOURTH DISTRICT

Most of the developments in the District point toward a firming of the current economic recovery. New orders and producers' backlogs in manufacturing are still rising and are expected to show further gains in March. Nonfarm payroll employment continues to rise, although the insured unemployment rate leveled off in February after having declined for several months. The steel inventory liquidation is largely completed, suggesting a continued recovery in output and shipments in that industry. Some of our directors believe, however, that increases in manufacturing industry payrolls in the near term will be quite modest. Finally, several Pittsburgh banks lowered passbook savings rates, reflecting an unfavorable spread between deposit rates and loan rates.

Nonfarm payroll employment continued its small recovery into January. The District's insured unemployment rate, which has been declining since last September, leveled off in February, however. Most major metropolitan areas in the District are beginning to show signs of recovery, but continued unemployment problems are reflected in the addition of Wheeling, West Virginia, and Pittsburgh, Pennsylvania, in February to the list of areas with substantial unemployment. Although some industrial directors have reported recalls of workers, numerous layoffs and some plant closings have been reported, indicating that the employment turnaround is of modest proportions. Several directors foresee strong sales gains in the period ahead, but in general they have indicated that there will be no major employment additions in their plants.

Consumer steel inventories declined at the end of January to year-ago levels, suggesting near completion of inventory liquidation. Steel output rose strongly in February and is expected to increase again in March. Reporting steel companies indicated that new orders are strong, with the exception of certain types of construction steels. There were slight increases in both the production and sales of domestic new cars in February, and further small gains are expected for March. Truck production is running at maximum capacity, and February truck sales were at a record monthly high level.

Reports from directors indicate the pace of business for firms supplying products to the construction industry is excellent. Comments on the machine tool industry ranged from "dismal in February" to more optimistic comments of general recovery. Two directors mentioned rising orders in steel and office machines; however, they also expressed the view that employment gains would be limited.

Our latest survey shows that the District's manufacturing sector continued to show clear-cut signs of recovery in February, with faster than anticipated increases in new orders, shipments, backlogs, and labor utilization. On the other hand, there is little to suggest any sizable pickup in the rate of inventory buildup. The available evidence on inventories suggests that inventory accumulation has not yet turned around. Firms expect the upward pace of manufacturing activity to continue in March, with large gains in new orders.

District bankers have continued to talk about the unfavorable margin between deposit rates and rates on loans and securities. This has been coupled with an expectation that business loan demand will not revive until sometime in the second quarter. As a reflection of these concerns, several large Pittsburgh banks cut their passbook savings deposit rate from 4 1/2 percent to 4 percent on March 1 and extended the maturity structure of rates. Stated mortgage rates were also reduced (the base rate on conventional loans is now 6 3/4 percent). It is too soon to determine whether the pressures of these combined moves will induce mutual savings banks and savings and loan associations to follow.

FIFTH DISTRICT -- RICHMOND

Results of our most recent survey suggest that the pace of economic activity in the District continues to advance, perhaps at an increasing rate. Manufacturers generally report further increases in shipments, new orders, backlogs of orders, employment, and hours worked per week. Bankers and trade and services respondents indicate substantial improvements in sales accompanied by increases in employment. While business loan demand continued the weakness first reported in the last survey, the demand for consumer and mortgage loans remains strong. Contact with our regular survey respondents and other businessmen fails to indicate any substantial step-up in the rate of inventory accumulation. Respondents continue to view the outlook for future business conditions with considerable optimism.

The diffusion of responses of manufacturers in our latest survey indicates that strength in shipments, new orders, and backlogs of orders is greater than at any other time in the last six to eight months. Increases are reported by important producers in such industries as chemicals, metals, textiles, and synthetic fibers. Manufacturing respondents report sharp increases in employment and hours worked per week, while trade and services respondents indicate a substantial increase in employment but no change in hours worked per week. Banking respondents report that there has been little change in employment in their areas and that available labor supplies are moderately higher.

