For use at Noon, E.D.T.
Wednesday
August 7, 1996

Summary of Commentary on

Current Economic Conditions

by Federal Reserve District

July 1996

SUMMARY OF COMMENTARY ON CURRENT ECONOMIC CONDITIONS

BY FEDERAL RESERVE DISTRICTS

JULY 1996

TABLE OF CONTENTS

SUMMARY*

The economy continued to expand in June and July, though in some areas the pace of growth has moderated since the last report. A number of districts report tight labor markets, especially for entry-level workers; however, wage pressures remained subdued. Retail sales slowed in most districts, particularly for non-auto durables. Many districts report continued expansion in the manufacturing sector, and a number have seen a pickup in hiring. Most manufacturers and retailers report that inventories were roughly on target. Housing markets remained fairly strong in most districts, though a few areas report a slowdown; a number of districts note particular strength in the multi-family segment. Commercial and industrial real estate markets continued to firm in almost all districts. A number of districts note brisk tourism activity—especially on the east and west coasts.

Crop conditions have generally improved since the last report, although late plantings across the Midwest raise the potential for damage in the event of an early frost. While there are scattered reports of rising commodity prices, most districts report that input prices, as well as prices for finished goods, were essentially flat. Most districts report increased demand for commercial and industrial loans, but softer demand for consumer and mortgage loans.

CONSUMER SPENDING

Retail sales softened in most districts, though sales were generally up from a year-ago. Boston, New York, Philadelphia, Cleveland, Richmond, Atlanta, Chicago, and Dallas note some

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* Prepared at the Federal Reserve Bank of New York and based on information collected prior to July 30, 1996. This document summarizes comments received from business and other contacts outside the Federal Reserve and is not a commentary on the views of Federal Reserve officials.

weakening since the last report. However, contacts in Minneapolis, Kansas City, and San Francisco say that sales remained strong. Retail inventories were generally on target.

Demand for non-auto big ticket durables—such as home furnishings, appliances and electronics—was particularly soft in several districts (New York, Philadelphia, Cleveland, Richmond, Atlanta, Chicago, and Kansas City). Auto sales were mixed; most districts report steady sales , but Kansas City reports a pickup, while Dallas notes some softening. New York and Chicago report that unusually cool weather may have contributed to weakness in seasonal items, such as fans and air conditioners. Apparel sales were fairly good in the New York, Atlanta, Kansas City and San Francisco districts, but were weak in the Boston, Philadelphia, and Dallas areas.

MANUFACTURING

Manufacturing activity continued to expand in most districts. Boston, New York, Philadelphia, Minneapolis, Kansas City and San Francisco report that conditions firmed. However, Richmond, Atlanta, and Dallas note some softening. Cleveland and Chicago also report some recent moderation in growth, but add that the sector is still strong. Most districts report that inventory levels were in line, although they were a bit high in Richmond. However, auto-industry suppliers in the St. Louis and Chicago districts report lean inventories, and this has hindered light truck assemblies.

Conditions in high-tech industries are very strong in Minneapolis but weak in Dallas; San Francisco notes increased activity in research and development, but some moderation in growth of computer manufacturing. Dallas reports increased demand for energy-related products.

REAL ESTATE AND CONSTRUCTION

Residential real estate markets remain fairly strong in most districts. Some slowing was observed in the Richmond, Atlanta, Chicago and St. Louis districts. However, Boston, New York, Cleveland, Minneapolis, Kansas City, Dallas, and San Francisco report continued improvement. Boston, New York and Atlanta noted particular strength in the multi-family housing market.

Commercial real estate continued to firm in almost all areas. Tight markets and declining vacancy rates are cited in Boston, New York, Richmond, Chicago, Minneapolis, Dallas, and San Francisco. St. Louis and Atlanta report mixed conditions, with the latter mentioning strong demand for office and industrial space, but softening demand for retail space.

NONFINANCIAL SERVICES AND TOURISM

Service activity continued to expand in districts that report on this sector. A monthly survey of service sector firms in the Richmond district shows increased activity in July. Temporary employment firms and contractors in the Philadelphia and Richmond districts report brisk business. San Francisco reports a pickup in software development activity.

Tourism has been notably brisk in the seaboard regions—Boston, New York, Richmond, Atlanta, and San Francisco. Minneapolis reports that tourism is below expectations, but roughly on par with last year. The Olympics have clearly attracted large numbers of tourists to the Atlanta area, and other parts of the district have benefitted as well—large numbers of Atlanta residents reportedly visited Florida during the games. However, some of the district's other traditional destinations report disappointing traffic.

FINANCIAL SERVICES

Banks in virtually all districts report that demand has softened for consumer and mortgage loans but strengthened for commercial and industrial loans. The New York, Cleveland, Richmond, Atlanta, Chicago, St. Louis, and San Francisco districts report increased demand for business loans, while Philadelphia and Kansas City report steady demand. However, consumer and mortgage loan activity weakened in the New York, Richmond, Atlanta, St. Louis, and Kansas City. Banks in New York, Philadelphia, and Chicago indicate some increase in loan delinquencies, while Cleveland reports that delinquency rates have leveled off. Insurance companies in the Boston district report mixed sales of insurance products but increased mutual funds sales.

AGRICULTURE AND RESOURCE-RELATED INDUSTRIES

Crop conditions were mixed but generally improved since the last report. Contacts in St. Louis, Minneapolis, and Kansas City report that crops were generally in good condition; conditions were below normal but improving in Cleveland and Chicago. Late crop plantings in the Cleveland, Chicago, St. Louis, and Minneapolis districts raise the potential for crop damage in the event of an early frost. A severe drought in the Dallas district—and parts of the St. Louis district—has caused extensive damage to corn and other crops, although recent rainfalls have helped somewhat. Hurricane Bertha caused some moderate crop damage in the Richmond district.

The energy industry has picked up in the Minneapolis, Kansas City and Dallas districts, with contacts reporting increased drilling activity. The strength is largely attributed to high crude oil and natural gas prices, while Minneapolis also cites new seismic and drilling technologies as a factor.

EMPLOYMENT & WAGES

Labor markets remain tight, but there has been no widespread increase in wage pressures. Contacts in virtually all districts outside the Northeast cite tight labor markets and scattered shortages of both skilled and entry-level workers; most report that wage pressures remain subdued, though San Francisco reports that "wage inflation pressures are evident in some areas". Businesses in Atlanta, Kansas City, and Dallas mention limited availability of entry-level workers; contacts in Philadelphia and Richmond report increased demand for temporary workers; Chicago reports shortages of construction workers and professionals.

PRICES

Despite scattered reports of rising commodity prices, most districts report that both input prices and costs of finished goods were, on balance, flat. Manufacturers in Boston and Richmond report stable to declining input prices; those in New York, Chicago and Kansas City report some rise in materials costs. Other districts report mixed trends in raw materials costs; steel prices reportedly increased in Chicago and Kansas City but declined in Cleveland and Dallas. Prices for finished goods were generally flat in the New York, Atlanta, Chicago, St. Louis, Minneapolis, and Kansas City districts, and up slightly in Boston and Richmond. Contacts in Philadelphia and Atlanta attribute the difficulty of raising prices to intense competition. Cattle farmers have been pinched by weak cattle prices and rising feed prices. Corn and soybean prices fell sharply in late July, after surging in preceding weeks.

Some areas report an escalation in real estate costs. Contacts in Boston, New York, Richmond, Atlanta, and Dallas note upward pressure on commercial rents. Boston and New

York also report some firming of residential rents. St. Louis mentions a pickup in new home prices, driven by rising costs of both land and construction materials.

