

CONFIDENTIAL (FR)

CURRENT ECONOMIC CONDITIONS BY DISTRICT

Prepared for the  
Federal Open Market Committee  
by the Staff

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## SUMMARY\*

On the whole the economy continues strong. Manufacturing activity is rising in most areas and is expected to continue upward. Labor markets are tightening and some labor shortages are reported. Inventory investment is reported to be rising only slightly, but plant and equipment spending is increasing as some manufacturers find themselves operating at near-capacity levels. Residential construction is continuing at a high level in most districts. Commercial construction is rising according to some reports. Retail sales generally remain strong. Farmers are making larger than average incomes despite various operating problems. However, on the darker side, inflationary expectations are rising significantly. Bankers report some credit tightening and frequently mention rising interest rates.

Production activity is rising. Most districts report increases in new orders, shipments, order backlogs or similar barometers of manufacturing activity. Some districts (St. Louis, Richmond, Boston) talk of strong increases in output. Durables manufacturers are mentioned with more frequency than non-durables producers in the various districts' discussions of rising manufacturing. The Richmond districts' furniture manufacturers are operating at a high level of output despite labor shortages. San Francisco reports that activity at Seattle's Boeing facilities are picking up. Cleveland refers to "dramatic increases in orders for machine tools."

Labor markets are tightening in some places. The Dallas report speaks of "particularly buoyant" employment opportunities. Labor shortages

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\*Prepared by the Federal Reserve Bank of Philadelphia.

are reported in central Florida. In St. Louis labor markets are "very tight" and employment for Research and Development personnel is picking up. No general labor shortage appears to exist, however. Minneapolis, for example, reports no shortage of skilled labor. Boston reports both labor shortages and pockets of high unemployment. Manufacturing jobs in Philadelphia aren't presently increasing. Cutbacks in the Federal budget are mentioned as a possible cause of unemployment pockets in some locales.

Most districts discussing inventories (New York, Cleveland, Philadelphia, Richmond) report that spending from this sector is not bullish. New York mentions "no discernible change in inventory." Cleveland talks about inventory investment leveling off at a lower level.

Plant and equipment spending is on the rise. The steel industry and consumer durables manufacturers in Cleveland's district are expected to expand their facilities. Chicago reports that an informal survey there revealed that manufacturers in the following fields are operating near full capacity: paper, petroleum, refining, machine tools, appliances, furniture, color television, trucks, recreational vehicles, electric motors, construction machinery, flat rolled steel, foundries, tool and die shops, lumber, gypsum board, insulating material, fertilizer and certain chemicals. Many firms in Philadelphia's monthly survey are currently reporting plans for increased plant and equipment outlays.

Residential construction is expected to rise or at least continue unabated in most districts. Minneapolis conducted a telephone survey of HUD officials and found that "the freeze on subsidized housing should not effect district homebuilding in 1973, but could dampen residential construction in 1974 and 1975." However, Atlanta and Dallas do refer to

diminishing rates of housing starts. San Francisco expects that its high level of construction may turn down. The reports on non-residential construction are mostly bullish.

The outlook for retail sales is generally good, although some districts do report that sales are still recovering from a lull that followed holiday buying. San Francisco's sales expectations are optimistic and they point out that tax refunds should boost consumers' spending this spring.

Inflationary expectations are rising on a broad front. Chicago reports that the oil companies there are not entering into their usual one or two-year contracts with oil truckers and other large users because of expected price rises. Philadelphia reports that the respondents to its survey report significant increases in their expectations about prices for the second month in a row. Minneapolis reports that some labor unions there plan to disregard the 5.5% wage guideline. New York reports that a number of its respondents are so concerned about inflation they think that price controls are probably necessary.

Most bankers across the nation are experiencing rising loan demand from businessmen and consumers. Applications for mortgages also show few signs of diminishing. Some Boston bankers are being more restrictive in granting lines of credit. Time and savings deposits are providing a small amount of new funds in most of the cases reported.

FIRST DISTRICT - BOSTON

New orders for capital equipment and consumer durable goods are continuing to advance strongly, according to our directors. Labor shortages are reported as well as continuing pockets of high unemployment. District bankers expect strong loan demand in the coming months, but are extremely worried about the competition from new accounts.

Our directors expect 1973 to be a very good year for the capital goods industries. Manufacturers of capital equipment see the projections finally being confirmed with substantial orders. Aerospace continues to be an exception in the vibrant capital goods industry. Not only are defense orders down, but commercial aircraft orders are below that expected three to four years ago.

Orders for consumer durables, especially those related to autos and travel campers, were noted as being very strong. Orders for nondurable consumer goods were reported as lackluster, but January is an off-season for these products.

Retail sales in Connecticut continue to be severely depressed by a three-month-old bus strike in six major cities in the state. At the moment, according to our director from Connecticut, there does not appear to be any early resolution to the conflict. If it continues for another 60 days, and retailers miss Easter sales after losing some Christmas business, small retailers in Connecticut will be in a severe financial squeeze.

Some of our directors report difficulties in hiring new staff, both skilled and unskilled workers. However, pockets of unemployment with unemployment rates in excess of 10 percent exist in the District.

