# SUMMARY OF COMMENTARY ON CURRENT ECONOMIC CONDITIONS BY FEDERAL RESERVE DISTRICTS

January 1985

TABLE OF CONTENTS

# SUMMARY*

The economic expansion continued in most districts. The pace of recovery, although slower than early in the year, was moderately strong at year end. Retail sales activity during the holiday season was satisfactory and, in some cases, better than expected. Home sales and construction activity appeared to have rebounded significantly in response to declining mortgage interest rates. Manufacturing, employment and output continues to grow in most districts and manufacturers are reportedly optimistic about future sales prospects. The major sources of weakness appear to be agriculture and the mining and minerals industries. Overall, however, most districts report favorable trends in unemployment and continued low inflation.

## Construction and Real Estate

In sharp contrast to reports of just a month ago, most districts report increased strength in home construction and sales activity. The recent decline in mortgage interest rates is credited with fueling this turnaround. Only Chicago, Minneapolis and St. Louis report continued significant weakness in housing activity. Nonresidential construction activity also is reported to be at satisfactory levels in most districts. Some overbuilding and weakness in commercial rental markets is reported by New York, however.

---

*Prepared at the Federal Reserve Bank of San Francisco.

Manufacturing and Industry

Manufacturing employment and output growth was reported by many districts in December. Major sources of strength include the automobile, aerospace and electronics industries. San Francisco and Atlanta also report improved conditions in the paper and wood products industries. Chicago reports cut-backs in year-end steel production, however, and manufacturing activity appears to be generally sluggish in Dallas.

Agriculture

Agriculture appears to be broadly weak. The continued strength of the dollar and heavy debt burdens have depressed product prices and affected adversely the financial conditions of many farms. San Francisco estimates that 15 percent of agricultural loans in California are currently nonperforming. Kansas City estimates that this percentage may be as high as 90 percent in some areas of that district. The new federal debt adjustment program appears to be having only limited success in offsetting these developments.

Consumer Spending

Retail sales activity over the holiday period was healthy in virtually all districts. Boston, for example, reports sales increases of 6 to 10 percent. In the Philadelphia district, retail sales were up 5 to 10 percent over December, 1983. A few districts -- such as Cleveland -- ascribe the strength of Christmas retail sales growth partly to unusual, pre-holiday promotional events and price-cutting. In most districts, however, retailers appear to be optimistic about future sales volumes as well.

## Finance

Loan demand generally reflected the upturn in economic conditions with reports of increased commercial and consumer lending. Mortgage rates have declined significantly and increased home sales have generated increased demand for mortgage debt. In New York, however, the rebound of housing has yet to be reflected in mortgage lending data. Normal seasonal borrowing patterns also needed to be considered in evaluating year-end financial activity. As Atlanta reported, year-end commercial borrowing often softens as the result of reduced inventory financing requirements.

FIRST DISTRICT - BOSTON

The expansion appears to have resumed in the First District. Retailers experienced reasonably satisfactory year-over-year increases in Christmas sales, although promotional activity reduced margins. Retail inventories are a little higher than desired. In the manufacturing sector, recent order experience varies considerably, with some firms reporting order increases, others flat order rates and a few decreases. However, all the manufacturers contacted have projected significant real gains in 1985. Manufacturing inventories are in line with sales, based on past experience; but several contacts are not satisfied with this performance and are pushing to lower inventory-to-sales ratios. There is no evidence of any pickup in inflation; recent price increases have been very modest and price expectations for 1985 seem to have moderated. Mortgage rates have been gradually falling for several months.

Retailing

Stores in the First District reported respectable but not spectacular sales increases over the preceding year in December and early January. Promotional activity reduced margins and inventories are somewehat above plan. Most merchants expressed optimism about sales growth in 1985.

Sales increases among the retailers contacted ranged from 6 to 10 percent above December 1983. The recent year-over-year increases are generally smaller than those recorded earlier in 1984, but most stores expected this because 1983 finished so strongly. Contacts with affiliates or branches in other parts of the country said New England stores showed the best performance.

Shoppers were very responsive to promotional activity and sensitive to value. One chain reported sales under plan everyday in December except for a big one-day promotional event. This event was so successful that the chain almost achieved its planned sales total for the month. In contrast, two other contacts said management decided against extraordinary promotional activity and settled for moderate increases in volume. Fine jewelry, cosmetics, menswear, furniture and other hard goods were the strongest performers; most apparel, shoes, and video/computer games lagged. Shopping was quite selective; while some stores did quite well, their neighbors saw very little traffic.

Manufacturing

Manufacturers are more positive about the outlook for 1985 than they were a month or two ago. Many of the firms contacted saw orders level off after last summer. In some cases, orders remain flat although still above year earlier levels. Other firms, however, have seen a resumption of growth and everyone contacted expects real gains in 1985. Capital goods, particularly for certain process industries, are one of the more notable weak spots. Among the products doing well are nonresidential construction materials and devices, automotive products and industrial automative products and industrial automation equipment.

Price increases remain very modest for both inputs and outputs. The firms contacted are resisting increases from their traditional suppliers and are exploring new sources of supply. The firms are also finding strong resistance to their own attempts to raise prices. One contact noted that his list price is up but the actual price is unchanged. Wage increases are expected to be moderate in 1985.

Inventory-to-sales ratios are fairly good by historic standards. However, several respondents are not satisfied with this performance and have programs to bring inventories lower. Firms are also reported to be keeping a tight rein on hiring. Capital spending in 1985 is generally expected to be the same as or higher than in 1984.

Several respondents reported improvements at subsidiary operations overseas. Two firms noted that business in Mexico has picked up considerably; Brazil was also mentioned as an area of improvement. Reports on European operations were mixed.

Mortgage Market

Mortgage rates eased in December. Commitment rates for fixed-rate mortgages fell 25-50 basis points in the month. Rates are about 100 basis points below September levels. Rates have also declined for adjustable rate mortgages.

# SECOND DISTRICT--NEW YORK

## Introduction

Economic activity in the Second District advanced at an uneven pace in recent weeks. Consumer spending strengthened during December and on into early January. The demand for new homes was also strong and residential builders are quite optimistic about their prospects in 1985. While overall employment reached record levels, district purchasing managers for the most part reported that production and new orders were unchanged in December. The absorption of office space remains slow in many areas with vacancy rates showing little improvement.