Gains in sales were reported by a large proportion of trade and services respondents, and bankers indicated substantial improvement in both automobile and general retail sales. Some price increases were reported in the trade and services areas, but the diffusion of manufacturing responses suggests no significant changes in industrial prices. Both groups of respondents indicated further increases in wages paid.

Manufacturers report a slight decline in actual inventories and a moderate increase in inventory levels relative to desired levels. Trade respondents indicate increases in both the actual level of inventories and the level of inventories relative to desired levels. Conversations with representatives of several large retail outlets and manufacturers in the District suggest that no important changes in inventory policy have occurred in recent weeks nor are any planned. A sizable number of manufacturing respondents report that current capacity is less than adequate.

In spite of the indicated pickup in both trade and manufacturing, demand for business loans continues soft, but bankers report good increases in the demand for consumer and mortgage loans. According to banking respondents, both residential construction and nonresidential construction continue strong.

On balance, results of our survey and other contacts indicate that businessmen in the District continue to view business prospects with optimism. Nearly 60 percent of the banking respondents repoted that they expect an increase in business activity in the months ahead.

SIXTH DISTRICT -- ATLANTA

Most businessmen and bankers report stable or improving business conditions and sentiment. Confidence is distinctly stronger than it was a year ago, yet appears to be building gradually. Reports tend to indicate that increased credit availability is having a desired effect and that economic strength is spreading to nonresidential construction and manufacturing, including plant and equipment spending. Retail sales and tourist expenditures are, reportedly, holding up well. Very little comment has been made about Phase Two controls. The areas of greatest inflationary pressure continue to be Florida real estate and utility rates.

An increase in the availability of financing is evidently responsible for an announcement of plans to begin construction on a large hotel in downtown Nashville later this year. This project had been held up earlier by high interest rates and a lender's demand for use of the first two floors of the building. Previously postponed capital improvements at the Birmingham airport have recently been given to go-ahead, and capital improvements will soon begin at the New Orleans airport. Moreover, a large shopping mall is being planned for the Birmingham area.

Residential construction is reported to be booming along the northeast Florida coast, where several large condominium projects are planned or under construction. Strength continues in the Orlando area, where construction has begun on 1,600 apartment units. Disney World has also announced further plans for a second-home community near Orlando. Northwest Florida also reports great strength in residential construction. A planned unit residential complex has been announced for a tract north of Atlanta. Construction on this project is expected to be completed in five to eight years.

Our directors describe manufacturing activity in middle Tennessee as "strong", with one major firm working overtime, and unemployment in east Tennessee as "very low". The University of Tennessee reports that the employment picture for graduates may be showing signs of improving. During the first academic quarter, the number of organizations interviewing on campus is expected to increase to 271 from last year's 232. However, another director reported that, while business is good in Alabama, one should not expect unemployment in many parts of Alabama to be significantly reduced. Still, there have recently been employment increases at scattered apparel plants in Alabama and other southeastern states. An apparel concern that has about 8,000 employees in Alabama has recently announced major capital expansions, including two new plants. Elsewhere, plant expansions have been announced in meat packing, chemicals, and auto manufacturing.

Retail sales are generally reported to be holding up well. Tourist business in Florida is booming. Disney World is in the process of hiring 1,300 youths of high-school and college age for Easter and summer work. Ringling Brothers Circus is going to build a permanent circus complex costing $50 million about thirty miles southwest of Disney World.

Land speculation is reported in North central Florida, where property is turning over at a rapid pace and at skyrocketing prices. The TVA has warned of a possible future electric rate increase, and a Georgia power company will request higher rates later this year. Commercial bankers express concern about the profit squeeze caused by the combination of large time deposit increases and weak loan demand, but no new reductions in time and savings deposit rates have been detected.