District bankers expect strong loan demand in the coming months, with upward pressures on interest rates. Requests for bank loan commitments are continuing to grow, but not at an abnormally high rate for this stage

of the cycle. However, some banks are becoming more restrictive in granting lines of credit. Bankers in Massachusetts, Connecticut, and New Hampshire are very concerned over the potential competitive effects of new accounts on their demand deposits.

All three of the outside correspondents contacted this month, Professors Eckstein, Samuelson, and Dr. Shapiro, favored a monetary growth target of 6 percent. There was disagreement about the cause of the recent sharp increases in short-term money rates. Eckstein and Shapiro argued that the rapid rise in short rates was not sustainable, not being justified on the basis of fundamentals. They attributed the sharpness of the rise to concern about the course of inflation in general, and the willingness of the Federal Reserve to control monetary growth in particular.

Eckstein strongly criticized the high rates of growth of RPDs and the monetary aggregates over the last few months, and suggested that this "poor management" stemmed from placing too much attention on operational problems (the implementation of Regulation J) in relation to the more basic policy problems. He felt that the emphasis on aggregates in recent years has been successful, and repetition of the attempt to manage interest rates would lead to an abrupt halt in monetary growth as in the 1966-69 era. His policy prescription was for a smooth 7 to 8 percent growth in RPDs. Shapiro advocated a 6 to 9 percent growth in RPDs on the grounds that this would stabilize inflationary expectations in a favorable way and produce stability in long rates.

Samuelson did not believe that uncertainty about monetary management has contributed to the increase in short rates. He attributed the rise to exceptional strength in the economy which, in keeping with his philosophy of an "activist, swinging" monetary policy, led him to the recommendation that monetary policy needs to be tighter in the near term (4 percent money

in February) than it needs be in the intermediate term (6 percent in most quarters). He also stressed rate flexibility, suggesting that a run-up now could be followed by a leveling off or decline in the future.

Dr. Shapiro pointed to two factors relevant to the interpretation of inflationary pressures later this year. First, several steps have been taken to increase the supply of food which will alleviate the upward price pressure 3 to 9 months from now. Secondly, he cautioned not to generalize from the first few major settlements under Phase III. This warning was based upon John Dunlop's espoused preference for a case by case approach. The average collective bargaining settlement will be composed of wide extremes, rather than the blanket application of a fixed, permissible standard.



SECOND DISTRICT - NEW YORK

In the view of this Bank's directors and other business leaders contacted recently, the Vietnam accord may have a beneficial psychological influence on consumer confidence, but in general is not expected to have any major economic impact. The respondents reacted cautiously but favorably to Phase III, which was viewed as heralding eventual elimination of wage and price controls. They also approved of the Administration's budget policy, but in general felt it would be difficult to implement in the face of Congressional pressures. Little noticeable change in business inventory policies was reported.

The Second District directors generally agreed that most of the "peace dividend" accruing from the Vietnam settlement had already been realized, with a number of the directors pointing to the insignificant involvement of American troops in the war over the past several months. These directors, moreover, did not look for a resulting cut in Federal spending, both because of expected United States economic help to North and South Vietnam and increased military pay. One director, however, felt that defense expenditures during fiscal 1974 could be "significantly" reduced through a reduction in military personnel. He said this might occur since, with the changeover to an all-volunteer army, the actual number of volunteers may fall short of the levels planned in the defense budget.

The respondents in general reacted rather favorably to the modifications of the wage-price controls under Phase III, viewing it as an important step toward the eventual elimination of price and wage controls.

In this context, several directors felt these changes were particularly welcome in the light of the distortions and inequities that were emerging under Phase II. A number of respondents, however, recognized that inflationary pressures continued strong and that some form of controls was probably still necessary. One director, a senior official of a large oil corporation, stated that wages and prices may increase somewhat faster under Phase III, but that the rise could be held to modest proportions if sound monetary and fiscal policies are pursued. However, another director, a banker, thought that the Administration's estimates of inflation were somewhat optimistic, and saw inflation during 1973 in the range of 3 to 5 percent, and probably closer to the higher figure. Several respondents stated that the results of forthcoming major labor negotiations would play an important role in determining the success of the program.

All of the directors reacted favorably to the Administration's budget strategy. A number referred to the need for fiscal restraint in the light of the current economic situation. The Buffalo branch directors felt the strategy would gather widespread public support. These directors, however, along with the head office directors, had reservations regarding the Administration's ability to keep expenditures in line with the proposed budget in the face of Congressional opposition.

Most directors did not report any discernible change in inventory buying policies. The president of a nationwide retail firm expressed the view that retail firms were not accumulating inventories as a hedge against inflation at this time. On the other hand, the president of a large metals producing firm did report that there was now evidence

of inventory accumulation in metals in anticipation of further price increases.

The director associated with the oil industry said that petroleum inventories were severely depleted as a result of very strong demand, a leveling off in domestic production, and inadequate levels of imports. Against this background, he fears the nation may be facing a serious gasoline shortage later in the year.

THIRD DISTRICT - PHILADELPHIA

Most businessmen contacted report little change in current business conditions in the Third District, but the six-month outlook is more optimistic. New orders and shipments are up after a temporary lull which followed the Christmas rush. Current employment opportunities are flat, but the six-month outlook for hiring is good. Most of the respondents to this District's survey are satisfied with their current level of inventory, but many expect to increase inventories within six months. Plant and equipment investment is increasing. Housing demand continues strong. Demand for bank loans continues to expand but deposits are flat. These positive factors are partially offset by inflationary expectations, which have risen significantly for the past two months.