## Consumer Spending

On balance, December retail sales were strong in the Second District, despite some softness early in the period. Sales gains over December 1983 generally ranged between five and ten percent as area stores engaged in extensive advertising campaigns and heavy price markdowns. Retailers became apprehensive at the start of the month when spending slackened. As the holidays approached, however, sales picked up considerably and continued at a brisk pace well into January.

The inventory situation among District retailers was mixed at year-end. While most reported stocks at comfortable levels, some expressed the need to reduce excess inventories in the weeks ahead.

Construction and Real Estate

Residential construction activity remains strong. While the arrival of cold weather has slowed the rate of exterior work, interior subcontractors report a high level of activity even though this is usually their slack period. Optimism about the months ahead is high. One electric utility, for example, has already received more orders to supply connections for housing subdivisions this year than in all of 1984. In addition, in response to the heavy volume of customer traffic, prices of new homes in some downstate areas are reported rising by as much as ten percent. While lower mortgage rates have undoubtedly made homebuying more affordable, their recent decline does not seem to be a major factor in the strength of District construction.

The absorption of new office space remains slow in many parts of the District and vacancy rates in these areas showed little improvement. In northern New Jersey, Westchester and Fairfield Counties, observers report that markets are relatively soft and leasing activity is slow. Manhattan is a major exception where demand continues strong in midtown and some large space users recently signed leases in the downtown area. Another exception is Long Island where commercial leasing is described as fairly brisk with a resultant reduction of inventories there.

Business Activity

The pace of the business expansion in the Second District leveled off during recent weeks. In December the majority of purchasing agents reported no change in business conditions while the percentages reporting gains or declines in new orders were virtually offsetting. Inventories are considered to be at satisfactory levels, particularly after several weeks of paring by

Buffalo area firms. District businessmen are generally optimistic about the outlook over the next six months though some expressed uncertainty about the overall economy.

Plans for several new or expanded industrial projects have recently been announced. Among these are a record $554 million in capital expenditures scheduled by a Rochester manufacturer for 1985, a $200 million natural gas co-generation plant to be built in Syracuse, and a $125 million expansion by an upstate paper maker. In addition, the Port Authority of New York and New Jersey and the New Jersey Economic Development Authority plan to convert several buildings which were abandoned when firms left Yonkers and Elizabeth into two new industrial parks.

Employment continues at record high levels in New York and New Jersey. Moreover, during 1984 New York City had its largest employment gain since record-keeping began in 1950. December unemployment rates were at or below the national rate of 7.2 percent in both New York State and New Jersey.

## Financial Developments

Despite the continued strength of district housing activity, some upstate commercial banks report no upturn as yet in the demand for mortgage loans. Seasonal elements have been suggested as an explanation of at least part of the sluggish demand. In some areas, relatively high unemployment rates have also been cited. Banks seem confident, however, that continued lower mortgage rates should reverse this pattern in the first quarter of 1985.

# THIRD DISTRICT - PHILADELPHIA

The Third District economy appears to be healthy at the start of 1985. Manufacturing is generally stable, the retail sector is on target after finishing 1984 above plan, and the financial sector reports substantial loan growth. Real estate continues to benefit from declining interest rates.

The outlook contains prospects for further expansion in almost all sectors. The majority of manufacturers see growth ahead although they are cautious. Retailers anticipate sales gains of over 10 percent, and plan to take measures to avoid a profit squeeze. Bankers project that continued confidence in the economy will propel loan demand. The only exception to the generally upbeat outlook may be in real estate, where the current tax law reform proposals are dampening the demand for investment properties. Purchases of owner-occupied properties are expected to continue to grow, however.

## MANUFACTURING

Stability is the watchword of Third District manufacturers according to the January Business Outlook Survey. While 27 percent of the executives polled say business is up, over half of the survey respondents report no change in industrial activity, and 17 percent note a decline since December.

The performance of the specific indicators support the general reports of respondents. Thirty-nine percent of the respondents say inventories are down, the result of flat new orders and increased shipments. A majority of manufacturers report no change in producers' backlogs, employment, the length of the average workweek, or delivery times.

Looking ahead, manufacturers appear to be optimistic in their outlook, but reserved in their actual plans to prepare for further growth. Over 60 percent of the manufacturers polled foresee their businesses expanding further in the next six months. Widespread growth in new orders and shipments is projected, but respondents have no plans to add to either inventories or payrolls. They may lengthen working hours though, should demand for their products increase.

Industrial prices have remained steady. Over two-thirds of the survey respondents say there has been no change in input costs from last month, and three-quarters have held their prices at December levels. As for the future, prices are expected to rise in the first half of 1985; almost three-quarters of the respondents forecast higher costs and about half plan to charge more for their finished products.

RETAIL

Retail sales are right on target so far this year, after what some local retailers have called a "scary" holiday season. A rush of activity in the last week before Christmas helped area merchants to exceed their selling expectations for the season and end the year with sales up 5 to 10 percent over December 1983; heavy promotion was largely responsible for the surge in year-end figures. Inventories are "clean" and at desired levels as retailers prepare to take inventory and receive new spring merchandise.

Healthy growth is expected over the next six months with sellers anticipating sales advances of 10 to 15 percent over last year's levels. They expect to have to continue to rely on sales promotions to achieve these gains, however. As a result, some retailers are planning to undertake strong cost-cutting measures in order to avoid a profit margin squeeze.

FINANCE

Area commercial banks are registering pluses in both wholesale and retail lending. Commercial loan activity is up with growth ranging from satisfactory (4 percent) to exceptional (25 percent) on a year-over-year basis. Economic expansion through mid-1985 is anticipated, leading lenders to project further C&I loan expansion of about 10 percent over current levels. Substantial increases in retail lending also have been experienced by Third District banks. Consumer loans are reported to be up 20 percent or more over year-ago levels and bankers expect continued strength in consumer confidence to lead to gains of about 10 percent over present levels by July.

The prime rate was cut at area banks to 10.5 percent on January 16. Bank economists see the potential for another rate drop due to low inflation and the strength of the dollar, but they say the prime subsequently may be pushed up to 11 percent by the end of the second quarter of 1985 as the economy picks up steam. They expect the federal funds rate to increase to 8.5 or 9 percent by July.

REAL ESTATE

Area realtors report continued strength in residential real estate sales in mid-January. Townhouses, in particular, are doing well in the City of Philadelphia, with sales over 10 percent better than last year. The surge in home buying has been attributed almost solely to declining mortgage interest rates. Thirty-year fixed-rate mortgages are being offered for as low as 12-1/2 percent and adjustable rate loans, negotiable after one year, for 10 percent, depending on terms. Realtors note that purchases of residential properties for investment purposes are just about dead. The tax law reform proposal has encouraged a "sit and wait" attitude in investors looking for tax shelters.