FIRST DISTRICT - BOSTON

Business conditions are generally good in the First District. Retail results are mixed, with hard-goods chains and tourism doing especially well. Manufacturers report rising demand for most products. Input prices are reportedly stable or declining. Commercial real estate activity is robust in New England markets. Insurance companies indicate sales vary by type of product, with their mutual funds having the largest sales gains.

Retail

Although June and July are normally a slow time for retailers, hard-goods chains in the First District report good news--double-digit sales gains compared with year-earlier levels. By contrast, apparel specialty and off-price chains report sales declines of from 0 to 5 percent. Respondents' expectations for the next six months are similarly mixed, ranging from 15 percent growth to 5 percent decline. While most are optimistic about the economy, two contacts express concern with rising consumer debt.

Vendor prices remain stable, with the exception of paper prices which have reportedly fallen 20 to 30 percent in the last year. Retail prices are generally level. All respondents express satisfaction with inventory levels. Wage increases range from 3 to 5 percent. Only one contact anticipates significant growth in capital spending and employment in 1996.

New England's tourist offices report strong activity this summer, boosted by double-digit increases in the numbers of international visitors over the previous summer. The two airline carriers that provide most of the region's European service note that foreign travel is up an average of 20 percent. Boston area hotel occupancy and room rates for June were up 3 and 8 percent, respectively, compared with the previous June. Advance reservations suggest New England's fall tourist season will be exceptionally strong.

Manufacturing

First District manufacturing contacts report that demand is higher than a year ago for most products. Some indicate double-digit improvements for health care, industrial, and aircraft equipment. By contrast, orders for heavy duty truck parts and memory chips are said to be slowing sharply, and the market for apparel textiles remains sluggish. Automotive equipment markets are mixed. Car production reportedly is increasing, but automakers are shifting suppliers--to the advantage of some First District contacts and the disadvantage of others. Shifts in microelectronics and automotive demand are prompting some manufacturers to make inventory corrections.

Most manufacturers indicate that, overall, materials costs are steady, with declines for steel and copper as well as some chemicals and selected grades of lumber. Selling prices generally are flat to up slightly. Because of automakers' continued demands for price cuts, some suppliers are deciding to emphasize equipment sales to other industries.

Employment is increasing at a majority of respondent firms, although these expansions are generally modest. Highly skilled machinists and computer specialists are reportedly hard to find, but general labor availability is not viewed as a constraint. Although a couple of respondents report wage and salary freezes, most anticipate increases this year in the 3 to 5 percent range.

Capital spending trends are mixed. Several contacts with ambitious investment plans note they could be scaled back if market conditions weaken.

The consensus among manufacturers is that the economy is in good shape for the remainder of 1996. However, evaluations for individual companies vary depending on particular products or technologies, and some contacts mention analysts' worries about an economic slowdown in 1997.

Commercial Real Estate

Improved economic conditions in New England have led to a strong and active commercial real estate market. Contacts report high levels of activity and significantly lower vacancy rates throughout the region. The market is particularly strong in the Greater Boston area, with very low levels of inventory and office and industrial vacancy rates around 10 percent and 7 percent, respectively. Lower vacancy rates are also reported in Connecticut and Maine. Contacts note variation across different market sectors. Apartment buildings represent the strongest sector, with low vacancy rates and high rents throughout, while the retail market is the weakest.

Commercial rents have gone up in the Greater Boston and Portland markets. Contacts anticipate rent increases elsewhere as inventory levels decrease further in response to the high level of activity and limited new construction.

Nonbank Financial Services

Respondents at insurance companies report mixed sales of insurance products in the second quarter. Among their lines of business, mutual funds tallied the biggest sales gains. Employment was flat or lower in the second quarter of 1996 compared to the second quarter of 1995. The downward trend in employment is expected to continue as the industry consolidates.

Respondents see two important trends in the insurance industry. One trend is continued consolidation. Consolidation is occurring both because of the requirement for high capital expenditures in many segments of the industry and because of ongoing competition within the industry and with other financial services firms selling investment products to the consumer. The second trend is restructuring of the distribution system. In particular, contacts note that selling insurance products through banks provides an opportunity to the industry since it can be more cost-effective than the agency system.

SECOND DISTRICT--NEW YORK

Most sectors of the Second District's economy improved in recent weeks. Both the commercial and residential real estate markets continue to strengthen—vacancy rates are down, construction of multi-family units has surged, and sales of both new and existing single-family homes are up. Regional purchasing managers report continued growth in the manufacturing sector in July. The boom in tourism continues, with New York City hotels approaching full occupancy. On a weaker note, retail sales, which had been fairly brisk in May, slowed in June and July, and were generally below plan; also, banks reported a slight rebound in delinquency rates in July. Wage and price pressures generally remain subdued, except in Manhattan's tight real estate market, where rents on apartments and hotel-room rates have risen sharply.

Consumer Spending

Retail sales in the district were, on balance, below plan in June and July, as business slowed from May's brisk pace. On a year-over-year basis, same-store sales ranged from a 1 percent decline to an 8 percent gain in June, with gains of 0 to 6 percent in July. Most department stores continue to cite women's apparel, and upscale apparel more generally, as the top performing categories, and home goods as the weakest. Discount chains report that only "consumables"—small-ticket, frequently purchased items—have sold well in recent weeks. Some of the recent weakness was attributed to cooler than usual weather in June and July (especially compared with last year), but a number of contacts believe that underlying demand has softened a bit. It was noted that June and July are not considered critical months for retailing.

All of the retailers surveyed reported that inventories were on or close to target as of late July. With retailers now starting to build inventories for the fall season, most say they are "cautious" in their expectations for the second half of the year. Virtually all contacts report that their effective selling prices are steady, that merchandise costs are flat to declining, and that there are no wage pressures.

Construction & Real Estate

The region's commercial real estate markets are firmer than they have been in a number of years. In New York City, office vacancy rates, which had blipped up in May, retreated in June—midtown Manhattan's rate fell to 14.5 percent, from 14.8 percent in May, while downtown's rate edged down to 24.7 percent from 24.9 percent. The reduced vacancy rates were due to a lack of new properties coming on the market and to existing office space being converted to residential use; leasing activity remained steady. In northern and central New Jersey, brisk leasing activity has pushed vacancy rates down 0.8 points to 17.9 percent in the second quarter—two points lower than a year ago, and the lowest level since 1987.

The District's residential real estate markets were generally strong in June, led by the multi-family sector. Manhattan's housing shortage and double-digit rent increases continue to make headlines, while prices for co-ops and condominiums have reportedly risen more modestly. In New York State, building permits for multi-family structures surged in both the first and second quarters, and are running at more than double last year's level. Virtually all the gains were concentrated in New York City and its northern and eastern suburbs.

Realtors in the district also report fairly brisk demand for existing single-family homes. In New York State, second-quarter sales surged 16 percent from a year earlier, though gains were more moderate in June. While second-quarter data are not yet available for New Jersey, most realtors report that the market is strong, fueled by first-time buyers. Home prices are rising at about a 4 percent annual rate in both states. The market for new single-family homes is mixed. New York State homebuilders report steady improvement—down-state New York remains strong, while upstate markets are beginning to snap out of their chronic slump. In New Jersey, however, builders report that the housing market remains "in the doldrums"—traffic is mediocre, there is no sense of urgency to buy, and affordability remains a problem.