According to the respondents of this Bank's monthly Business Outlook Survey, production activity in the Third District is rising slowly again after it temporarily slowed after Christmas. About 20 percent of the firms responding to the Survey report increases in their new orders and new shipments. Most other respondents report no change in their production, but looking into the future most area businessmen are bullish. Sixty-five percent of the respondents to the Survey currently expect increases in their new orders and shipments within the next six months.

Employment opportunities in this District are flat. Over 80 percent of the firms report no current change from last month in their number of employees or the length of their average work week. But, employment prospects for the coming months are brighter. Over 40 percent of the responding firms expect to increase their number of employees, and a

fourth expect to increase their average work week within six months. This is a significant increase in the six-month employment outlook over what was reported one month ago.

Most area businessmen report that they are not currently expanding their inventories. However, within the next six months half the respondents to this Bank's Survey do expect to increase them. Plant and equipment spending plans for the next six months are the same as they were last month--half the firms plan to increase their investment and a third expect no change.

Construction activity in the Third District is recovering from local delays caused by a cement workers' strike during December. Most of the construction underway in this District is residential rather than commercial or governmental.

Inflationary expectations rose again this month. A fourth of the Survey respondents are paying or receiving higher prices this month while the rest report no change. In the next six months two-thirds of the firms expect to receive higher prices and three-fourths of them expect to pay higher prices. This is the second month in a row in which inflationary expectations rose significantly. Most of this increase is on the respondents' six month horizon rather than in the current month, however.

Third District bankers report that both their savings deposits and their demand deposits are up only slightly, after allowing for the seasonal fluctuations. The bankers say they must buy CDs if deposits are needed. Two of the bankers contacted pointed out that there was a negative spread for funds acquired in the CD market at current rates

(after adjusting for reserve requirements) and then loaned at the prime rate of 6 percent. One large bank reported a "tremendous" monthly increase in its business loans. The other banks report continued good demand for business, consumer and real estate loans.

FOURTH DISTRICT - CLEVELAND

The consensus of about 40 economists--mainly from important industrial firms and commercial banks in the District--who attended the Fourth District Business Economists Round Table Meeting held at the Bank on January 26 is that gains in GNP, both in current dollars and in real terms, will moderate during the year. The rate of inflation is expected to accelerate, and there are indications that capital spending will remain strong throughout 1973.

The median forecast of the business economists is for a GNP of \$1,264 billion in 1973, with real growth of 6.1 percent and an increase in the price deflator of 3.4 percent. A further upward surge in prices is expected during the first quarter, generated largely by food and fuels, but also by the Phase III program. Some support for this view has been provided already by the Cleveland purchasing agents' report for January, which shows a sharp increase in the percent of firms paying higher prices. On the other hand, some of our industrialist directors reported that they have instructed all divisions of their firms to operate on the Phase II basis until the rules of Phase III are clarified in order that their companies do not become cases.

The consensus of the business economists is that by the fourth quarter of 1973 real GNP will be expanding at less than 4 percent, inflation will be at a 4 percent rate, and unemployment will average 4.8 percent. Several reasons were offered for the projected slowing of the expansion during 1973: gains in consumer spending are expected to be somewhat less during the first two quarters of the year than the increase during the final quarter of 1972, and even less vigorous gains are projected for the second half of 1973. An implicit assumption was that consumers would save a large

share of tax refunds. In addition, the group was concerned about the fact that consumer spending for durable goods has been high relative to disposable income and that consumers have been taking on installment debt at an unsustainable pace. Accordingly, the economists expect the burden of debt repayment will begin to impinge on outlays for durable goods. For example, the median forecast of nine economists whose firms depend heavily on the auto market calls for total new car sales this year to be at virtually the same level as in 1972. Consumer spending for appliances and household furnishings is also expected to taper off in the second half, reflecting the group's projection of declining residential construction expenditures beginning in the second quarter.

Gains in inventory investment are expected to contribute less to the rise in GNP during the first two quarters of 1973, and inventory investment is projected to level off during the second half of the year. The economists also foresee a worsening of the net export deficit in the current quarter, reflecting the relaxation of oil import quotas. Most of the group expected an improvement in the deficit during the balance of the year, however.

Nonresidential fixed investment is the only major sector where growth is expected to remain strong throughout 1973. Dramatic increases in orders for machine tools lend support to the expectation of a strong year for capital spending. A machine tool firm in Cleveland said its new orders in the fourth quarter of last year had doubled from the year earlier quarter, which in turn were up significantly from the final quarter of 1970. One of our directors reported that his machine tool firm booked enough new orders in the month of December alone to carry the company's business through 1973 and into part of 1974.



A change in the composition of capital spending is also expected this year, with larger shares going to manufacturing and to expansion of plant capacity; these changes are expected to benefit the steel industry. Demand for flat-rolled products, used mainly in autos and appliances, is peaking now, while demand for heavy products should be increasing over the months ahead.

The business economists also held an extended discussion about the energy crisis. There was general agreement that this nation will continue to face severe problems in meeting its energy requirements during the next three to five years. The near-term implication is that this nation will have to rely increasingly on fuel imports until long-run solutions are effected. Concern was expressed over the impact of this situation on the balance of payments. Also, it was agreed that over the near-term, prices of fuel and energy will rise substantially, businesses will continue to face disruptions of fuel supplies, and the Federal Government will become increasingly involved in the energy field.