# Fourth District - Cleveland

## Summary

The Fourth District economy shows signs of sluggishness with no clear direction. On the upside, there are reports of strong gains in retail sales, especially of autos. Employment rose in December, and commercial bank loans increased in all categories, especially the consumer sector. On the downside, manufacturing output, orders and backlogs fell in December and manufacturing employment was unchanged. House builders remain extremely cautious, although other housing market participants' outlooks have been bouyed by interest rate declines. The coal mining, and oil and gas exploration industries are depressed.

## District Labor Market Conditions

Labor market trends in the District were mixed in December. Ohio employment (s.a.) rose in December after having fallen in October and November. However, unemployment (s.a.) also rose in December after falling in November. The unemployment rate in Ohio rose in December to 9.1% (s.a.) from 8.7% in November. Unemployment rates (n.s.a.) in ten metropolitan areas in the District ranged in November from 6.5% in Columbus to 15.6% in Wheeling. An index of leading indicators of employment in Pittsburgh has shown little change since last February, suggesting that employment there will not grow further.

## Retail Sales

Fourth District retail sales registered a further strong gain in December. Some auto dealers report sales were up as much as 28% over a strong year-earlier period, apparently aided in part by an easing in inventory constraints, and the strong sales gains have continued into early January. Representatives from area department stores report that December sales more than met expectations. Year-over-year gains were in the 7% to 11% range. Some merchants report extensive price reductions while others say price reductions were quite limited. Most analysts attribute the fourth quarter rebound in sales to a still-positive consumer attitude. However, an economist at one department store chain noted that he expects retailers to continue trimming inventories over the first quarter of the year.

## Manufacturing and Energy

Manufacturing activity in the District shows signs of weakening, and the energy sector is depressed. Surveys of production managers in Cincinnati and Cleveland show production, new orders and backlogs fell in December. However, there are some indications that the falloff may be seasonal, and manufacturing employment was unchanged. In Cleveland, a substantial majority of respondents expect business to be better in the first half of 1985 than in the last half of 1984. Price pressures continue to be moderate. Vendor delivery performance continues to improve. Raw material inventories are declining slowly, and finished goods inventories are generally flat, except where order declines have resulted in some involuntary accumulation. Contacts continue to report very conservative policies on inventory accumulation.

Many firms in this District report continued strong competition from imports is restraining price increases and keeping profit margins small. A containers producer reports a continued shift from glass containers to plastic and paper substitutes. A producer of personal safety equipment used in industry had strong earnings in 1984 and expects a strong 1985. Some chemicals factories in southern Ohio are operating at capacity.

Major steel producers report some pickup in orders from the automobile industry and steel service centers, but transactions prices remain well below published prices because of excess domestic capacity and strong competition from imports. Steel inventories remain high. A steel mill in western Pennsylvania recently announced a 500-worker layoff.

Capital goods producers have mixed views on the report that domestic firms plan a 6.8% real increase in expenditures on plant and equipment in 1985. One firm, which expects a recession to begin no later than the second half, expects the real change in business fixed investment to be negative, partly because of uncertainty about tax law changes. Another firm thinks the figure is on the mark while a third expects a 10% real increase.

Coal mining remains a depressed industry. Many workers are on a three-day week, and improvement is not expected until late-1985 when excessive stockpiles will have been worked down. Falling oil prices have depressed oil and gas drilling activity in this District.

## Housing

Except for home builders, housing market participants in this District report continued improvement in their housing-related businesses and cite declining mortgage rates as the primary cause. The consensus is that housing activity will rebound at a slow, sustained pace until mid-1985. Housing market participants expect that the rate on fixed rate mortgages will decline as much as another 50 basis points, but won't fall below 12%.

Realtors, who remain the most optimistic among market participants, experienced further improvement in December in listings and contracts closed. There are some signs that the move-up market is reversing its flat performance of 1984. Realtors' optimism is reflected in one District firm's plan to open three times as many new franchises during 1985 as in 1984.

Mortgage lending volume is expanding because of lower mortgage rates, and one lender reports that loan volume in December was 50% higher than a year earlier. Lenders anticipate that the resumed popularity of the fixed rate mortgage will persist until the second half of 1985, when they expect rates to rise. Lenders will sell most new fixed-rate mortgages in the secondary market if commitment rates are favorable.

Builders remain extremely cautious. New orders remain sluggish, and buyer traffic, which a major builder reports was up 11% nationally in December, fell 35% in Ohio. Because of poor earnings in 1984, builders are positioning to minimize downside risk.

Commercial Banking

Loan outstandings in all major categories increased at Fourth District banks during the past month. Contacts report that consumer loan demand has been quite good, and it should remain relatively strong on the strength of new car sales. Business lending has picked-up somewhat, and contacts are generally optimistic about future demand for commercial loans. One banker, however, thinks that recent business loan demand has been rather weak and doesn't expect an improvement before March. Deposit growth has been moderate for both transaction and nontransaction accounts at District banks in the past month.

# FIFTH DISTRICT - RICHMOND

## Overview

There appears to have been a lull in industrial activity in the District over the past month, although employment levels remain firm. The District economy seems fundamentally strong. Retail sales turned in a strong showing, better, by all indications, than national data suggest. Construction activity is also quite strong, but unusually good weather may be a factor in that sector. Yet, manufacturers seem to have experienced a dip in orders and shipments, and inventories also declined over the past month. Heavy discounting by retailers gave a significant boost to unit sales, and left their inventories relatively low as well.

## Manufacturing

Activity in the manufacturing sector is clearly less robust than in recent months. The deterioration of the activity in the textile and apparel sector is continuing, although the pace may have slowed somewhat. Import competition continues to plague the industry and is of major concern to industry participants and observers. Other industries have not recently offset the weakness in the textile and apparel industries as they had in the last few months, however, and orders, shipments, and order backlogs dipped broadly around year end. Manufacturers also report weakness in prices.

Whether because of the recent decline in business activity or for other reasons, attitudes and expectations among District manufacturers also seem to have deteriorated of late. There is spreading concern over inventory levels and over excess plant and equipment capacity, although there is virtually no sentiment for changing current expansion plans. The outlook is also somewhat weaker than in recent months. Although manufacturers, on balance, seem to expect little change in output at their own firms, there is a slight preponderance of sentiment favoring declining activity at the national and market levels over the next six months. Despite these losses in activity and changes in attitudes, however, employment seems to be making further gains, at least apart from the textile and apparel industries.