SEVENTH DISTRICT -- CHICAGO

The likelihood of a gradual uptrend in total business activity for the remainder of 1972 is widely accepted in this District. However, most analysts in the region who attempt to estimate economic aggregates foresee a rise of $80 billion to $90 billion, at most, in gross national product (GNP) for 1972 over 1971. Fears of a resurgence of price inflation are widespread. Employers are greatly concerned over productivity and union opposition to work-rule changes. Consumers continue to add to liquid savings at a high rate. Retail sales of durables are much more vigorous than sales of nondurables. Orders and output for most types of capital equipment are either vigorous or improving moderately. More companies are concerned about whether inventories of components and finished goods are adequate to take full advantage of a more pronounced uptrend in demands. Nonresidential construction of most types apparently will rise this year, while residential construction, although continuing at very high levels, is expected to slow down gradually. With an ample supply of funds, lenders are again seeking to make certain types of loans that they deemphasized in the late 1960's.

The uptrend in employment in recent months appears to have been less vigorous in the Seventh District than in the nation. Employers have been very cautious in increasing staff. With rising output, spectacular increases in productivity are occurring in some industries. One major airline is handling about 10 percent more traffic than a year ago with about 10 percent fewer employees. Jobs remain "hard to get", in almost all areas of the District, certainly by comparison with 1969. Employers usually are able to choose between a large number of applicants and can apply higher standards. At the same time, large employers are subject to pressures to avoid using hiring standards that may be judged to discriminate against minority groups.

Makers of furniture, appliances, and TV sets continue to be very pleased with the trend of orders and sales. Inventories are said to be in good shape. The main increase in inventories since last year has been at the distributor level, a development that is viewed as desirable.

Retailers we know report sales of nondurables are lagging sales of durables. But it is very difficult to get an adequate reading on retail sales by type or region, partly because companies are secretive and partly because the fortunes of particular chains and individual stores are shifting year by year. The completion of large new shopping centers, the introduction of seven-day shopping weeks, and the changing character of certain retailers--product lines, locations, merchandising techniques, etc.--keeps the picture in a state of flux and reduces the value of reports from a fixed group of stores, even if reports are current and accurate.

While it is often said that consumers are "cautious","buying what they need", etc., there is much contrary evidence. Perhaps the most vigorous component of the consumer goods field is recreational vehicles--motorcycles, golf carts, snowmobiles, and motor homes (called "expensive toys" by a prominent District producer). Production of most of these goods has been at or near capacity.

The improvement in capital goods continues to be spotty, with heavy trucks the star performer. Sales of some types of farm and construction equipment are far above last year's rate. None of the capital goods producers are reporting further declines in orders, but complaints about the lack of a vigorous uptrend are common.

Steel orders and shipments are now improving in a steady fashion in place of the "sputtering" uptrend noted earlier in the year. Some steel users are believed to have reduced stocks excessively and are now reversing the process. Steel demand from producers of motor vehicles, other consumer durables, construction, and shipbuilding is good. Demand for steel for bridges, highway projects, pipelines, and railroad equipment is still slow.

A District chemical company with a broad product line reports that orders are strong for most lines and that the market has a much better "tone" than a few months ago.

Housing experts expect a gradual decline in starts, seasonally adjusted, as the year goes on. First, vacancy rates are rising, especially for high-priced homes and apartments. Second, reports of shoddy construction, charges of dishonest Federal Housing Administration appraisals, and sharp increases in foreclosures in the central areas of some large cities (especially Detroit) may cause some home buyers and lenders to be more hesitant in making commitments.

Banks and other lenders are actively seeking borrowers. Business loan demand at large banks continues very weak. Some banks are increasing real estate loans and purchases of consumer instalment paper. Some life insurance companies are returning to the farm mortgage field. Savings and loan associations are becoming active in financing mobile homes. With savings inflows continuously very strong, some large banks are no longer offering consumer certificates of deposit (CDs) at premium rates, and bank executives are outspoken about their desire to cut the passbook savings rate if competition would permit. On the other hand, a very large bank is now offering longer maturity CDs (up to four years) at graduated rates (up to 6 1/4 percent).