FIFTH DISTRICT - RICHMOND

Results of our latest survey of businessmen and bankers suggest that the Fifth District economy retains a strong upward momentum. Manufacturers' shipments, backlogs, and new orders registered strong increases over the past month, although production is being impeded by labor shortages in some areas of the District. Retail sales, including sales of automobiles, advanced over the previous month. Employment showed little change from recent high levels, but hours worked per week increased. Residential construction was unchanged, while nonresidential construction increased. Bankers and businessmen continue to be optimistic about the economic outlook in the District.

Our latest survey shows continued widespread strength in the manufacturing sector. There was a substantial rise in the number of manufacturers reporting increases in shipments, new orders, and backlogs. Increases in new orders and backlogs were especially pronounced. Furniture manufacturers are still plagued by labor shortages, and textile sales and production appear to be especially strong. While inventories reportedly declined further in the past month, inventory levels relative to desired levels are judged to be about right by most respondents. Numerous manufacturing respondents reported that current plant and equipment capacity is lower than desired.

Manufacturers reported little change in recent high levels of employment and additional increases in hours worked per week. On balance, banking respondents believe that employment in their areas has increased since the last survey. Unemployment rates as low as 1-1½ percent were reported in some local labor market areas. Increases in wages and prices received were experienced by a sizable number of manufacturers and retailers.

The retail sales picture in the District continues strong. Despite a sharp decline in the number of banking respondents reporting increased retail sales in their areas, on balance, bankers believe that retail sales showed further gains in the past month. Contacts with retailers indicate that they remain optimistic about the outlook for retail sales.

Banking respondents reported continued increases in the demand for all types of loans. Although loan demand appears to be strong throughout the District, demand for loans in North Carolina appears to be especially brisk. Banking respondents reported no change in residential construction in their areas and additional increases in nonresidential construction. A large brick producer in the District recently announced major expansion plans.

Unfavorable weather conditions plagued District farmers throughout much of the 1972 crop season, lowering yields per acre and damaging fruits and nuts, especially peaches. Nevertheless, farmers' January-November 1972 cash receipts from farm marketings registered an 8 percent gain over a year earlier. Livestock receipts were up 9 percent, and those from crops 7 percent. Farmers' January plans for the 1973 planting season point to increases in feed grain and soybean plantings, and decreases in cotton and wheat.

District businessmen and bankers remain optimistic about the general economic outlook. More than 50 percent of the banking respondents expect an improvement in business activity in their areas in the immediate future.

SIXTH DISTRICT - ATLANTA

Businessmen remain confident about the near-term outlook. The word "boom" is being used more often in describing current conditions. Residential construction may be weakening, but much commercial and industrial construction is planned. Labor shortages are reported in central Florida. A shortage of natural gas has caused some temporary plant closings.

Residential construction may be leveling off. In recent months, there has been a reduction in announcements of new projects. In Mobile, a decline in residential construction is reported, especially in the multi-family area. Along the Mississippi Gulf Coast, hardly any housing starts have been reported in the \$18,000 or below category because of high foreclosures on inexpensive homes. Apartment and condominium starts are predicted to decline in the Nashville area. One of the few new residential projects announced recently concerned possible development of expensive homes and condominiums on an island off Georgia.

Commercial construction remains very strong. Plans for a \$35 million office building have been announced for a site opposite the Federal Reserve Bank of Atlanta. Sears will build a \$30 million catalogue center in Jacksonville. This huge facility will employ 1,000 initially and 2,000 eventually. A \$28 million Federal building and an \$18 million hotel have been announced for Nashville. Hospital expansions totaling \$14 million are planned for cities in east Tennessee. An \$8.5 million office building is planned for Orlando. A sharp increase in retail sales is reported to be the reason for announcements of new shopping centers in the Mobile area. The drugstore division of a nationally known retailer will open at least ten outlets in the Atlanta vicinity. Other announcements include: a

\$4 million motel near Atlanta; a 4-story office building in an Atlanta industrial park; and a shopping center in a north Georgia city.

Industrial development also continues at a rapid pace. An \$18 million glass manufacturing plant is to be built in east Tennessee. This plant should eventually employ 500. An Alabama utility will construct an \$18 million general services complex. There has been a rash of relatively small new plant and plant expansion announcements for middle Tennessee. Businesses are reported moving into central Florida at a rapid rate. An electronics firm plans to build a \$4.75 million plant near Tuskegee, Alabama. A major expansion is planned by Armstrong Cork at its Pensacola plant. Other announcements include: an electrical parts plant in north Georgia; a plant to manufacture containers in Atlanta; a plywood plant near Jacksonville; and a motor home plant in Alabama.

Florida's tourist industry is prosperous. Attendance is up 15 to 18 percent over a year ago at Walt Disney World and other central Florida attractions. However, a glut of motel rooms is reported in the Disney World-Orlando area where thousands of motel rooms are currently under construction.