Manufacturing

Regional surveys of purchasing managers suggest continued growth in the manufacturing sector and a slight uptick in prices paid in July. Purchasing managers in Buffalo reported that production activity held steady in July, following brisk growth in the second quarter, while new orders continue to expand at a moderate pace. Meanwhile, growth in metropolitan New York City's manufacturing sector accelerated from its already rapid second-quarter pace, with that survey's diffusion index climbing to a new cyclical high in July. (A parallel survey of purchasing managers in New York City's non-manufacturing sectors signals steady, moderate growth). Finally, purchasing managers in both Buffalo and New York report a moderate rise in prices paid, with both diffusion indices climbing into the mid 50's.

Other Business Activity

Labor markets were relatively stable in June. New Jersey's unemployment rate held steady at 6.1 percent, after falling a half point in May; New York State's edged down to 6.3 percent in June, from 6.4 percent in April and May. Employment grew in both states in June, but at a slower pace than in prior months. Consumer confidence, though still at an exceptionally low level, improved noticeably in July. Finally, the boom in tourism shows no signs of abating: hotel occupancy rates in New York City climbed to a 17-year high in the second quarter, and room rates continued to rise at a 10 to 15 percent rate.

Financial Developments

According to a survey of senior loan officers at small and medium sized banks in the District, loan demand has softened over the past two months. The largest decline in activity occurred in the residential mortgage loan segment, with demand lower at nearly 45 percent of the banks surveyed and steady at over 35 percent. Refinancing activity for all types of loans continues to decline, though at a diminishing pace. However, demand for commercial and industrial loans continued to increase.

Banks reported modest increases in loan delinquencies in all lending categories. Loan officers are generally more willing to lend than two months ago, and nearly all have maintained the same credit standards. Average loan rates continued to rise—they are higher or unchanged at almost all of the participating banks. The spread between the average lending and deposit rates is steady at nearly 60 percent of the banks and narrower at close to 30 percent.

THIRD DISTRICT - PHILADELPHIA

Firms in the major business sectors of the Third District gave varied reports on activity for July. Most of the manufacturers surveyed noted increases in shipments and orders; however, producers of building products and industrial equipment were experiencing slower business. Most of the retailers contacted said sales were healthy but the year-over-year gains in June and July were below those achieved in the early spring; some merchants even noted slight declines. Auto dealers generally said sales have been steady. Most of the bankers polled for this report said loan volumes outstanding were flat, and they continued to describe competition for commercial lending as strong. Some also said that, while consumer loans remained level, delinquencies were on the rise. Recent comments from employment agencies in the Philadelphia area indicated that demand for clerical workers remained healthy and that there has been some increase in the demand for manufacturing workers.

MANUFACTURING

Manufacturing activity in the Third District continued to expand in July, according to reports from area firms. Half of those polled indicated they had stepped up shipments since June while only one in ten noted declines. Half of the manufacturers contacted also reported increases in new orders, and only one in five said orders had slipped from the prior month. The improvement in business was reported from nearly all the major industrial sectors in the region;

however, manufacturers of building products and industrial equipment said that an increase in interest rates earlier this spring adversely affected demand for their products.

Area manufacturers extended working hours slightly and hired more workers in July, and they are planning some further increases in staffing levels during the second half of the year. While the balance of opinion among area manufacturers is that business will continue to improve during the third and fourth quarters, several noted that both domestic and foreign competition appears to be keeping prices in check.

RETAIL

Third District retailers contacted in late July gave mixed reports. While most said sales were continuing at a healthy rate, many noted that year-over-year gains in June and July were below the gains in earlier months, and several merchants indicated that their sales were just even with or slightly below the levels of a year ago. In particular, apparel sales appeared to be slowing and growth in housewares and electronics sales was easing. Discount stores, which sell more hard goods, were achieving better results than department stores, which are largely dependent on clothing sales. Despite the apparent slowing of sales, most of the retailers surveyed for this report did not indicate that inventories were excessive.

Auto dealers reported that sales were running at a steady pace, modestly above the rate for last summer. Light truck sales were up more than car sales on a year-over-year basis. Most dealers expect sales to continue at the current rate, although some are apprehensive that growing consumer debt burdens could lead to a downturn later in the year.

FINANCE

Most of the Third District bankers contacted for this report said total loan volumes outstanding at their banks had been level in recent weeks. They continued to describe competition for new commercial loans as strong and net interest margins as tight. Bankers also said consumer lending was flat, and they generally do not expect this category of credit to increase in the near term. Some bankers said they expect a combination of slower consumer spending and more restrictive credit standards to limit or reduce consumer lending in the second half. Some also expect the rate of consumer loan delinquencies to rise further this year until tighter credit standards become more prevalent.

SERVICES

Employment agencies and personnel contracting firms in the Philadelphia area reported continued demand for clerical and data-entry workers from banks, law firms, and television-shopping companies. Recently, employment agencies have also seen increased demand for temporary workers from manufacturers. Additionally, business at employment contractors has increased as a result of the outsourcing of certain business functions by major firms in the region. In several instances, according to both temporary employment agencies and contractors, the back-office staffs that these firms eliminated have become employees of the agencies and contractors supplying services to these firms, but many of the former employees have taken some reductions in pay and benefits.

FOURTH DISTRICT - CLEVELAND

General Business Conditions

The District economy continues to expand at a moderate pace amid relatively modest price increases and low unemployment. Joblessness has dropped below 5 percent in many areas, with northern Kentucky and central Ohio posting rates of less than 3-1/2 percent.

The construction sector has reported the highest growth rate in the past few months, following a relatively lackluster spring. Residential construction has been especially strong in central Ohio and western Pennsylvania.

Agriculture

The condition of crops in the District has improved considerably in the past eight weeks, and in some cases (notably tobacco), production has been good. Still, many crops, including corn and winter wheat, are underdeveloped for this time of year. Rainfall in early July facilitated pollination of corn crops, but cool weather during the last half of the month has been counterproductive. As of mid-July, only 4 percent of Ohio's corn crop was in the silking stage of the pollination process, compared with a five-year average of 42 percent. The corn crop in Kentucky and Pennsylvania is also underdeveloped (by 18 and 12 percentage points, respectively).

Potentially good harvests are being reported for a variety of fruits, including strawberries, cherries, and tomatoes in Ohio, and peaches in West Virginia. In Kentucky, apples are reportedly in good condition.

Manufacturing

Manufacturing activity in the second quarter was much improved from the first three months of the year. Although orders growth dropped off slightly in June and July, order books are reportedly full enough to keep industrial activity at a high level through the fall. The slowdown in industrial orders has been most prominent in foreign markets, especially Western Europe. Industry sources with business interests in Asia continue to report strong demand.

Capital goods firms are still producing at a high level, and suppliers to the light vehicles industry report a sharp increase in production between the first and second quarters. Several sources note that lean inventories and recently raised production schedules in light vehicle manufacturing are responsible for the increased production at auto suppliers. Heavy truck manufacturers, which cut production earlier in the year, have noted a leveling off this summer. Elsewhere, demand for machine tools and electronic machinery are both reported to be good, especially in areas related to housing, such as electrical components and light construction machinery. Off-highway machinery and industrial controls are noted to be flat, however.

Cost increases are said to be modest. Reports from area purchasing managers indicate price hikes for a variety of chemicals and agricultural commodities, but price declines are noted for a broad range of metals, wood products, and fuels. Although a few firms indicate increased difficulty in attracting and retaining workers, wage growth is reported to be between 2 percent and 4 percent, similar to earlier in the year.

Consumers

District retail sales have been mixed. Apparel sales are said to be brisk, while sales of furniture and other home goods have dropped off. Computer sales continue to moderate from last year's pace, and audio products remain in their nearly yearlong slump. Many retailers indicate that June receipts exceeded their expectations, but sales appear to have stumbled in July. One large chain store said that sales at its recently opened Ohio stores are not up to par with other regions.