Coal production bounced back shortly before year end, and currently seems to be holding near the very strong year earlier levels. Also, coal shipments and imports generally are still keeping the District ports and other transportation sectors quite busy.

## Consumer Activity

Retail sales also finished the year on a strong note as consumers responded aggressively to sales promotions and discounting. Month to month gains of eight to ten percent were not uncommon in the District. This surge of selling drew inventories down below normal levels at many stores, but there does not seem to be any sense of urgency about rebuilding stocks. Many retailers apparently are relieved that inventories are down so far, and are inclined to wait further developments before making restocking decisions. While there is no clear indication of current pricing policies in the retail sector, there are some signs that dealers are attempting to rescind the discounts offered earlier.

## Construction

The construction sector remains a high point in Fifth District activity. Commercial and industrial building, still strong in the larger metroplitan areas, is spreading to the smaller cities in the form of office and industrial parks. Industrial building seems to have picked up recently, and planned construction, particularly for plant expansions, appears even stronger, despite the flagging optimism noted in the manufacturing sector. Residential sales and construction are also said to have rebounded, although even at the recent trough, activity was substantial. In addition, early readings on building permits suggest continued strength in residential construction into spring.

Agriculture

Agricultural economic conditions in the Fifth District will likely remain weak into 1985. Although District farmers will probably continue to fare better than their counterparts in many other regions of the U.S., the projected tighter U.S. net farm income and cash flow levels seen for 1985 are expected to adversely affect financial conditions in agriculture in the Fifth District. An income downturn for farmers this year will reduce the growth of farm loans, and hamper the serviceability of existing debt.

Agricultural bankers continue to be wary of farm foreclosures as they perceive the market for farmland to be extremely thin. As a result, bankers are generally favoring restructuring of farm debt whenever it appears to be a realistic solution to the cash flow problem facing farmers.

Expectations

The recent fading of the optimism previously seen around the District appears to be related to uncertainty concerning such things as the trade deficit, the budget deficit, and the tax reform proposals rather than to current District business conditions. Business decisions concerning plant expansions, employment, and so forth continue to point to stable improved levels of activity. The exception, of course, concerns inventories, particularly at the retail level.

## SIXTH DISTRICT - ATLANTA

The southeastern economy continued to strengthen toward the year's end. Employment growth was noted even in the more depressed areas of the region. Consumer spending, which had been disappointing in the mid-holiday-shopping period, revived toward Christmas, and post-Christmas sales activity also was brisk. Commercial construction remains active, and the pace of home building quickened, owing to further declines in mortgage interest rates. Bank lending to consumers increased in early January, suggesting that demand for automobiles remained strong. A mild winter relative to the rest of the country boosted tourist activity. On the other hand, real estate and business lending by banks was soft. Many crop farmers, adversely affected earlier by heavy rainfall and flooding, are now suffering from low prices for corn and soybeans.

Employment and Industry. Labor market conditions improved in November. Unemployment rates broke out of a four-month plateau and declined in four of the six District states. Rates in Alabama and Mississippi, still at double-digit levels, moved up slightly more in November. Job markets continued to brighten in Florida and Georgia and welcomed improvements also occurred in Louisiana and Tennessee.

Strength in paper, petrochemical, defense and aerospace industries overshadow lingering weaknesses in import-sensitive sectors. High operating rates have encouraged some paper plants to expand. Demand for linerboard and bonded paper is particularly strong, and prices are firm. Activity in Louisiana's petrochemical industry continued to brighten as evidenced by higher levels of offshore drilling, growth plans for capital spending, and reductions in inventories. Defense-related spending and aerospace production continue to augment the region's economic activity. Defense-related work doubled at Oak Ridge Laboratories from 1983 to 1984, and spokesmen expect a 25 percent improvement in 1985.

On the other hand, several important sectors have experienced little improvement of late. Employment declined further in the region's steel and textile sectors during December. Although falling long-term interest rates have aided home building, inflows of Canadian lumber are still a concern of the region's lumber and wood product producers.

Consumer Spending. Holiday shopping in the Southeast matched or surpassed sales growth nationally, according to a survey of District retailers. Consumer spending was particularly brisk for video-cassette recorders, microcomputers, television sets, and microwave ovens. In contrast, unseasonably warm weather through December depressed sales of winter clothing. Merchants also reported narrower profit margins due to intense competition from new stores. Post-Christmas efforts to trim inventories were apparently successful; however, deep discounts were required to move merchandise. Regional merchants expect sales growth to moderate in 1985. Automobile dealers were pleased with their sales performance in 1984, and they are decidedly optimistic about prospects for early 1985.

Construction. Residential construction reversed a decline early in the fourth quarter as mortgage interest rates eased and a feared plunge in economic activity failed to materialize. Home builders expect further declines in mortgage rates to extend the recent strength in building through the first half of 1985.

Nonresidential construction continued to grow in early January. Although property managers consider the region's office market to be overbuilt, recent increases in rental rates should provide some relief. Shopping center construction continued to increase in December even though merchants contend that competition is already intense.

Financial Services. Overall loan demand at large commercial banks followed its normal pattern and tapered off in November and December for both consumer and business loans. Contacts report that consumer loans have picked up in early January, with a large proportion going to finance purchases of automobiles. Business loan demand was soft, reflecting reduced borrowing to finance inventories. Real estate lending by commercial banks was below normal, and mortgage loan commitments from savings and loan associations were weak earlier in the fourth quarter.

Tourism. Unusually pleasant weather in the region gave winter tourism an added boost in the final months of 1984, and contacts report bright prospects for coming months. Attendance at tourist attractions generally exceeded expectations. Hotel/motel revenues increased vigorously in most southeastern states, and occupancy rates continued to show strength. Passenger volume also grew at the region's airports.

Agriculture. Conditions in the southeastern agricultural economy maintained typical diversity in 1984. Crop farmers, whose cash income flourished a year ago, fared less well in 1984 as commodity prices declined. Conversely, total revenue increased for livestock and poultry producers in 1984. The poultry industry showed considerable improvement as high prices accompanied increased production. Income to pork farmers also grew sharply while the dairy and beef cattle industries experienced declines.