EIGHTH DISTRICT -- ST. LOUIS

Business activity in the Eighth Federal Reserve District continues to increase moderately. According to a survey of leading businessmen, the uptrend in construction activity established last year is apparently being maintained. Retail sales at larger department stores are running somewhat ahead of a year earlier, and factory orders continue to improve moderately. Demand for transportation services is rising. The agricultural sector is quite optimistic as a result of recent price increases for a number of major farm products. Some businessmen, however, expressed doubt that the rosy projection of a $100 billion gain in gross national product (GNP) will be achieved. They point to the reluctance of businesses to make major investments in view of expected moderate profit levels. Furthermore, few report increased employment or intentions to hire additional personnel. Savings at financial agencies remain at high levels, and interest rates on mortgages are receding.

With the construction industry leading the way, business activity continues the moderate uptrend established in late 1970. Suppliers of new building materials and new household equipment report rising sales. Expenditures for improvements on older buildings are likewise increasing.

Farm income prospects have improved substantially in recent months, and farmers are spending more on production items. Sales of farm production supplies, especially chemicals, are running well ahead of vear-ago levels.

Airlines travel continues the sharp uptrend which began in the fourth quarter of last year. With the relatively narrow margin between use and capacity, the gains point to an early increase in passenger plane production.

Retail sales are running ahead of year-ago levels at most stores and somewhat ahead of the amounts budgeted. Major retailers in the area, however, do not believe that this will be one of their better profit years. They report increasing difficulty in showing a profit at large downtown stores, where their volume of business is usually greatest. The large chains report that all of their gains are coming from outlying branch stores.

Despite the gains in factory orders and retail sales, new investments and additions to payrolls are being delayed as long as possible. Major manufacturing firms report that nothing has occurred to date to merit an increase in their investment plans. One official reported that he could see nothing more than a very moderate uptrend, with some increase in profits resulting from stringent cost cutting. There were a few reports of increases in expenditures for labor-saving equipment and plant modernization, but none reported major plans for increasing overall capacity. Two retailers reported some new investments in outlying stores, but both indicated excess capacity in some older establishments.

It is difficult to find a major manufacturing firm that admits to an expansion of its work force. Some have changed the composition of their work force, adding engineers and reducing manual laborers and vice versa, and occasionally one will report rehiring some employees who were laid off earlier. The interviews thus confirm the statistical reports that the employment gains have occurred almost entirely in services trades and in construction.

Financial agencies report that inflows of savings continue at a high rate, and withdrawals are below average. Negotiated rates paid on large savings accounts are down somewhat. Maximum permissible rates are still being paid on most regular savings accounts by the savings and loan associations, but some commercial banks have reduced their rates paid from the maximum permissible levels. Loan volume continues to rise moderately, but interest rates on mortgages have receded somewhat in recent weeks. Some conventional mortgage loans of up to 80 percent of the purchase price are being made at a 7 percent rate, and some loans up to 67 percent of the purchase price are made at a 6.75 percent rate. These rates are down from 7.25 percent and 7 percent, respectively, since the first of the year.

NINTH DISTRICT -- MINNEAPOLIS

Although bank directors remain optimistic about District retail spending in 1972, reports varied concerning retail sales in January and February. Business loan demand at Ninth District commercial banks was described as steady or weak. Ninth District businessmen in general were characterized by bank directors as being comfortable or satisfied with their current inventories.

Directors' reports were mixed concerning retail sales in January and February. The head of a large Minneapolis-based retailing firm indicated that his sales had flattened out in January and February, while another director reported that automobile and hard goods sales had improved in the Twin Cities during the first two months of 1972. Severe weather was cited by two directors as restricting sales in their areas, but another reported that retail sales in his had matched or exceeded earlier expectations in both January and February.

Bank directors continue to anticipate that 1972 will be a good year for consumer spending. One director was quite optimistic about retail trade in his area, and cited as evidence the fact that three groups are considering building shopping centers there. A director from South Dakota indicated that his state is looking forward to a very good tourist season this summer. One director, however, revealed that retail sales in his area probably will not be as strong as they were in 1971, while another does not expect retail sales growth in his area to match the projected advance in national retail spending. In addition, an economist with a large District retailer is forecasting that in 1972 national retail sales will be up 7.2 percent from a year ago, and department store sales will advance 12.1 percent.