The only uncertainty in the employment picture is the effects of possible cutbacks at military installations. The Atlanta army depot will be laying off 1,300 civilian personnel, but an increase in employment at Atlanta's Fort McPherson is expected to partly offset this. Extremely wet weather in much of the District has hindered construction and other outdoor work and produced some temporary unemployment. Unemployment in the New Orleans area has been reduced by increased industrial and tourist activity and a pickup in offshore drilling activity. Unemployment rates in areas of central Florida are below 2 percent, and shortages of construction and agricultural labor are reported.

A Florida director reports that: "The citrus industry is slow in getting its harvesting operations going. Labor is the big problem. With what appears to be the largest crop in history, fruit pickers are short. The transit seasonal labor force does not appear to be as large as in previous years. The big problem: the crop has been late in maturing and as a result a large percentage is now maturing at a rapid rate, much faster and in such quantity that the present labor force cannot harvest before the crop starts falling from the tree."

A shortage of natural gas has caused some temporary plant closings in Louisiana and Alabama. Plants whose contracts with pipeline companies are about to expire cannot get assurances that they can renew. Supplies of jet and diesel fuel are also reportedly critically short in Louisiana.

SEVENTH DISTRICT - CHICAGO

The expansion in the Seventh District is vigorous and all but universal. The capital expenditure outlook is exceptionally strong. Reports on retail sales indicate that January continued the strong pace of December. Phase III has allowed greater flexibility, but most larger firms continue to act as though they are still under restraint. A consensus of informed opinion in this region indicates output is being pressed to capacity in many sectors, and that restrictive monetary and fiscal policies are desirable.

Larger firms are proceeding cautiously under the "voluntary" controls of Phase III. They remain uncertain of the new structure, and do not wish to be called to account by Congress or the Administration and have to "justify" their actions.

The fuel crisis reported in the January Red Book worsened in the next 10 to 12 days. Shortages of natural gas and fuel oil were hampering production. The greatest concern was over supplies of diesel fuel that threatened to reduce intercity truck traffic significantly. In the past two weeks, however, the fuel crisis has receded. Partly, the improvement reflected steps taken to direct supplies to areas where shortages were most severe, and partly the greater flexibility in pricing permitted after January 11. Most important, however, was the turn from abnormally cold to unseasonably warm temperatures. (Pussy willows have been seen sprouting in the Chicago area.)

The fuel problem has not disappeared and a critical situation is expected again next winter; perhaps even in the next several weeks if the weather changes. Gas utilities have received permission to refuse

additional commercial and residential customers. Despite an 8 percent increase in prices of distillates, prices of imports are still about one-fourth higher than U. S. prices and U. S. oil companies are not bidding aggressively for additional foreign supplies. Oil companies, moreover, are not entering into the one to two year contracts normally offered to truckers and other large fuel users. Some industrial construction projects have been cancelled because supplies of natural gas or oil cannot be assured.

The energy crisis would be much less significant if nuclear power was becoming available as scheduled. Availability of nuclear power, now and potential, has been adversely affected in three ways: (1) some operating plants are not allowed to produce at full capacity, (2) at least one plant that is ready to generate power is being held back by litigation, and (3) some projects "planned and sited" are not being constructed because of environmental disputes.

An informal survey finds the following industries operating at effective capacity, although not in all operations: paper, petroleum refining, machine tools, appliances, furniture, color television, trucks, recreational vehicles, electric motors, construction machinery, flat rolled steel, foundries, tool and die shops, lumber, gypsum board, insulating material, fertilizer, and certain chemicals. Some large firms complain that "our suppliers can't keep up with us". Some also worry about the inefficiency of 7-day weeks, and problems of quality control under "forced draft" schedules. The problem of estimating capacity utilization rates is very complicated and some published rates (such as those for oil refineries) are said to be much too low, for a number of technical reasons.



Capacity estimates in some industries include high-cost facilities that owners have no intention of activating.

Construction should be at a high level again in 1973. Residential construction, especially apartments, has been holding up well in this area. Prices of used homes are rising. The freeze on subsidized units did not surprise makers of construction machinery and building materials. Subsidized projects already approved will hold such construction near the recent pace for the next year. Contracts for manufacturing and commercial buildings have been very strong in recent months.

Job opportunities are excellent for skilled metalworkers, mechanics, draftsmen, engineers, accountants, stenographers, social workers, nurses, and other hospital workers. Demand for executives has increased substantially.

Teachers are in substantial oversupply. Nevertheless, teachers have been striking (illegally) for higher wages and other conditions. As a result of a long strike in January, the starting salary of Chicago teachers was raised to \$9800 for a 39-week year.

Many employers expect "reasonable" labor contracts in 1973. But the Pay Board recently approved a 13 percent pay raise for Chicago longshoremen, retroactive to last April. This contract calls for further increases of 11 percent in April 1973 and a 10 percent rise a year later. (The 1974 wage for these unskilled workers would be \$8 per hour, including fringes. Other unions are well aware of these terms.)

A January survey indicates acreage will be up 7 percent for corn and 5 percent for soybeans. These increases may be boosted by revisions in the wheat and feed grain programs that will provide more acreage for corn

and soybeans. Transportation bottlenecks are slowing movements of grain from elevators. Delayed unloadings at ports are partly responsible.