## SEVENTH DISTRICT--CHICAGO

Summary. The flat trend which has characterized economic activity in the Seventh District since last spring continues in early 1985. However, analysts with District firms do not anticipate a recession. Despite robust auto and truck sales and output, most sectors important here are about holding even, some at very depressed levels. There is little hope that the gap in the region's performance relative to the nation that developed in the 1980s will be ameliorated in the near future. Total employment has barely increased since last spring, and some lines, including farm, construction, and mining equipment, medical care, and financial institutions have cut staff and/or have scheduled extended layoffs. Continued gains in the value of the dollar have defeated strenuous cost-cutting efforts of District producers to regain a viable position relative to foreign competitors. Steel output ended 1984 at a low level, and District steel producers anxiously await effective agreements to restrict imports. Sales and orders for heavy trucks and trailers have softened from the good level of last spring, but remain fairly high. Office and commercial construction prospects in the Chicago area remain vigorous, probably because of favorable tax treatment. General merchandise sales in late 1984 disappointed some large chains, and price cuts to move excess stocks have adversely affected profits. Price competition in cement, steel, paperboard, oil products, and airline fares is also intense. Depressed conditions in District agriculture are increasingly burdensome. Farmland values declined 5.5 percent in the region in the fourth quarter, and are down 27 percent from 1981 highs, with further declines probable.

Labor Markets. Jobs are hard to find in the Midwest. Through November, total payroll employment in the five-state area had risen less than 4 percent (S.A.) from the recession low in December 1982, and less than 1 percent since last April, only half the U.S. rate. Reports of new layoffs, extended shutdowns, help-wanted ads, and reports of hiring intentions suggest no improvement since November. Manufacturing employment has been about unchanged since last spring, while growth of nonfactory jobs has been very small. Despite favorable press reports by university PR departments, many of last year's college grads, often with good records from top-rated schools, have failed to find suitable employment. Others hired in recent years are out looking again. Job freezes and efforts to cut surplus staff are almost universal, including state/local government, hospitals and medical supply producers, commodity dealers, and financial institutions--sectors that were hiring steadily in the 1970s. As a result of the collapse of the video game craze (with output centered in Chicago) employment in area firms has dropped from 7,000 to 1,400 since 1982. A recent report of 100 job openings at the main Chicago post office caused a mob scene of thousands of would-be applicants. Wage freezes and give-backs, often fiercely disputed, are occurring in a number of sectors, especially meat packing and food retailing.

Capital Equipment. Construction and farm equipment producers remain under severe stress, with an historic consolidation and retrenchment underway. Output of farm equipment in 1985 is expected to fall from very low levels, even if sales hold up, because inventories of a leading producer will be liquidated. Very weak mining activity means virtually no demand for equipment. Industrial markets for diesel engines (except trucks) remain soft.

Competition from foreign producers, in domestic markets and abroad, remains a severe problem for a wide range of producers, in large part because of the high value of the dollar, but also because of poor sales worldwide. The leading construction equipment producer (with a commanding position worldwide a few years ago) has had three straight loss years and laments "our dramatic cost reduction efforts are being offset by the soaring dollar". Most investment is heavily oriented toward quality assurance and elimination of jobs. Often machines and components for these programs are imported.

Motor vehicles. Auto sales improved in December as shortages of popular models eased. Further inventory building is planned in the first quarter of 1985. Major producers expect small gains in sales in 1985 from last year's high level. Auto industry employment remains well below 1978 levels, but new workers are being hired "off the street" at some District plants for the first time since the late 1970s, as workers on extended layoff have been rehired or exhausted their eligibility for recall. Orders for heavy trucks and trailers have slipped somewhat since last spring, but remain high. Heavy truck sales in 1984 were 80 percent higher than the recession low in 1982, but well below the 1978-1979 pace. Deliveries in 1985 are expected to be near 1984 levels.

Steel. Fourth-quarter steel output at District mills was lowest in 1984, and output fell more than usual at year-end as customers sought to cut inventories. A small rise in steel consumption is expected in 1985. Steel for motor vehicles will remain at high levels, and bids on fabricated steel for office buildings continue vigorous. Orders from equipment manufacturers have increased only moderately. Questions regarding the timing and effectiveness of "voluntary" import restrictions overhang the 1985 outlook for domestic production.

Nonresidential Construction. Contracts for nonresidential building (floor area, F.W. Dodge) in the five states were up 33 percent in 1984 from a year earlier, but 36 percent below 1979. The U.S. total was up only 19 percent, but within 13 percent of 1979. A surprising number of large office buildings are under construction or planned for downtown Chicago, and office and retail development continues vigorous in high-growth suburbs. Commercial construction activity may be artificially stimulated by the possibility that rapid depreciation for tax purposes will be ended. Car and truck makers plan new plants, mainly in Michigan and Indiana, with states and municipalities competing in offering costly incentives to promote local sites. Rehabilitation work continues at a strong pace, also encouraged by tax breaks. Highway improvement work is expected to rise through 1985 and into 1986, largely depending on federal fund allotments.

Housing. Permits for District residential construction slipped in the second half of 1984. Declines in mortgage rates since mid-1984 improve prospects. In 1984, housing construction permits in the five states were up 11 percent, but were down almost 60 percent from 1977. Used home sales held up well in late 1984, aided by lower mortgage rates.

Retail Sales. General merchandise sales in December and early January were mixed, but mostly below expectations. Discounters performed best. Inventories are excessive despite reduced orders starting last summer. Aggressive markdowns have been common. The share of sales on credit has leveled, after rising in recent years. Delinquencies are up, but not "dangerous". Appliance sales were at record levels last year, led by a 55 percent surge in microwave ovens, half of which are imported.

# EIGHTH DISTRICT - ST. LOUIS

## Summary

Although lower than earlier expected, Christmas retail sales were strong, but inventory pressure held prices and profits down. Auto sales in 1984 were above 1983 levels and are expected to remain strong in early 1985. The construction industry anticipates increased activity if interest rates continue to fall. Business loans grew at a 16 percent annual rate in December, only slightly below the 17 percent rate for the year. The outlook for prices of most District agricultural commodities suggests another difficult year for farmers.

## Consumer Spending

District retailers report smaller sales volume increases for December than those realized in the previous year. Large inventories required retailers to mark prices down heavily, potentially resulting in lower profit margins. Lower than expected Christmas sales in the Louisville area forced some retailers to carry larger than desired inventories into 1985.

Automobile sales ended the year above 1983 levels. District dealerships reported increases in both new and used car sales for 1984, though new car sales experienced larger gains. December sales were slightly above the December 1983 level. Dealers are attempting to build inventories, but do not expect 1985 sales volumes to reach 1984 levels.