Business loan demand at Ninth District commercial banks was described by most directors as steady or weak. One director, who considered business loan demand in his area weak, did report a recent pickup in consumer and real estate lending, while another attributed brisk business loan demand in his area to the fact that businessmen and farmers needed more money to operate this year. Still another director reported that higher livestock prices have been responsible for an increase in agricultural loans in his area.

Ninth District businessmen in general were characterized by bank directors as being comfortable or satisfied with their current inventories. These observations concur with those made by manufacturers responding to our latest industrial expectations survey, as 72 percent of the respondents considered their inventories satisfactory. The remaining respondents were equally divided, with 14 percent describing their inventories as high while the other 14 percent considered theirs too low. Because severe weather in the northwestern part of the United States had slowed the production of lumber products, one director did report, however, that suppliers of building materials in his area were concerned that a shortage of building materials could develop. He also indicated that restrictive price ceilings had discouraged manufacturers from producing certain needed building materials.

TENTH DISTRICT -- KANSAS CITY

Consumers in the Tenth District are contributing to increasing economic activity, according to reports received from retail food chains, large department stores, automobile dealers, and banks. Sales of new domestic automobiles have been generally better so far in 1972 than in the latter months of 1971. However, soft goods seem to be moving better than consumers' durables other than automobiles, according to most department stores. Consumer credit at District banks continues to climb, both in the form of instalment loans and the use of bank credit cards. District banks have also experienced stronger loan demand from local business borrowers in the last few weeks.

Response from retail sellers of nonfood items (primarily large department stores) across the District indicate that, with few exceptions, sales so far in 1972 are running well ahead of a year ago. There is apparently no general movement toward additional inventory building beyond what has already been budgeted for this year. On balance, soft goods seem to be moving better than consumers' durables. Most retailers interviewed expect 1972 to be a good year, although a major Kansas City department store anticipates little sales strength until fall.

Interviews with automobile dealers and distributors in Kansas City, Denver, Oklahoma City, and Omaha revealed that sales of new domestic automobiles were generally better so far in 1972 than in the closing months of 1971 (Omaha excepted). Inventory situation reports varied, depending on the make of car, but most dealers described their inventories as "normal" or "satisfactory". Some foreign car dealers indicated that their sales had been hurt by the New Economic Policy, especially in the latter months of 1971, but that their positions were improving this year.

A number of retail food chains were surveyed for current information on food sales and prices. Although the reports on sales were mixed, the information on prices formed a consistent pattern. On balance, food prices have not risen significantly since the lifting of the freeze, according to those firms contacted. Nevertheless, all reported a sharp increase in the retail price of meat some as high as 25 percent. In the last month, meat prices have shown greater stability, but only because retail gross profit margins have narrowed to unprofitably low levels. Efforts are being made to restore profit margins to more normal levels and, unless wholesale carcass prices fall sharply, retail meat prices may rise above current levels in the coming weeks.

These reports tend to support the behavioral patterns of food retailers observed in the past. Typically, retail food prices neither rise nor fall in direct proportion to price changes at the farm level; instead, changes in retail food prices tend to lag behind those at the farm level and are also subject to less variation. During the last two years, for example, the average price of choice slaughter steers rose about 10 percent, but the increase in the beef and veal component of the consumer price index was less than 5 percent. Similarly, average hog prices fell nearly 20 percent over the period, but the pork consumer price index dropped only 9.5 percent. Except for two brief interruptions, farm prices have climbed steadily since December 1970 and now average about 10 percent above a year ago. Sharply higher prices for meat animals have been responsible for most of the 7 percent gain since last November as well as the recent resurgence of the wholesale price index and consumer price index. Despite the prospects for some easing of beef and pork prices at the farm level in the weeks ahead, further increases in retail meat prices seem likely, given the aforementioned behavioral characteristics of food merchants.