Non-auto retail inventories are reported to be adequate, and prices are holding steady or declining slightly.

Although auto sales were essentially flat in the region during June and July, year-to-date receipts remain above last year's levels. The slip in early-summer sales has been attributed to lack of product. Indeed, many dealers report that they had adequate buyer interest, but were unable to provide desired options and equipment. In general, dealers remain very optimistic about the upcoming months.

Banking

Loan demand is holding steady overall, although reports are quite mixed by institution. Consumer borrowing has been especially variable, as a number of institutions reported recent strength in this category while others noted a significant drop-off. Consumer credit delinquencies have leveled off recently, breaking the erosion of household credit quality seen over the past year. Commercial credit demands are continuing to expand in most areas.

FIFTH DISTRICT-RICHMOND

Overview: Fifth District economic growth moderated somewhat in June and July. Manufacturers reported slower activity, particularly in textiles. Decreased imports led to a decline in port activity, and sluggish housing sales translated into weaker residential construction. Service sector activity expanded; retail sales grew at a steady pace; and commercial real estate activity strengthened. Contacts in several sectors continued to report wage pressures. Despite the adverse impacts of Hurricane Bertha, tourism expanded and yield prospects for some crops improved.

Retail Trade: District retailers reported that retail sales growth changed little in recent weeks, although big-ticket sales, inventories, and shopper traffic grew more slowly. Respondents to a mail survey indicated that employment growth picked up and wages rose faster in July. Over the past several weeks, retail prices rose at a faster rate and retailers expected the rate of increase to accelerate somewhat during the next six months. Contacts anticipated a slight decrease in demand for their products in the second half of the year.

Services: Service producers contacted by mail indicated that the pace of business activity increased in July. Revenues and wages grew more quickly and employment growth was unchanged. Service producers said their prices rose faster in July than they had in June. Respondents expected prices and demand for their products to rise during the next six months.

Manufacturing: Manufacturing activity weakened in July and tight input markets continued to constrain some firms. Except in West Virginia, respondents to a mail survey of District manufacturers reported declines in shipments. Most durable-goods producers indicated that new orders had weakened in July, although one West Virginia manufacturer noted that his company had difficulty meeting its customers' delivery requirements. Manufacturers continued to indicate that their inventories were above desired levels. Textile manufacturers reported that sluggish apparel sales forced them to cut back production to avoid inventory buildups. Several industrial machinery and equipment suppliers reported that their output was constrained by a scarcity of skilled labor. Manufacturers indicated that finished goods prices increased slightly and that raw materials prices were down slightly in July from June. Respondents' six-month outlook was for lower finished goods prices and somewhat higher raw materials prices.

Tourism: Tourist activity continued to pick up in July despite the effects of Hurricane Bertha along the District's coastal areas. Our contacts noted that activity during the Fourth of July holiday was above a year ago and they attributed the increase to unseasonably mild weather and the holiday falling late in the week. One contact from a popular mountain resort in West Virginia reported that the Fourth of July tourist activity was the strongest in that resort's history. Hurricane Bertha inflicted only minor property damage along the District's coastal areas, but a contact from North Carolina's Outer Banks told us that the area lost over $5 million in business revenues after tourists were evacuated. A hotel manager in the Virginia Beach area said he had 300 rooms vacant because of the hurricane. Contacts reported that summer bookings continued to look good.

Port Activity: Activity at District ports declined in June from May. When compared to a year ago, export shipments increased and imports fell. Port representatives continued to anticipate that exports and imports would increase during the next six months, with five of six ports expecting exports to rise faster than imports. One port contact attributed the pickup in exports to increased shipments of poultry to Eastern Europe and auto parts to South America.

Temporary Employment: The demand for temporary workers continued to increase in recent weeks. Demand was particularly strong for secretarial help, skilled warehouse and production workers, and computer-literate workers; the need for general laborers declined. In most areas of the District, temporary workers' wages were unchanged, and contacts in those areas expected little change during the next six months. However, in areas of the District with low unemployment and a shortage of skilled labor, temporary-worker agencies reported pay hikes and expected further increases in coming months.

Finance: District contacts reported that overall loan demand softened slightly in the last six weeks. The demand for mortgage loans, especially refinancings, continued to weaken in the face of higher interest rates. Many contacts noted that while higher mortgage rates had pushed some marginal home buyers out of the market, some qualified buyers were "priced out psychologically" by the higher rates. According to several lenders, current economic and political uncertainty had also left many commercial borrowers "sitting on the fence."

However, one contact noted that since the first of June, lending for commercial real estate development in his area had picked up considerably.

Residential Real Estate: District real estate agents and homebuilders contacted by telephone indicated that residential real estate activity softened somewhat in most areas of the District in June and July as potential home buyers' interest waned. Builders reported that they took out fewer building permits and started slightly fewer homes. A West Virginia homebuilder reported that the largest supplier of residential electrical supplies in his area went out of business because of sluggish housing construction activity. District real estate agents said that, despite higher customer traffic, sales were sluggish. One contact summed up the situation by observing, "the traffic is nice, but the sales conversion ratio is low." Despite somewhat lower activity, pressures on inputs markets remained. Lumber prices increased and subcontractor wages rose. A South Carolina homebuilder told us, "we are scraping bottom for labor in our area."

Commercial Real Estate: Commercial real estate activity picked up in June and early July. Commercial real estate brokers contacted by telephone indicated that leasing activity continued to escalate; one South Carolina contact said activity in his area was at a "fevered pitch." Vacancy rates declined, and rental rates continued to climb, as they have since last fall. A South Carolina contact noted that "rent concessions have evaporated," and a North Carolina respondent said she expected the market in her area to stay "landlord-oriented." The availability of prime office space continued to tighten, and many contacts reported shortages. Respondents throughout the District, and especially those in North Carolina, witnessed an increase in new construction.

State Revenues: State tax collections were higher in West Virginia but were flat in other District states in June. Withholding tax collections increased significantly in West Virginia as employment growth improved over the past two months, particularly in the construction and business service sectors. Growth in retail sales collections remained the same in South Carolina, Virginia, and West Virginia; were slightly lower in Maryland; and rose substantially in North Carolina. Real estate receipts rose in Maryland and West Virginia. However, one Virginia contact indicated that fewer mortgage refinancings had reduced real estate recordation receipts.

Agriculture: Intense storms damaged some District crops, but the rains associated with the storms benefited others in recent weeks, according to agricultural analysts. Hurricane Bertha caused up to $180 million in crop damage in North Carolina--over half of that to the tobacco crop. Corn and cotton also sustained substantial damage. On the plus side, Bertha's rains were credited with saving the corn crop in the eastern areas of Maryland and Virginia that had been suffering from severe drought; an agricultural extension agent now looks for a "bumper" corn crop there. Post-Bertha thunderstorms in late July led to scattered crop damage in parts of Virginia and Maryland, but also improved District crops' yields prospects.

SIXTH DISTRICT - ATLANTA

Overview: Reports from contacts provided a mixed but positive picture of the District economy through mid-July. While retail sales generally have been above year-ago levels, they have been below merchants' expectations for this summer. Manufacturers slowed production seasonally in July, and many revised downward their expectations for growth through the end of the year. While tourism generally has been strong in most of the District, several popular regional travel destinations have reported year-over-year declines in business. Home sales and construction continue to outpace year-ago levels, but Realtors and builders have become more cautious about their prospects for the remainder of the year. Commercial and multifamily real estate markets continue to improve, and Realtors report that the number of speculative developments underway in the District is increasing. Bankers noted that overall loan demand improved slightly during the last month, with commercial lending growing more rapidly than consumer lending. Although several local area labor markets continue to be tight, wage pressures remain muted. Factory and retail contacts reported little change in the prices they are receiving for goods and services rendered.