Business Activity

General business activity declined in Arkansas at an annual rate of 2.6 percent in December, based on preliminary calculations of an index of seven indicators. The decline follows a 4 percent increase in November. Business activity in Missouri maintained its November growth rate of 5 percent.

Orders for scrap iron and metal were up in January, implying a small increase in steel production; scrap prices rose 5 percent. The movement to limit steel imports has spread cautious optimism in this industry.

Construction

Single-family housing construction continued the decline that began in May. In the St. Louis area, single-family housing starts for November and December were approximately 20 percent below the 1983 level. Respondents look for an increase in housing starts if the steady decline in interest rates continues. Multi-family housing construction continues at a pace substantially above that of 1983.

Banking and Finance

The volume of total loans and leases outstanding at large weekly reporting District banks increased at a 30 percent annual rate from November to December (not seasonally adjusted), nearly twice the growth rate for the entire year. Consumer lending, bolstered by the strong seasonal influence, grew at a 40 percent annual rate for the month compared to 11 percent for the year. Loans for business and real estate purposes, however, grew at rates of 12 and 6 percent respectively, about half the rates for the entire year.

Lending trends at small District banks differed from those of the large banks. Total loans grew at an 11 percent rate in December, slower than the 15 percent growth rate for the year. Business loans, however, grew rapidly in December, increasing at a 25 percent rate compared to the year's 11 percent rate. Consumer loans at small banks grew at a 19 percent rate in December, only slightly faster than the 17 percent growth rate for the entire year.

An informal survey of the five largest banks and five largest savings and loans in the St. Louis area found that only one bank had adopted the newly-reduced $1,000 minimum deposit level for Super-NOWs and MMDAs. Two of the institutions stated they would later adopt a tiered rate structure offering lower rates for lower deposit balances. The remaining respondents had not yet publicly announced their intentions.

## Agriculture

The status of Eighth District farmers can be summarized by comparing current cash prices for major District products to prices one year ago. Despite a 15 percent increase in export volume, corn prices have fallen about 20 percent. Soybean exports are running about 15 percent below last year's volume and prices are down 25 percent. Cotton exports are holding near the previous year's volume but prices are down about 15 percent. Abundant cattle supplies are expected to prevent any significant price increases this year. Only hog producers, who expect to see substantial price gains by year-end, might look to 1985 with optimism.

# NINTH DISTRICT - MINNEAPOLIS

The Ninth District economy has grown at a modest rate in the last few months. Employment conditions have remained stable, with hire-backs in mining offsetting new layoffs in manufacturing. Consumer spending, while not as strong as some merchants hoped, has generally surpassed the previous year's excellent performance. Encouraging signs have appeared in commercial and industrial construction. Financial activity has been normal for this time of year. But little improvement has occurred in the hard-pressed agriculture sector.

## Employment

Overall, employment conditions have remained fairly stable. The Minneapolis help-wanted advertising index barely changed between October and November. Unemployment remained low in major metropolitan areas of the district, including Minneapolis-St. Paul and Rochester, Minnesota, and Rapid City and Sioux Falls, South Dakota. In northern Minnesota, employment in mining-related activities did fall off sharply in November. But over one-third of the laid-off workers were called back in January, and more are expected to be called back in the coming months. Also, a new white paper mill will employ between 300 and 500 workers in the troubled Upper Peninsula of Michigan. Recently, however, two sizeable manufacturing firms laid off 500 workers apiece, one in St. Paul, Minnesota, and the other in Sioux Falls, South Dakota.

## Consumer Spending

District retail sales of general merchandise during the holiday season bettered 1983's excellent holiday sales, but not by as much as some merchants had expected. For example, one Twin Cities department store group expected better sales growth. A larger chain of stores in the same area, however, met its growth objectives and is continuing to do so in January. Inventories aren't excessively high at either chain. Similar reports come from other large cities of the district, including Sioux Falls, South Dakota, and Bismarck, North Dakota.

While regional auto sales dropped this December from the unusually strong levels of a year earlier, they picked up some in January. For example, one large domestic manufacturer reports that its district car and truck sales fell more than 20 percent this December, but still were better than in most years. Several of this Bank's directors note similar soft November and December vehicle sales in their areas of the district. Auto inventories have reportedly increased recently from generally low 1984 levels. But regional sales managers for domestic manufacturers report a big sales pickup early in January.

Housing activity also appears to have slowed and rebounded in the last few months. Twin Cities home sales fell off a bit in November from the pace of a year earlier. Primarily due to a reduction in multifamily buildings, the number of Twin Cities housing permits this November also did not reach its year-earlier level. The value of Twin Cities residential construction contract awards did increase strongly in November, though. Future permit figures should reflect this increase.

Adequate snowfall has helped district ski resorts attract tourist dollars this winter. Ski areas in Montana and the Upper Peninsula of Michigan report good skiing conditions.

Commercial and Industrial Construction

Commercial and industrial construction activity in the district has been robust lately. Minnesota commercial and industrial contract awards were about 50 percent higher this November than last. Three of the district's largest contractors report a recent pickup in activity, which they expect to continue. None of these contractors has had problems getting supplies. The most recent available data indicate that industrial vacancy rates have declined a bit in the Twin Cities. One Bank director notes that construction projects (including a new hotel) are really taking off in Rapid City, South Dakota; this area is benefiting from the needs of the military.

Finance

Deposits at Ninth District banks, thrifts, and credit unions each rose in December--altogether, at an annual growth rate of 15 percent. At the same time, at large district banks, commercial and industrial loans grew slightly slower and personal loans financing holiday expenditures grew much faster.

Agriculture

The district's gloomy agriculture picture has not brightened much lately, however. The Minnesota farm price index fell 2 percent in December, its fifth monthly decline in the last six months. This Bank's late December survey of rural bankers indicates that low farm income aggravated farmers' debt repayment troubles in the fourth quarter and that little or no improvement is expected early this year. This Bank's directors largely agree with that assessment, noting as well a continuing slide in farm land values. Falling land values are mainly responsible for an estimated $8.9 billion loss of Minnesota farmers' equity over the past three years. Cheap grain has helped improve the profitability of livestock operations, though.