Tenth District banks have experienced stronger loan demand from local business borrowers in the last few weeks, although activity in national accounts remains quite low. Construction and real estate loans for business expansion have picked up markedly in Albuquerque and Denver, while in other areas of the District, banks reported increased inquiries for these types of loans. There are some scattered signs of a prospective increase in loans to businesses for inventory purposes, although to date these have manifested themselves mainly as requests for larger credit lines and a more optimistic attitude noted in talks with business customers. Consumer credit continues to climb, with the maintenance of a steady rate of increase in instalment loans and some acceleration in the use of bank credit cards.

One reason for the relatively poor showing of national accounts may be the attempt of some District banks to maintain their prime rates above the New York level. By decreased use of their credit lines and threats to move their accounts to other banks, national customers have forced District banks to 4 3/4 percent or 5 percent on loans made to national borrowers. The prime rate to local borrowers remains as high as 5 1/2 percent at some banks.

Deposit flows continue strong at District banks, as increases in savings and consumer time deposits have more than offset seasonal decreases in demand deposits. District banks have not lowered their consumer time deposit rates in the last few weeks (most are still at Regulation Q ceilings). Some banks have experienced a runoff in their negotiable certificates of deposit, but many are adjusting rates to be able to turn over their existing stock.

ELEVENTH DISTRICT -- DALLAS

Recent indicators of economic activity suggest renewed strength in the District economy. Industrial production in Texas increased significantly in January. Moreover, employment in the five District states rose substantially, and the average unemployment rate for the region dropped. Construction activity in Texas also increased significantly, and retail sales continued to show strength. However, automobile registrations fell in January from a month before.

The seasonally adjusted Texas industrial production index rose to a record level in January, thus recovering from its slight drop in December. Among manufacturing industries, the most significant production gains in January were registered in petroleum refining and in the textile mill products, apparel products, and stone clay and glass products industries. The only industry to record a decline in January was the printing and publishing industry. The manufacturing component of the production index has risen sharply since last July after remaining relatively stable during the preceding eighteen months. Since mid-1971, this component has grown almost 7 percent.

Mining output also rebounded in January, gaining 2.3 percent over last month. Although improvements were reported in all industry groups, the significant gains were in natural gas liquids and crude petroleum mining. Contrary to the trend in manufacturing, the mining sector has fallen significantly from year-ago levels as this month's output was 2.9 percent behind that of January 1971. Output of utilities fell slightly in January but was still well ahead of its level a year earlier. The Texas oil allowable was raised for the month of March to a level 86.0

percent of capacity. This is the fourth consecutive monthly increase, reversing the steady downward pattern of allowable which existed for the first eleven months of 1971. No other District state changed its allowable in March.

Total employment seasonally adjusted in the five southwestern states rose a significant 1.3 percent in January. With this rise in employment, the average unemployment rate for these states dropped to 4.5 percent from 4.8 percent in December. The January jobless rate was the lowest in more than a year. Nonfarm payroll employment in the five-state region also increased significantly in January, with the service industries being the only major industry group to show a decline from December. The largest employment increase was reported in the construction industry.

Construction activity in the five southwestern states--as measured by the value of contracts awarded--increased significantly in January, with the increase occurring mainly in Texas. Except for Arizona, all other District states reported reductions from December. All three major categories of construction shared in the monthly gain, but residential building continued to show the greatest strength. The total value of contracts in the five-state region in January was more than half again greater than its level a year ago.

Sales of department stores in the District continued to show year-to-year gains in January, with Houston reporting the largest increase. New automobile registrations on the other hand continued to fall, with Dallas, Forth Worth, and Houston all reporting declines of about 25 percent from December. However, registrations were still substantially above their levels of a year ago.

District agriculture is progressing well. Wheat is making good growth over the District, although lack of moisture is becoming a limiting factor on dryland wheat. Cotton planting is making excellent progress in south Texas where soil and moisture conditions are generally good. Corn and sorghum planting is also making good progress, and the winter vegetable harvest continues active with favorable weather conditions prevailing. Range and livestock conditions declined slightly in January but remain well above levels of a year ago and are moderately above the ten-year average. There were 1.8 million head of cattle on feed in Texas on February 1, or 16 percent more than a year before. In Arizona, cattle on feed totaled slightly more than one-half million head, 4 percent larger than a year earlier.