EIGHTH DISTRICT - ST. LOUIS

The Eighth District economy continued strongly upward in January according to a selected group of businessmen. Retail sales were well ahead of year-ago levels. Manufacturing output and sales continued to expand. Rising bullishness in the capital goods industries was especially noticeable. Construction generally remained at a high level for the winter season. Employment rose moderately, and businessmen reported very tight labor markets over most of the District. Demand for credit continued to outpace the growth of loanable funds causing upward pressure on interest rates. As a result of the January freeze, some farmers were able to resume crop harvesting, but many will experience substantial losses because of the poor harvesting season.

Retail sales in January were well above year-ago levels throughout the District. Leading department stores, however, indicated that sales on a seasonally adjusted basis have tended to level off since December.

Manufacturing continued strongly upward in January. A major chemical firm reported that its sales were 10 percent ahead of January a year ago, and that sales of plastics and related products were up 12 to 15 percent. Sales of paint, coatings, and wallcoverings were also up sharply. Many firms cannot obtain the quantity and quality of raw materials desired. Pulpwood and semifinished products for the paper and paperboard industries were reported in short supply and being rationed. Similar shortages are also in prospect for light crude oil, a raw material for many chemical products.

Although sluggish until recent months, reports indicated that the capital goods industry is beginning to boom. Sales of electrical equipment for manufacturing firms and welding and cutting equipment for both domestic use and for export were up sharply.

Business investment plans are apparently being revised upward as a result of the rising levels of sales and orders. Whereas last year few firms reported plans for new capital investment, many now report plans for new plants and plant expansion.

While construction remained at a generally high level over most of the District, it was quite spotty, varying from very high to low, depending on the availability of building supplies and weather conditions. Residential building was reported at a relatively high level in all the major District cities. All types of construction was booming in northeast Mississippi, but unfavorable weather and material shortages have brought construction to a standstill in southeast Arkansas.

Employment was increasing throughout the District. Most manufacturing firms reported moderate increases in production workers, and some report additions for research and development purposes. The labor market remained very tight over most of the District. The unemployment rate in the District is generally well below the national average with the exception of St. Louis and Fort Smith. Businessmen reported an especially tight labor market in western Tennessee, and that unemployment was virtually nonexistent in southern Kentucky.

The District agricultural situation varies from very good to very bad depending on local weather conditions during harvest. Farmers were unable to harvest a sizable percent of their cotton and soybean crops in southeast Missouri and northwest Arkansas and may face major losses. In most other parts of the District, excellent crops have been harvested and sold at high prices.

Credit demand in the Eighth District has increased. Banks reported rising interest rates on all types of loans. Savings and loan associations

reported that inflows of savings had tapered off. Interest rates charged by savings and loan associations remained stable in January, although rates are expected to rise during the year.

NINTH DISTRICT - MINNEAPOLIS

According to bank directors' reports, some acceleration in price increases is anticipated as a result of the shift to voluntary compliance in Phase III. In general, District businesses have not experienced difficulties in hiring skilled labor. No immediate curtailment in District business activity is foreseen as a result of recently announced cutbacks in Federal programs. Due to temporary factors, the demand for short-term agricultural credit increased in the fourth quarter, and is expected to ease in early 1973.

The consensus among bank directors is that price increases under Phase III regulations will be somewhat greater than if the more restrictive Phase II rules had remained in force. A District manufacturer associated with the construction industry revealed that prices of inputs purchased by his firm have already risen since the imposition of Phase III. Furthermore, some unions negotiating with his firm have indicated a willingness to abide by the 5.5 percent wage guideline, while others plan to disregard it. Another director anticipates prices to rise, but so far his firm has not encountered any price increases. Unless the government effectively jawbones, in one director's view, Phase III will not hold down price increases.

Although isolated instances were cited, no widespread shortage of skilled labor exists in the District. A Duluth banker indicated that some skilled labor was becoming difficult to hire in his area, and a Montana director disclosed that in his area building trade workers were in short supply. Another director stated that experienced workers were not available in his area and employers were hiring younger and more

inexperienced workers. One director reported that his firm had not encountered any skilled labor shortages but noted delivery times of steel products had recently been extended.

The recently announced freeze on Federal subsidized housing and cutbacks in agricultural programs are not expected to have any immediate, pronounced impact on District economic activity. According to a telephone survey of District HUD officials, the freeze on subsidized housing should not affect District homebuilding in 1973, but could dampen residential construction in 1974 and 1975. Also, several directors reported the freeze on subsidized housing could curtail some future homebuilding in their areas. District farmers currently are enjoying a relatively high level of prosperity, so the cutback in farm programs is not expected to have any immediate serious impact on District agriculture. However, in a South Dakota director's opinion, the farm conservation programs have been quite successful and stopping these projects will be detrimental to his area. The termination of FDA programs announced in the President's 1974 budget, a Duluth banker indicated, could adversely affect northeastern Minnesota. In another director's view, the recently announced cutbacks in Federally supported construction projects could take the edge off many areas' expected expansion in business activity this year.

According to our latest agricultural credit conditions survey, fourth quarter demand for short-term agricultural credit at many District commercial banks advanced after declining earlier in the year. Part of this increase can be attributed to a dramatic increase in farmer spending in some areas, as farmers incurred expenses prior to January 1 in order to reduce 1972 income taxes. Also, District farmers strategically postponed marketings to defer income taxes until next year which delayed loan

repayments. These developments, however, are considered temporary and short-term agricultural loan demands are expected to ease in early 1973. Fourth quarter demand for long-term agricultural credit was quite strong and may even strengthen further in the first quarter.