## TENTH DISTRICT--KANSAS CITY

Overview. With the important exception of agriculture, modest improvement seems to characterize the Tenth District economy at the turn of the year. Although Christmas sales generally fell short of expectations, they were better than a year earlier and retailers are mildly optimistic about 1985 sales. Retail inventories are higher than desired and will be trimmed. Mortgage demand at thrift institutions is expected to increase as mortgage rates are expected to remain flat or decline slightly in early 1985. Both farmers and farm lenders continue to experience difficulties, with little relief as yet coming from the recent federal debt adjustment program. Interest rates on farm operating loans have declined, however, as has the prime rate. Both loan demand and deposits are up at district banks.

Retail Trade. Most retailers report that 1984 sales were up 5 to 10 percent over 1983. Oklahoma is an exception, as the depressed oil industry has contributed to weaker sales. Consumer electronics are reported to be selling very well in all areas. In recent months, respondents in Kansas City and Denver report only moderate improvement while elsewhere in the district sales are reported as flat to worsening. Although Christmas sales compared favorably to previous years, they fell short of the expectations of most retailers. Those expectations led to higher than desired inventory levels and will likely cause inventory purchases to decline. Retailers are mildly optimistic about sales for 1985 and expect no significant price changes.

Automobile Dealers. About half of the automobile dealers contacted report recent sales above year earlier levels. Easier credit market conditions have allowed adequate financing for both dealer floorplanning and customer purchases. Some respondents report large inventories, but others say that inventory levels may not be satisfactory to meet the strong demand expected in the near term. Most dealers expect 1985 sales to improve over 1984.

Purchasing Agents. Purchasing agents report input prices through the fourth quarter of 1984 up 3 to 10 percent over a year earlier. They also expect price increases in a range of 2 to 8 percent for 1985. Inventories are at satisfactory levels but some moderate further trimming is planned for early 1985. There are no reports of problems in getting materials.

Housing Activity and Finance. Homebuilders report that housing starts in 1984 exceeded those in 1983 with the biggest gain occurring in multi-family starts. Sales of new homes in 1984 were at or slightly above 1983 sales. Prices of new homes have remained about constant. Prices for most housing materials have remained stable or have risen only slightly. The demand for mortgage funds and mortgage commitments at savings and loan institutions is expected to increase in 1985, but not before spring. Mortgage rates in the first half of 1985 are expected to remain near their current levels or decline slightly and then to remain flat or rise slightly in the second half of 1985. Lower minimum deposit requirements on MMDA's and Super NOW's have brought improved inflows of new savings deposits to some institutions, while others are not reducing minimum requirements at this time.

Agriculture. The Farmers Home Administration's (FmHA) new debt adjustment program, effective November 1984, is meeting with only limited success in the Tenth District. Although some non-FmHA borrowers and lenders in Nebraska and Oklahoma have attempted to qualify for this program, the overall response has been weak. Even where farm borrowers have shown interest in the program, many are failing to qualify. Agricultural bankers cite excessive paperwork and stringent positive cash-flow requirements as reasons for the program's apparent ineffectiveness to date.

Paydowns on agricultural loans at the end of 1984 were below average in most of the Tenth District, and below earlier expectations. Bankers in Missouri, Nebraska, Kansas, Oklahoma, and Colorado estimate that 50 to 90 percent of their farm borrowers made unsatisfactory or no loan paydowns in 1984. Several Tenth District banks report that 5 to 10 percent of their farm borrowers will receive no more credit. As a result, agricultural lenders expect to see more liquidations in 1985, and, therefore, they expect to experience losses.

Interest rates on operating loans have continued to decline, with rates now ranging from 12.75 to 14.5 percent. Agricultural lenders in all district states but Oklahoma report interest rates falling by as much as one and a half percentage points over the past eight weeks. In Oklahoma, however, rates are largely unchanged at 14 to 14.5 percent.

Banking. Respondents at Tenth District banks report increased loan demand, with advances in virtually all categories except agricultural loans, which are unchanged. Deposits are also up, with demand deposits, conventional NOW's, Super NOW's, IRA'S, large CD's, and MMDA's all showing gains. Only small time deposits, which have been essentially flat, and passbook savings accounts, which have shown some falloff, have failed to advance. The prime rate stands at 10.75 percent at a majority of the banks, with some banks coming down recently to 10.5 percent. Consumer lending rates have shown little change with few banks having lowered their rates, but roughly half expect to do so if the prime rate continues to fall. Most respondents have not yet made a final decision about lowering the minimum deposit on MMDA's and Super NOW's to the allowable $1,000; those that have reached a decision have elected to do so. Lowering the minimum deposit is viewed as necessary to match competitors, rather than as a means to generate more deposits.

## ELEVENTH DISTRICT--DALLAS

Economic growth in the Eleventh District continues its slow pace. Manufacturing sales growth is negligible overall. Retail sales never approached expectations for the holiday season and remain relatively slow. Oil and gas drilling is increasing slightly, but falling oil prices continue to prevent a significant recovery. Residential construction continues to slow with overbuilding remaining a problem in most markets. The strongest sectors are auto sales and nonresidential construction, both of which remain well above last year's figures.

Manufacturing output growth in the District remains sluggish overall. Only nonelectrical machinery manufacturers consistently report improved sales largely as a result of the continued recovery in the oil field machinery sector. Some primary and fabricated metal producers report higher than expected unit sales, but these gains are offset by lower prices. Apparel manufacturers face increased seasonal demand, but gains are not as strong as normal. Electrical machinery producers, especially semiconductor firms, report serious declines in demand. This had been the strongest sector of manufacturing but rising inventories have caused layoffs and lower production levels. Moderate weather has diminished the normal seasonal upturn in refining. Virtually all sectors report stable input and product prices.

The number of drilling rigs in District states remains relatively steady, posting slight gains in recent months. Respondents state that this is a normal seasonal upturn that occurs at the end of the year. The rig count, however, is still 1 percent below last year's level. A weak oil price outlook has prevented significant gains. The exception to the overall sluggish drilling picture continues to be the Gulf of Mexico where the number of active rigs has increased over 20 percent in the last year.

Auto sales are very strong. Some respondents report that this December was the busiest ever and the first days of January maintained this pattern. The strength is widespread across different models. Higher shipments of domestic cars have reduced the inventory problems that plagued dealers throughout 1984.

The weakness of retail sales continued through the holiday season and into January. Sales volume, although fairly high, was lower than expected and was achieved only through widespread use of mark downs. Sales of virtually all categories, except electronics, were soft. The reduction in profit that accompanied the discounting has prompted retailers to adopt such cost-saving plans as reducing orders for 1985 and cutting employment. Retailers blame reduced business on slowing economic growth and competition for consumer's income from auto and home sales.