Consumer Spending: A majority of District retailers reported year-over-year increases in sales through mid-July, although many also commented that sales have been below their expectations. While sales of apparel have improved over this period, sales of durable goods, particularly home products, have slowed. Retailers generally say that they expect flat to modest increases in fall sales compared to year-ago levels. Inventories were characterized as on target throughout the District.

Manufacturing: Factory activity slowed seasonally in July, with contacts reporting decreases in production and shipments in most industries. Inventories of finished goods increased, and contacts reported that they were less optimistic than before about the near-term outlook for their businesses. An increasing number of firms expect new orders to slow in the next few months, with production remaining relatively flat over the period. Apparel producers continue to report declines in overall business along with plant consolidations and closings. By contrast, producers of home furniture and appliances expect to see modest improvement through the end of the year, as recent home buyers furnish their new domiciles.

Tourism and Business Travel: Tourism and business travel continues to be strong in most of the District through mid-July. Approximately two million visitors are expected to visit Atlanta and other District cities during the Summer Olympic Games. However, while many local sites have seen significant gains in tourism prior to and during the first week of the Olympics, in Atlanta contacts characterized the situation as "feast or famine." Generally, heavy spending near Olympic venues has provided a notable contrast to the disappointingly light traffic recorded at some of the District's other traditional tourist destinations, and a large suburban sports-related festival was prematurely closed after very light attendance. As of this writing, the tragedy in Centennial Olympic Park has had no negative impact on event attendance, and is unlikely to have any notable economic consequence. Outside of the Olympic spotlight, many cities in Florida have benefitted from a surge in tourism and business travel, much of which has been fueled by the large number of Atlantans who are vacationing and doing business outside of the city for the duration of the Games.

Construction: Most real estate contacts reported that single-family home sales were above year-ago levels in June and early July. However, builders said that by mid-July the pace of home construction had slowed from the rapid pace recorded earlier in the year. Contacts in much of Georgia reported year-over-year declines in homebuilding in the last two months, although gains were reported in northern Alabama and Nashville. Most Realtors characterized current home inventory levels as adequate, although supplies remain tight in some local areas. Realtors generally said that their outlook had become more cautious in the last month.

Multifamily homebuilding and commercial construction continue to improve in most areas. Low vacancy rates and rising rents continue to support new industrial and office development, although the pace of retail construction has moderated. While most commercial projects continue to be build-to-suit, several speculative developments are underway, and more are expected to be announced in the next six months. Most real estate agents anticipate moderate-to-strong growth in commercial and multifamily construction through the end of the year.

Financial: According to contacts in the banking industry, overall loan demand rose in July compared with June, although it was flat when compared with year-ago levels. While mortgage lending generally has held steady, auto lending slowed during the month. Commercial lending improved moderately.

Wages and Prices: Contacts generally said that wages were stable over the last month, with fewer complaints of labor shortages being reported. While service and retail sector employers continue to note a lack of applications for entry-level positions, a majority of contacts in the skilled professions characterized labor supplies as adequate. Fewer contacts expect to hire new employees than was the case in early summer. Manufacturers and retailers both indicated that prices remain subject to intense competitive pressures, both from international firms seeking to increase their share of U.S. markets, as well as from domestic consumers who remain vigilant in their search for bargain-basement prices.

SEVENTH DISTRICT--CHICAGO

Summary. The Seventh District economy continued to expand through June and July at a slightly slower rate than in our last report. Retail sales growth was positive but continued to lag that of the nation. Residential housing activity lost some momentum, but overall construction activity continued to increase. The manufacturing sector, bolstered by strong demand for durable goods, expanded in June and July but showed some signs of slowing toward the end of the period. Banking activity remained strong, while several financial institutions noted a continued rise in delinquency rates. Despite tight labor markets and continued strength in the economy, there was little evidence of accelerating increases in wages or other input costs. Grain prices fell as crop conditions improved and cuts in livestock production eased concerns about tight grain supplies.

Retail sales. Retail sales continued to increase in year-over-year comparisons, but the growth rate slowed slightly from June to July. Several large retailers noted that sales growth in the District remained below their national averages. Slower-than-expected sales gains resulted in some unintended inventory buildup, most notably in electronics and seasonal items, such as air conditioners and lawn and garden equipment. One retailer described demand for summer goods as "nonexistent". Most retailers, however, reported that inventories were in good shape and much better than at the same time last year. Auto dealers reported that sales were strong and that showroom traffic remained high.

Housing/Construction. Growth in the housing industry lost some of its momentum in June and July but most contacts noted that the market remained very strong. Several home builders and realtors reported that activity had picked up from May's weather-induced slump, but not as much as anticipated. Shortages of skilled labor and some building materials hindered contractors' efforts to make up lost time in many areas. A few metro areas were reporting inventory buildup, but most contacts noted that builders were not concerned and were not using incentives to clear inventories. Most builders and realtors reported that the first-time buyer segment remained robust. Contacts in some of the District's largest metro areas reported that office vacancy rates continue to fall and may be at a level that could spur new construction. A realtor in one of these areas noted that several large projects were already underway and that "this is the best office market (he's) seen in 5 1/2 years".

Manufacturing. Most District manufacturers reported strong demand and lean inventories heading into the third quarter, while upward pressure on costs remained constrained. Purchasing managers' surveys indicated modest expansion through June and early survey returns showed that the expansion continued in July--but at a slightly slower rate. Survey results from one major metropolitan area indicated slowing production growth from June to July with some inventory building; new orders, however, remained quite strong. Appliance and machinery producers reported that demand was being buoyed by the continued strength in housing and construction activity. Auto suppliers noted that production was at capacity and a shortage of parts was hindering light truck assemblies. Several steel analysts indicated that orders were still strong and inventories remained lean at every level.

Despite the continued increase in activity, there was little evidence of acceleration in price increases. While costs of some inputs continued to drift upward, several producers indicated that they were unable to pass along these increases to final goods purchasers. However, steel producers reported some success in getting their July price increases to stick.

Banking. Banking activity remained strong through much of July, although several financial institutions reported a continued rise in delinquencies. Most District contacts noted that business lending was the most vigorous segment of the banking market. One major bank reported its strongest business lending month of the year in June and indicated that this strength had continued into July. Several banks noted a modest scaling back in consumer and mortgage lending, but one large bank could find no let up in demand from its "high quality" customers. Many contacts expressed concern about rising delinquency rates for consumer and retailer loans, but viewed the increases to be within normal credit performance standards.

Labor markets. Labor markets remained tighter in the District than in the nation as a whole despite relatively slower job growth. The rebound in manufacturing employment noted in our last report was short-lived. Contacts from around the region and purchasing managers' surveys suggested flat to slightly reduced manufacturing payrolls in June and July. Shortages in professional and technical occupations persisted; shortages were particularly severe in the construction industry, where inclement weather in May and early June delayed many projects.

Wage pressures remained subdued despite the very tight labor markets. However, some employers reported enhancing benefits packages to attract and keep workers, especially in the construction industry.