TENTH DISTRICT - KANSAS CITY

A check of a number of Tenth District firms involved in the energy field elicited mixed responses regarding their capital expenditure plans. Petroleum refiners report no plans for increasing on-line capacity either in the immediate or near-term future. At the same time, electric power companies in the District will be adding considerable generating capacity as a result of completion of large capital projects begun some time ago, with further expansion planned over the next 3-5 years. Elsewhere, investment plans suggest optimism over the near-term outlook. For District farmers and ranchers, 1972 was their most prosperous year ever, and, while the first half of 1973 appears very strong for agricultural income prospects, sharply higher production costs will likely temper these gains somewhat. A reflection of strength in the farm sector was evident in loan demands at District banks in January. Demand was strong in most categories with increases reported in loans to farmers and particularly in business loans. Most bankers felt that the vigor of the current economic expansion, rather than the rise in interest rates from competing lenders, was the primary explanation for strength in loans. However, increases in competing interest rates were cited by some bankers as the cause of some minor time and savings deposit runoffs.

The hard winter's drainage of fuel supplies prompted inquiries regarding the capital expenditure plans of major oil producers and power companies. Tenth District petroleum refiners report no plans to increase plant capacity during 1973, nor any projects underway that will increase on-line capacity in the near future. Several refiners say that, while inadequate capacity is a major problem, it is directly related to the

lack of an assured crude oil supply. One of the refiners hopes to start construction on a new refinery within 3 to 5 years, but its location will depend entirely upon the availability of crude oil. Although refiners are not expanding, they are spending considerable amounts for pollution control and equipment replacement. Refiners explain part of the recent shortage of heating oils and gasses as being a consequence of price ceilings which discouraged production of these hydrocarbons in favor of gasoline. Increasing incidents of fuel oil shortages are appearing in the District as cold weather continues.

Despite shortages of petroleum fuels, electric power companies in the Tenth District continue to plan new facilities that will use natural gas as the primary fuel. Only one nuclear plant is being built in the District. Pollution abatement requirements have forced one power company to retire a coal-fueled plant. Capital projects to be finished this year will add between 25 and 50 percent to generating capacity, and continued expansion is planned over the next 3-5 years.

Judging from a check on the investment plans of other kinds of businesses in the District, increases over last year would seem to be the rule. The airlines are riding the business cycle, as are the aircraft producers. Some of the airlines are buying more planes than they ordered, thanks to a gamble to build speculatively by Boeing and others. Construction activity is expected to remain steady this year overall. These prospects are apparently good enough to encourage related businesses, such as suppliers of structural materials, to make capital outlays for expansion and cost reduction. Even where profits are severely constrained by competition, such as for a major metal mining-refining outfit operating here,

the outlook is evidently sufficiently optimistic to stimulate expenditures for expansion and replacement.

Recent farm income estimates indicate that District farmers and ranchers enjoyed their most prosperous year ever in 1972. Buoyed by sharply higher crop and livestock prices, District cash receipts from farm marketings grew to \$10.8 billion, a 14 percent gain over 1971. Heavily oriented toward the cattle industry, which experienced continued growth and stronger prices last year, District cash receipts outpaced the 10 percent growth rate for the nation as a whole.

In the coming months, the prospects for District farm income remain especially strong. On January 1, the number of cattle on feed was 5 percent above a year ago, and with prices averaging about \$8 per hundred-weight higher than January 1972, a significant boost in District income can be expected. Actually, the bright outlook for farm income encompasses nearly all sectors. Following the 5 percent spurt in December, for example, farm prices rose another 5 percent in January to a new record high. However, while this development will help to underpin the income prospects over the first half year, sharply higher production costs during the same period will temper the income gains in the District to some extent.

Loan demands were strong in most categories at District banks in January with increases reported in loans to farmers and particularly business loans. When asked whether the strength in business loans could be partly due to the rise in commercial paper rates, most bankers responded in the negative. District bankers pointed out that only their largest customers have ready access to alternative sources of short-term funds, such as the commercial paper market. One banker noted that even though the data appeared to suggest that bank borrowing became more advantageous

during January relative to use of commercial paper, this impression might be misleading. His bank, for example, had effectively increased the prime rate to 6-1/4 percent without public announcement, the official prime rate at that bank remaining at 6 percent. Most bankers related the strength in loan demand by farmers and businesses to the vigor of the current economic expansion.

Tenth District bankers are beginning to report time and savings deposit runoffs due to the increases in competing interest rates. So far the drops have been minor, and are not expected to become a serious problem unless interest rates rise substantially further.

ELEVENTH DISTRICT - DALLAS

The most recent indicators of economic activity in the Eleventh District show somewhat mixed changes. In December, the Texas industrial production index declined slightly and, although total employment in the five southwestern states continued to increase, the unemployment rates edged upward. Nevertheless, construction activity in the District rebounded in December and District department stores sales continued to rise in January. New automobile registrations declined slightly in December but were still well ahead of their year earlier pace.