Residential construction in District states continues to slow. The permits issued in November were almost 50 percent lower than during November 1983. The biggest decline has been in multifamily units, although single family units have also declined significantly. Respondents note that lower interest rates may help clear the market of an existing surplus, but demand may not increase enough to induce significant amounts of new construction.

The value of nonresidential construction contracts in Eleventh District states was high in November and thirty percent over last year's level. The total did decline from October's exceptionally strong showing.

The gain was concentrated in Dallas, San Antonio, and Austin. The increase occurred despite concerns expressed by respondents of overbuilding in these markets. Most categories of nonresidential construction contributed to the increase with major contracts awarded for construction of roads and other public facilities, offices, and hotels.

In December, deposits at large banks registered a second straight month of ten percent growth over last year's levels. All categories of liabilities increased. The pattern was similar at member banks although the size of the increase was smaller. Year-over-year loan growth at the large banks declined slightly in December from November but the gains in both of these months exceeded the increase of October. Fourth quarter growth in all loan categories was below the pace of the remainder of the year. Real estate and consumer loans led the increase in lending. Business loans continue their pattern of slow growth.

Texas farmers and ranchers, unlike those in the rest of the nation, are increasing their borrowings. Both Production Credit Associations and the Federal Land Bank in Texas report hefty increases in loans. These increases suggest that the asset position of District agricultural borrowers is relatively better than others in the nation. Good weather conditions in West Texas have resulted in a better-than-expected cotton harvest, raising the estimate of total Texas cotton production to 175,000 bales. Texas cattlemen, responding to higher spot and futures market prices, continue to market unseasonably large numbers of fed cattle.

## TWELFTH DISTRICT--SAN FRANCISCO

The recovery of the economy of the Twelfth District was continuing at year end. The pace of the recovery in November and December was considerably slower than in the first half of the year, but there did not seem to be any signs of increasing weakness or recession. Indeed, buoyed by declining interest rates, home purchases and purchases of consumer durables and automobiles appeared to be up slightly from a few months ago. Manufacturing employment continues to grow and in most states in the District, unemployment rates continue to fall. Agriculture remains weak as a result of depressed export demand and strong crop yields.

### Consumer Spending

Consumer spending remains strong in most parts of the District, although the rate of growth is well below that observed earlier in the recovery. In Southern California, for example, retail sales in November were up about 15 percent over their level in November 1983 but down from the 24 percent growth experienced between 1982 and 1983. Similarly, in Utah November sales were up 12 percent over a year earlier. Preliminary data on Christmas retail sales volumes have been mixed, with reports of only modest increases in Christmas sales volumes over the 1983 level in the Intermountain states and the Pacific Northwest. Somewhat stronger sales were reported in California, but the preliminary picture is one of disappointing volumes. This is substantiated further by sluggish growth in credit card activity reported by banks.

Sales of new automobiles, however, were spurred by the sharp reductions in short-term interest rates that occurred toward the end of the year. In Oregon, for example, automobile sales early in the fourth quarter had grown by 24 percent in one month. Sales of other consumer durables -- particularly consumer electronics items -- remain healthy but sales growth over 1983 has been modest.

Manufacturing and Mining

Statistics on manufacturing employment show continued, but slowed, growth of this sector. For the District as a whole, manufacturing employment grew by about 2.5 percent in 1984, down from the 3.3 percent growth experienced in 1983. Although much of the District's wood products industry remains depressed, some bright spots recently have been observed. Plywood sales nationally set a new record and producers of this product in the Pacific Northwest are enjoying strong demand. Lumber producers were able to edge prices up slightly, with western lumber orders for the first week of December holding steady at what the industry considers "average" levels. The weak dollar has increased competition from Canadian wood products manufacturers, however, and plant closures in this industry continued throughout the District.

Mining also remains weak as a result of low prices and stiff competition from foreign producers. Throughout the District, however, the weakness in the wood products and mining industries has been offset by growth in other manufacturing industries and the services sector. In states like Oregon and Idaho, these developments are almost perfectly offsetting and unemployment rates have remained quite steady over the last several months. In California, however, the strength of the aerospace and electrical equipment industries has led to continued, gradual declines in unemployment rates. In Santa Clara County, California, the center of the nation's high technology industry, the fourth quarter unemployment rate was less than 4 percent.

Construction and Real Estate

The decline in mortgage interest rates caused an abrupt resurgence in new and used home sales in the fourth quarter. According to industry sources, home sales growth in the West was the highest of any region in the country. Weak areas remain, however, particularly in the Northwest; home sales in Oregon, for example, fell slightly early in the fourth quarter and the issuance of home construction permits declined about 30 percent between 1983 and 1984.

Agriculture

The agricultural sector in the District continues to suffer the effects of weak export demand and heavy debt burden. Prices for a number of crops have dropped sharply. Avocado prices, for example, range between 15 and 19 cents per pound, down from 80 cents per pound in 1980. Low wine prices -- due to stiff foreign competition -- have resulted in the removal of vineyard plantings in California after many years of steady expansion in this industry. It is estimated that approximately 10 to 15 percent of the loans to California farmers are nonperforming. The restructuring of the financial affairs of farmers likely will result in a high percentage of foreclosures and liquidations of farm properties.

Financial Institutions

Bank lending in the Twelfth District remained strong in December, as it has been throughout the fouth quarter. Both total bank credit (loans and investments) and total loans exceeded normal seasonal growth rates. December growth was paced by rapid increases in consumer lending (a 40 percent annual rate of growth). The strength reflected both banks' aggressive lending practices and a surge in consumer borrowing -- despite slower than expected retail sales over the holiday season. Recent declines in mortgage rates also may have accounted for the upsurge in real estate lending (an 11 percent annualized rate) in December, following weakness in this area throughout the year. Business borrowing also expanded at a rapid pace, rising at a twenty percent rate (annualized) for the month.

The recent decline in market rates has narrowed the spread between jumbo CD rates, money market fund yields, and MMDA rates, and altered banks' deposit flows and funding pattern. The lower rates appear to have led some banks and consumers to lock in longer term deposits, resulting in strong increases in both jumbo CDs and small denomination time deposits in December. The elimination of the differential between money funds and MMDA rates also resulted in renewed inflows into MMDAs; these deposits grew very rapidly in December. Most institutions in the West expect the recent reduction in minimum balance requirements on MMDAs and SNOWs to have little effect on inflows into these accounts, although the reduced minimums may lead to more tiering of rates and fees.