Agriculture. Corn and soybean prices fell sharply after hitting new highs in mid-July. Crop conditions across District states were mixed, but overall were rated slightly below normal as of the end of July. Late plantings and subnormal temperatures have increased the risk of damage from an early frost this year. Nevertheless, recent rains and forecasts of favorable weather through early August--a critical period for plant development--have buoyed District crop prospects. Updated reports showing surprisingly large cuts in livestock and dairy production--especially in District states--have added to the decline in crop prices. Sudden sluggishness in grain exports also eased earlier concerns about tight grain supplies this summer.

EIGHTH DISTRICT - ST. LOUIS

Summary

District economic activity has increased since the last report. Tight labor markets continue to be our contacts' primary concern. Strong sales in several industries have led to lower-than-anticipated inventories. Rising materials prices are also a continuing concern. Residential real estate and construction markets have softened somewhat. Loan demand at large District banks also appears to be softening. District crops are in mostly fair-to-good condition, although the corn and soybean crops are well behind schedule in some areas.

Manufacturing and Other Business Activity

Reports of tight labor markets continue to come in from all parts of the District. Contacts are also reporting high turnover rates, even at firms that are offering relatively high starting wages and fringe benefits. Besides the previously reported shortages of skilled and entry-level workers, some contacts have noted a need for semi-skilled labor. In some areas of western Kentucky, where poultry processing is a growing industry, firms are increasingly hiring foreign labor.

Firms that sell parts to the auto industry are reporting low finished goods inventories because of strong sales. Some firms supplying the construction industry also have low inventories because of strong sales, especially of power tools. Other firms in the steel drum and glass container industries report that their inventories are slightly below desired levels, but that customers' inventories are at desired levels.

Some St. Louis merchants located near the McDonnell Douglas plant have felt the effect of the machinists' strike, which began June 5. In many cases, merchants are offering special prices to striking machinists to attract business. McDonnell Douglas has hired about 400 out-of-towners to work alongside nearly 4,000 white-collar workers currently on the production lines.

The poultry industry continues to expand in western Kentucky, as another processor moves into the area, creating about 1,200 jobs. A telemarketer in the Memphis area is also expanding and adding almost 1,500 jobs. An Arkansas trucking company will open a new terminal and add 400 workers by winter. Two coal mines in southern Illinois, however, have announced they are closing because of a fall-off in demand. Together, about 550 jobs will be eliminated as the mines' customers switch to low-sulfur coal to meet federal pollution regulations.

Prices

Increasing prices for materials continue to affect some firms in the District. For example, St. Louis home builders note that prices of new homes have increased because of substantial increases in the costs of land and construction materials. On the other hand, a salvage metal processor and a maker of auto parts report few or no price increases, and, in one instance, a price decrease. Even with tight labor markets, there are still few reports of increased wage pressures. In those cases where starting wages have been bid up, the increase has generally not been passed on to consumers.

Real Estate and Construction

Some real estate agents have reported a recent softening of real estate markets, particularly in central Arkansas. They cite rising interest rates and strong sales earlier in the year that satisfied much of the pent-up demand. Residential construction permits issued in June in most District metropolitan areas reflect this recent slowing. Some pockets of strength can be found in western Kentucky and northeast Arkansas, however. Almost all District metro areas are well ahead of last year's permit levels. Mid-priced homes ($100,000 to $150,000) are reportedly selling well, while sales of higher-priced homes have slowed substantially. Nonresidential construction activity appears strong in northern Mississippi, central Arkansas and western Kentucky. Some commercial real estate agents, however, have noted a recent moderation in demand.

Banking and Finance

Total loans outstanding at 11 large District banks declined 0.6 percent between mid-May and mid-July after rising 1.5 percent between mid-March and mid-May and 2.7 percent between mid-May and mid-July one year ago. Commercial and industrial loans rose 0.8 percent in the most recent period, but real estate loans dipped 0.9 percent and consumer loans dropped 3 percent.

Agriculture and Natural Resources

Weather conditions varied considerable in July, with temperatures in the northern portions of the District slightly below average. Although rains during the latter half of the month helped substantially, many areas are still in need of topsoil moisture—particularly in the southern parts of the District. In addition, the timing of the rains in the corn- and soybean-producing areas were such that prices for these two crops have declined markedly from their highs earlier in the month. Overall, crops are generally in fair-to-good condition across the District. Notable exceptions include parts of Illinois and Indiana, where a substantial percentage of the corn and soybean crops are well behind schedule. In Missouri and the southern parts of the District, crops are generally in better condition and ahead of schedule. Winter wheat yields were average to slightly below average in Illinois, Indiana and northern Missouri, but were generally better than average in most other areas.

NINTH DISTRICT--MINNEAPOLIS

Moderate to strong economic growth continues in the Ninth District economy, with few adverse indicators. Once again, construction is a work horse across the district. Natural resource industries are also pulling, with oil development the strongest in a decade and iron mining straining to meet orders. Manufacturing appears quite strong, but with considerable variation across subsectors. Manufacturers report normal inventories. Crop conditions are generally very good, but hog and milk producers have cut output in the face of higher feed costs. Vehicle sales are reported as steady, and general merchandise retailers report satisfactory, but not spectacular, business. Wage increases are reportedly moderate and price increases scarce. Labor markets remain tight.

On the negative side, tourist business continues somewhat slower than projected. Beef producers face markedly adverse prices, and lenders expect some ranch business liquidations.

Construction and real estate

"Building permit activity up in Minnesota," headlined an article describing residential construction in that state. The fact that this would be equally true for nearly any other urban area of the district highlights the importance of construction as a fountain of strength in the Ninth District economy. Growing cities such as Sioux Falls, S.D., Fargo and Grand Forks, N.D., Billings and Missoula, Mont., and Eau Claire, Wis., all report strong residential, retail, commercial and light industrial construction. Furthermore, at mid-year publicly let contracts for public and heavy construction in Minnesota and the Dakotas were 15 percent above 1995 levels, well on their way to making 1996 a fourth consecutive year of record spending in this category.

Sales of existing housing are also reportedly strong in most of the same areas. For example, new listings and pending sales at the Minneapolis-St. Paul multiple listing service were up 15 percent at mid-year over 1995, and the cumulative dollar volume of closed sales for the year was up over 25 percent. Similarly strong markets prevail in several other cities across the district.

Natural resource industries

"The level of activity in 1996 should double that generated in 1995," according to a North Dakota oil industry official. A mini-boom is taking place in that state, largely the result of new seismic and drilling technology which has boosted the success rate to 87 percent of all wells drilled. Drilling is extending to several counties that have not seen such activity for a decade.

Lake Superior iron mines are generally running full-out as they struggle to fill orders and catch up after a late opening of the shipping season earlier in the year. Other metal mining output is stable. Forest product output generally continues slightly above year-earlier levels. Output for the paper industry as a whole is below prior-year levels, but sales of some specific grades are reportedly strong.

Manufacturing and Technology

"We are having a good year, but no barn burner," reports a North Dakota cabinet manufacturer. "Manufacturing growth off the chart," heads a newspaper article describing Eau Claire, Wis., where a number of electronic component plants are under construction. Such comments illustrate a manufacturing sector that on balance is quite strong, but with considerable variation among subsectors.

Most producers of traditional items such as automobile components, consumer chemical products and furniture report a solid but unspectacular year. There are some exceptions, a North Dakota agricultural and construction equipment firm reportedly has a banner year, and a small wood molding firm in Michigan is expanding. But the strongest area apparently is high-tech products such as computer components, other electronic devices, and advanced plastic films. Many such firms report solid revenue increases or are building new plants. Other firms that integrate electronic equipment and computer software also report strong sales increases. Regardless of product, no manufacturers report delays in receiving raw materials, and their own inventories are generally reported as normal.