The seasonally adjusted Texas industrial production index eased slightly in December from its record November level. Production in both the manufacturing and utilities sectors edged downward while mining recorded a slight increase. Within manufacturing, nondurable goods production was essentially unchanged, but durable goods output declined as sizable decreases were recorded in the production of stone, clay, and glass, electrical machinery, and furniture and fixtures. The drop in utilities output was the result of a reduction in the distribution of electricity, while the increase in mining was centered in the natural gas, and metal, stone and earth minerals industries.

Production in January was probably adversely affected by the weather as unusually cold temperatures reportedly caused mechanical problems that cut crude oil output in some fields. Temporary curtailment of natural gas distribution also forced some refineries to shift to other fuels, reducing output and efficiency.

Seasonally adjusted total employment in the five southwestern states rose in December for the sixth consecutive month. Nevertheless, growth

in the labor force outstripped the gains in employment, causing the unemployment rate to edge up to 4.1 percent from 4 percent in November. Manufacturing employment was particularly buoyant as both the durable and nondurable goods sectors reported strong gains from November. Nonmanufacturing employment experienced a more moderate increase despite a sizable rise in service employment.

Construction activity in the five southwestern states, as measured by the value of contracts awarded, rebounded slightly in December, ending a three-month decline. Residential building fell for the fourth consecutive month, reaching the lowest level of activity since February. However, a sharp increase in nonresidential building and a more moderate increase in nonbuilding construction more than offset the residential building decline. The cumulative value of contracts for the District states for the 1972 year was nearly a fourth higher than in 1971.

Sales of department stores in the District continued to show year-to-year gains in January. In the five metropolitan areas for which data are regularly published, San Antonio and Houston showed the largest gains over a year ago, while Austin, El Paso, and Dallas recorded more moderate increases. The number of new automobile registrations in the four largest metropolitan areas of Texas--Dallas, Forth Worth, Houston and San Antonio--fell slightly in December, but were still ahead of their pace a year ago.

Agricultural activity slowed in late December and early January due to unfavorable weather conditions, and there was light freeze damage to winter crops. With the return of milder weather in recent years, most crops have recovered, and the cotton harvest is now about 90 percent complete. The unusually cold weather also resulted in higher than normal

livestock losses. Subsequent heavy supplemental feeding added further to the problem of soaring prices of livestock feed. High feed costs are also of major concern to dairymen.

TWELFTH DISTRICT - SAN FRANCISCO

Economic activity is maintaining a steady rate of growth in the Twelfth District. Consumer spending is strong, and construction expenditures are still high even though a decline is expected later in the year. Phase III of the Economic Stabilization Program is generally well accepted, despite some uncertainty as to its effectiveness. The consensus of our directors is that controls of some kind are needed for 1973.

After a record level of retail purchases in the last quarter of 1972, consumer spending is somewhat lower but still quite strong. Retailers throughout the District are optimistic about 1973 prospects, although profit margins are not satisfactory on some lines of business. One director thinks that sales of automobiles and other consumer durables will be weaker later in the year. However, the large amounts of tax refunds expected in the first quarter are favorable factors in maintaining consumer expenditures.

Construction activity is still at a high level but it is expected to turn down later this year. A major manufacturer of builders' hardware reports that sales currently are high, and no downturn is apparent in orders as yet. A favorable factor for housing demand is the continued inflow of funds to savings and loan associations which has kept mortgage rates stable. On the other hand, the reduction in Federal housing subsidies is expected to curtail residential construction. One large bank foresees a 20 percent reduction in housing starts in California.

Many agricultural prices are expected to remain near present levels, but cattle prices may be even higher. On the other hand, several directors think that wheat prices may be lower because of the increased



acreage of the coming crop; one director suggested the wheat crop might be 20 to 30 percent larger this year because of the relaxation of acreage allotments and this could lead to a large wheat surplus. Similarly, increased production of potatoes is expected to result in lower potato prices.

The rate of economic expansion is highest in Idaho and the Pacific Northwest which are states benefitting from the strong demand for timber and agricultural products. The greater production at the Boeing Company also is helping the Washington economy. In California, one bank forecasts that the growth rate in that state will be satisfactory, but it will be below the national trend. Reduced Government employment and an expected mid-year slowing in construction and certain classes of durable expenditures are reasons for this forecast. The San Francisco Bay area in particular is likely to experience a slower growth rate. Our directors accept the need for continued controls, but there is considerable variation in their assessments of the impact of Phase III. Some welcome the loosening in controls from those of Phase II, especially since continuation of the previous constraints would have caused increased distortions and inequities. Some think that the new controls cause too much uncertainty by their vagueness or that they will not be very effective. Most of the concern centers on the impact on wage settlements during the coming year. The consensus seems to be that, even though Phase III is less restrictive, controls do help in restraining wages.

The forest products industry seems to be particularly sensitive to the new controls. The industry price structure is already distorted by imports and strong demand. In this industry, the behavior of the small time producers, who are not controlled, probably will determine

now how prices will rise. There may be problems, but prices are expected to level off after an initial surge. Phase III may also permit higher wage settlements since forest products unions are likely to press for wage increases above the 5.5 percent guidelines. On balance, Phase III is described as creating a better atmosphere for investment in the industry.

Interest rates, with the probable exception of mortgages, are expected to rise. Long-term rates are being held down by various non-market factors, but short-term rates are likely to rise more than was expected earlier this year. An increase in the present 4 percent rate on passbook savings is a possibility. Demand for business loans and consumer credit is high in most areas.