The index of prices received by Texas farmers and ranchers registered a 2 percent gain in the month ended February 15, 1972 and was 21 percent higher than the level a year earlier. Most livestock and livestock product prices were up from both a month and a year ago. Crop prices generally declined from mid-January to mid-February but still averaged 20 percent higher than the year before.

Director sentiment still favors a slow to moderate growth in the economy, though reports hint at the beginnings of inventory accumulation, stronger retail sales, and heavier capital spending by business especially for pollution control. Phase Two is characterized by our directors as modestly successful in its psychological impact but of questionable long-range-control effectiveness.

TWELFTH DISTRICT -- SAN FRANCISCO

The views of our directors on economic conditions have not changed much from those expressed in the previous month: they expect a steady expansion to continue with a concurrent reduction in unemployment. The directors were asked about the prospects for an early acceleration of capital expenditures, and the concensus was that a strong investment upsurge is not about to begin, but that investment would maintain a moderate pace.

Although consumer spending and construction have provided much of the strength behind the current expansion, some directors expect a weakening in demand from those sectors. Consumer spending certainly has improved, but there seems to be no expectation that it will become much stronger. One director suggested that the improved automobile sales in late 1971 might well be at the expense of sales in 1972. Others pointed out unfavorable factors, such as the cut in disposable income of wage earners caused by the upward revision of the Federal income tax withholding schedules and, in California, the imposition of withholding for the state income tax.

As for construction, reports of continued activity--especially in residential construction--are tempered by concern about overbuilding. In California, vacancy rates have begun to climb in most areas of the state, and in time the point will be reached when financial institutions will be less willing to finance further projects. One respondent expects "substantial declines in authorizations" by lenders within the next six month. Certain classes of non-residential construction have been strong, for example, highway construction. On the other hand, high-rise commercial construction which had been very important last year in such cities as San Francisco may not be maintained in 1972.

The current level of construction activity has stimulated the lumber industry, particularly in Washington and Oregon. Demand for lumber and plywood has encouraged increased capital expenditures for mill expansion and modernization as well as directly increasing employment. Prospects for agriculture in the District continue to be good. The end of the dock strike has allowed the movement of grain to be resumed, although the carry-over of the 1971 crop may cause problems. Prices are expected to be good for beef and pork, and consequently feed grain producers as well as ranchers expect a profitable year. Sugar beet and seed grain prices are also expected to be favorable. In contrast, prospects are not so good for certain vegetable and fruit crops. The outlook for fruits for processing is unfavorable, and this is attributed by some directors to shifts in public demand away from processed fruits. Other fruit and vegetable producers whose crops cannot be harvested mechanically face rising costs of labor which may not be easily passed on. Yet the demand for some fruits, such as grapes, is rising, and there have been increases in acreage to keep pace with demand. Despite these weaknesses, the overall prospects for District agriculture continue to be favorable.

On the specific question of investment intentions, the majority of our nonbank directors indicate conservative investment plans. The only exception is in the lumber industry where, as previously noted, increased demand has required the expansion of capacity. Certain other industries are being required to make large capital investment to meet new pollution-control standards. There are regional variations as well. In Utah, a survey conducted by one of the banks indicated a jump in 1972 capital expenditures of about 12 percent. With those exceptions, our bank directors confirmed the lack of major shifts in investment activities above the rates of recent months.

In District banking, there have been no major changes. Many banks have cut their pass book savings rates to 4 percent even though savings and loan associations continue to pay 5 percent, and other commercial banks, including some relatively large banks, have maintained the 4 1/2 percent passbook rate. Lending rates have been reduced for certain lenders and categories of loans, but the lower price and greater availability of funds has not resulted in any resurgence of loan demand. Commercial-industrial loan demand in most states is described as unchanged or weak. In consequence, banks have been more aggressive in seeking business and making rate adjustments.