Agriculture

On the whole, crops across the Ninth District are in the best shape of the last five years, though additional rain would be beneficial in most areas, especially Montana. While most acres of major crops are rated good or excellent, crop development still lags normal stages in many areas. Barring extremely early frost, the district should have normal yields for major crops. Machinery sales are reported up from 1995 in some areas.

Hog and milk prices are somewhat higher than earlier in the year, largely in response to lower output prompted by high feed costs. Milk production in June was down 6 percent for Wisconsin and 1 percent for Minnesota from prior-year levels. But egg production was generally up, reaching a 9 percent increase for Minnesota in May over 1995 levels. Beef producers at all levels continue to face difficult conditions, with cow-calf operators bearing the brunt of the adjustment. Conversations with bankers and ranchers continue to point to widespread liquidations this fall. "I already have three years worth of business," remarked a South Dakota attorney specializing in farm bankruptcies.

Consumer spending

"Car sales are not real strong, but they are very steady," reports one Montana dealer. "About average except for pickups which are selling well in the oil areas and to some farmers," says a North Dakota association representative. "New registrations are a few percent above last year," according to a South Dakota official. This theme pervades reports about vehicle sales, and carries over into the general retail sector. "Business is steady, good," says one Montana retailer. "We are a little above our plan," echoes a representative of a regional department store chain. A national chain based in Minnesota reports modest year-over-year increases in its discount stores.

Several sources comment on the difficulty in distinguishing apparently sluggish sales increases in existing stores from the effects of major increases in retail capacity in the 1990s. Many sources indicate a fourth consecutive brisk building season for stores with new construction reported in virtually every town of 5,000 population or over. A more reliable indicator of retail activity may be sales taxes which, while lagged some months, are generally coming in above prior projections, and revenue officials expect this trend to persist.

Tourism

"Tourism continues to be down in the region," reports a Montana banker. "The season is slow," comments a South Dakota official. "It's finally getting better," comments a Wisconsin spokesperson. On balance, tourism is below expectations, but about even with year-earlier levels. Minnesota and Wisconsin officials describe brisker activity than colleagues in Montana and the Dakotas. An adverse Canadian dollar exchange rate, a late, cold spring and increased gasoline prices are all cited as contributing factors.

Employment, wages and prices

"Highly skilled people are really tough to find," says a North Dakota manufacturing CEO reprising a familiar theme in the Ninth District. Unemployment rates remain well below national averages in all areas of the district except the Upper Peninsula of Michigan, and help wanted signs are omnipresent in most urban areas. Employment growth has occurred across most sectors and help-wanted ads range across manufacturing, retail and business services.

Most reported wage increases are at the low end of the wage scale. Moreover, some employers are extending fringe benefits to previously uncovered low-wage jobs. Most wage increases are modest, however. Few price increases are reported other than for milk at the farm and retail, and for grains and grain products. Gasoline prices have moderated slightly from spring highs, and breakfast cereal prices continue to fall despite rising grain prices.

TENTH DISTRICT - KANSAS CITY

Overview. The district economy continued to grow at a moderate pace during the past month. Retail sales increased modestly, manufacturing and construction activity remained strong, and activity in the energy industry picked up. In the farm economy, however, continued financial losses in the cattle industry held down farm income, despite strong crop prices. Labor markets stayed tight for both entry-level and skilled workers, although reports of rising wages remained widely scattered. Overall retail prices were steady, even though prices rose for some materials used in manufacturing and construction.

Retail Sales. Retailers report sales improved modestly during the past month and remained above last year's level. Sales of apparel were strong, while sales of appliances and other electronic products were weak. Retailers generally expect sales to remain strong the next couple of months before slowing somewhat near the end of the year. Although most retailers were satisfied with their current inventory levels, some were trimming inventories. Automobile dealers report increased sales last month that stayed well above last year's level. Sales are expected to remain strong in the months ahead. Dealers indicate automobile inventories were generally smaller than desired, due to the transition to the new model year and to continued strong demand for light trucks and sport utility vehicles. While dealers report that high consumer debt has lowered the quality of applications for automobile loans, they indicate that overall credit quality appeared stable.

Manufacturing. Manufacturers continued to operate their plants at high levels of capacity use, and some plants report an increase in overtime work. None of the manufacturers, however, indicate capacity constraints caused production bottlenecks. Manufacturing materials were readily available with normal lead times, although some manufacturers report temporary difficulty in obtaining steel. Manufacturers were generally satisfied with their inventory levels, although some were reducing inventories slightly.

Housing. Most builders report housing starts held steady last month but at a much faster pace than last year's. Single-family homes accounted for most of the construction activity, although construction of multifamily units remained brisk. Builders expect construction activity to remain strong through the end of the year. Sales of new homes picked up slightly last month and remained well above last year's pace, despite a relatively low inventory of unsold homes. Prices of new homes held steady, staying somewhat higher than last year's level. While building materials were readily available, prices rose slightly, especially for lumber and roofing materials. Most mortgage lenders expect mortgage demand to remain strong through the end of the third quarter.

Banking. Banks generally report total loans grew somewhat faster than deposits last month, slightly boosting loan-deposit ratios. Most banks report gains in home mortgage and home equity loans. Home construction loans, commercial real estate loans, and commercial and industrial loans held steady, while consumer and agricultural loans declined. Banks also report gains in demand deposits, NOW accounts, and MMDAs. Security investments held steady while large CDs, small time and savings deposits, and IRA and Keogh accounts declined.

All respondent banks held their prime lending rates steady last month, although a third of the banks expect to increase their prime rate in the near future. Half of the respondents raised their consumer lending rates slightly last month, and a few banks expect a further increase in the near future. Lending standards were unchanged.

Energy. Activity in the district energy industry picked up in June. Prices of crude oil and natural gas stayed well above last year's level. As a result, the number of drilling rigs operating in the district rose 15 percent above last year's level.

Agriculture. The district's winter wheat harvest is nearly complete. As expected, wheat yields ranged from normal to poor, due to the unusually dry winter and spring in Oklahoma and Kansas. Recent rains, however, have brightened prospects for the district's corn and soybean crops, which are generally in good to excellent condition. While recent improvements in crop growing conditions have pushed crop prices down, prices remain much higher than a year ago.

Cattle feedlots and ranches continue to operate at a loss, due to high feed costs and weak cattle prices. Agricultural bankers report that district feedlots have cut production, with many operating at only half to three-fourths of capacity. In addition, ranchers have trimmed herds by selling older, less productive cows. Overall, little improvement is expected in district farm income this year, as continued financial losses in the cattle industry largely offset financial gains by crop producers.

Wages and Prices. Although supplies of both entry-level and skilled workers remained tight in much of the district, reports of rising wages were widely scattered. Retailers report a tight supply of minimum-wage workers, and some retailers believe the recently legislated increase in the minimum wage will eventually push up retail costs. Manufacturers indicate that most kinds of workers were in short supply, including welders, machinists, and clerical workers. One manufacturer paid more overtime instead of raising wages, and some manufacturers increased wages slightly. Prices rose for some manufacturing materials, especially steel, some paper materials, and some plastics. Prices generally held steady at the retail level, with retailers expecting little change in prices in the months ahead.

ELEVENTH DISTRICT--DALLAS

The Eleventh District expansion moderated in late June and July after strong growth noted in previous surveys. Most respondents expect business conditions to remain at good levels for the rest of the year. Manufacturing orders were softer, as construction-related orders slowed slightly and semiconductor orders remained weak. Increased drilling activity boosted orders for energy-related equipment. Retailers reported slower sales and noted reduced traffic at stores. Loan demand was mixed, as refinancings continued falling, new residential loans held steady, and loans for commercial construction and consumers picked up. Although construction activity held steady over the past six weeks, contacts in the residential sector expected slower housing construction in coming months. Nonetheless, contacts said higher demand for office space reduced vacancies, especially in suburban markets. Record heat and drought continued to impede agricultural production.

Prices and Wages

There were scattered reports of price pressures over the past six weeks. Contacts said prices were up for plastic products, some base petrochemicals and lumber. In addition, several manufacturing respondents said higher natural gas prices had boosted their costs. Crude oil prices were down from the last survey, but remained above $20 per barrel according to contacts. Despite low cattle prices, the June Texas All Farm Products Index of Prices rose 2.9 percent above the May level, pushed up by higher prices for hogs, broilers, eggs, milk and all crops except potatoes. Prices were reported as falling for steel, paper, some apparel products, semiconductors and computers. There were few reports of wage pressures, although contacts in some industries continued reporting difficulty finding qualified, entry-level workers. A few manufacturing respondents were concerned about the possibility of a minimum wage increase, but retailers said they would not be significantly affected.

Manufacturing

Manufacturing orders softened over the past six weeks despite stronger demand for most energy-related products. Semiconductor orders continued to fall, and contacts were more pessimistic about the outlook for the industry. Most respondents hoped the decline in orders would bottom out by year-end. Respondents in the computer industry reported flat demand overall, although firms that make "build-to-order" products reported stronger sales than the industry average. Many construction-related manufacturers reported somewhat softer demand in the past six weeks following extremely strong growth in orders earlier in the year. After reporting shortages in the last Beige Book survey, cement contacts said demand had softened in the last six weeks, allowing them to take customers off of allocation. Brick producers said plants continued to run at capacity and inventories were low, but demand had slowed slightly in July. Lumber producers reported steady demand and low inventories. Apparel manufacturers reported flat demand after a noted improvement in the last Beige Book. In energy-related sectors demand was strong for most products. Petrochemical producers said that demand was solid overall and profits were improving, but that demand for plastic products (such as polyethylene and polypropylene) was especially strong with low inventories and scattered shortages. Oil field machinery companies reported that increased drilling activity had boosted demand. Gulf Coast refiners said weaker gasoline prices combined with high prices for crude oil were reducing profits, however.

Retail and Auto Sales

Retail sales slowed in June and July, particularly for apparel. Retailers noted that traffic at stores was down. Inventories were in line with expectations, and there was no mention of price pressure. Contacts remained optimistic that sales would pick up in the fall. Auto sales softened in June and July, but inventories remained on the light side according to respondents.

Financial Services

Contacts in the financial services industry reported mixed loan demand over the last six weeks. Refinancings continued to decline as long-term interest rates remained at high levels. Other residential real estate loans reportedly held steady. Consumer loan demand was up for some contacts in Dallas/Fort Worth and Austin. In addition, respondents reported higher demand for commercial construction loans, fueled by plans for speculative office and warehouse construction.

Construction and Real Estate

Construction and real estate activity held steady in late June and July. Home construction remained at high levels, but contacts expect activity to cool in coming months because of higher financing costs and lower buyer traffic. Respondents said strong demand for industrial space continues to buoy nonresidential construction. While there are minimal office projects in the works, contacts reported tighter office occupancy and rising rents, especially in suburban markets.

Energy

The energy market strengthened since the last Beige Book report, and crude oil and natural gas prices were at relatively high levels. Domestic drilling activity increased, with virtually all of the increase in drilling attributable to rigs looking for natural gas. Offshore activity remains strong in the Gulf of Mexico with every available rig under contract. According to contacts, a number of projects are underway to build new rigs or to refurbish old ones.

Agriculture

Drought continues to stress agricultural conditions, according to contacts. In early July, rainfall reduced stress in some areas, but record-breaking heat kept pastures and forages dry in many parts of the Eleventh District. Numerous fields of failed corn and grain sorghum continued to be cut as farmers and ranchers searched for sources of hay to feed livestock.

TWELFTH DISTRICT -- SAN FRANCISCO

Summary

Reports from Beige Book contacts suggest a recent pickup in growth in California and Washington, partly tempered by a moderation of the rapid pace of growth in other Twelfth District states. Overall, there appears to have been a gain in District manufacturing activity, with the locus of growth shifting toward California and Washington, where residential real estate markets also are firming noticeably. Among services, communications and software development are particularly strong. Retail sales in the District generally were reported to have increased in recent months. Wage inflation pressures are evident in some areas.

Business Sentiment

About three-quarters of our contacts in the District, including almost all respondents from Northern and Southern California, expect growth in their region to outpace the national growth rate, which most expect to be at or above its trend pace over the next year. Survey respondents expect tightness in labor markets to continue for a while, and prospects for inflation are perceived to have worsened slightly in the past few months.

Retail Trade and Services

Retail sales in the District generally were reported to have increased further in recent months. Business improved at food stores in the Pacific Northwest and Intermountain states. In Utah, retail sales reportedly were strong in July, particularly for apparel and autos. In Washington, strong sales were reported at small retailers, major conventional grocery chains, and club-warehouse style stores. Retailers in the Puget Sound area also reported difficulties in recruiting qualified employees at existing wages, given increased job availability in other industries.

In services industries, continued strong job growth also was reported to be adding to wage and price pressures. Demand for telecommunications services jumped, and software development activity expanded in California and Washington states. Computer programmers and systems engineers reportedly are in short supply. Tourism activity also has been strong this summer, leading to significant increases in hotel room rates in cities such as Salt Lake City.

Manufacturing

Overall, there appears to have been a gain in District manufacturing activity in recent months, although emerging weakness was reported in a few localities. In Washington state, aircraft manufacturing is picking up, and electronics components manufacturers are benefiting from this and from the growth in demand for other types of business equipment. The rebound in commercial aircraft also reportedly is boosting orders for fabricated materials, components, and machine tools from suppliers in Oregon, Southern California, and Nevada. Lumber production reportedly increased in recent months. Food manufacturing was down in a few areas where harvests were delayed by wet weather. Manufacturing of information processing equipment and components reportedly was increasing in some areas and being scaled back in others; in general, such activity is increasing in California, particularly in research and development areas such as Silicon Valley, but there is a moderation of the rapid growth in manufacturing of computers and related equipment in the Pacific Northwest and Intermountain states.

Agriculture and Resource-Related Industries

Agricultural production reportedly was mixed, depending on the commodity. In general, demand for agricultural products was strong, buoyed by growing exports, and prices for several commodities were reported to have firmed. The supply of cotton was reported to be higher than last year, and tree fruits were plentiful, but yields on nut crops were medium to poor. Dairy products prices are increasing relatively fast.

Real Estate and Construction

Residential home sales and construction reportedly have strengthened in Washington and California, but the residential market is cooling a little in Oregon, Idaho, and Utah, following rapid earlier gains. However, throughout the Pacific Northwest and Intermountain states, nonresidential real estate vacancy rates are relatively low, and building of offices, commercial space, industrial facilities, and public infrastructure continued strong. Within California, the strength in nonresidential building is concentrated in the San Francisco Bay Area; many segments of the Los Angeles area nonresidential real estate market continue to experience high vacancy rates and not much construction.

Financial Institutions

District financial institutions generally reported firm loan demand and wide credit availability. Asset quality generally remained high, with only a modest deterioration in some consumer lines, such as credit card loans. Financial institutions reported pressures for large wage increases for information systems jobs and for entry-level customer service jobs in those localities with low unemployment rates.