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Summary of Commentary on _____

Current Economic Conditions

By Federal Reserve District

August 2009

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

August 2009

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SUMMARY*

Reports from the 12 Federal Reserve Districts indicate that economic activity continued to stabilize in July and August. Relative to the last report, Dallas indicated that economic activity had firmed, while Boston, Cleveland, Philadelphia, Richmond, and San Francisco mentioned signs of improvement. Atlanta, Chicago, Kansas City, Minneapolis, and New York generally described economic activity as stable or showing signs of stabilization; St. Louis remarked that the pace of decline appeared to be moderating. Most Districts noted that the outlook for economic activity among their business contacts remained cautiously positive.

The majority of Districts reported flat retail sales. Richmond, Philadelphia, Chicago, Atlanta, and Boston remarked that retailers continued to carefully manage inventories, keeping them in line with low sales levels. A majority of Districts confirmed that the “cash-for-clunkers” program boosted traffic and sales. Richmond, Atlanta, Chicago, and Minneapolis also noted increases or planned increases in automobile-related production. Most regions reported some improvement in residential real estate markets. Downward pressure on home prices continued in most Districts, although Dallas and New York noted that local prices were firming. Reports on commercial real estate suggest that the demand for space remained weak and that nonresidential construction-related activity continued to decline. San Francisco, Philadelphia, and St. Louis noted that the demand for nonfinancial services remained soft, although the pace of the decline was described as slowing in the latter two Districts. Loan demand was described as weak and many Districts reported that credit standards remained tight. Most Districts reported improvements in manufacturing production. For instance, Philadelphia, Richmond, Atlanta, Cleveland, and Chicago reported moderate increases in new orders. Labor market conditions remained weak across all Districts. However, staffing firms in Atlanta, Dallas, Richmond, Cleveland, Philadelphia, Boston, New York, and Chicago did report a slight pickup in the demand for temporary workers.

* Prepared at the Federal Reserve Bank of Atlanta and based on information collected before August 31, 2009. This document summarizes comments received from businesses and other contacts outside the Federal Reserve and is not a commentary on the views of Federal Reserve officials.

Wage pressures remained minimal across all Districts. Consumer prices were described as being steady in most Districts, although Kansas City and San Francisco noted some downward pressure on retail prices.

Consumer Spending and Tourism

Consumer spending remained soft in most Districts. The majority of Districts reported that retail activity was flat. Boston, Philadelphia, and Kansas City noted improvement in sales, but attributed the increase primarily to back-to-school purchases. Philadelphia, Chicago, Cleveland, and San Francisco observed that shoppers remained focused on essentials and continued to refrain from purchasing discretionary and big-ticket items. Kansas City and San Francisco noted weak restaurant sales. Richmond, Philadelphia, Chicago, Atlanta, and Boston remarked that retailer inventories were being closely monitored and were keeping them in line with low sales levels.

The majority of Districts reported that the cash-for-clunkers program helped boost traffic and sales, although Cleveland and Kansas City also remarked that used car sales were adversely affected by the program. The sustainability of the higher recent pace of new vehicle sales was questioned by industry contacts in the Richmond, Atlanta, Minneapolis, and San Francisco Districts.

Tourism activity varied. Kansas City, Minneapolis, and Richmond observed solid visitor numbers at local vacation destinations, whereas Atlanta and New York noted sluggish activity and aggressive hotel discounting. San Francisco reported that activity in California and Nevada was weak, but visitors to Hawaii had increased.

Real Estate and Construction

Residential real estate markets remained weak, but signs of improvement continued to be noted. Chicago, Richmond, Boston, and San Francisco observed an uptick in sales over the last six weeks, while sales in the Philadelphia District were described as steady. St. Louis commented that residential home sales had not improved. Most Districts reported that sales remained below the levels of a year earlier. However, Atlanta, New York, Cleveland, and Minneapolis documented some year-over-year gains

in select markets. Most Districts noted that demand remained stronger at the low-end of the housing market. Boston, Cleveland, Dallas, Kansas City, Richmond, and New York indicated that the first-time home buyer tax incentive was spurring sales. However, Philadelphia did note an upturn in sales at the high-end of the market. Reports on house prices generally indicated ongoing downward pressures, although Dallas and New York noted some increases. Construction remained at low levels overall, although Chicago and Dallas reported a small increase in activity.

Reports on commercial real estate markets indicated that demand for space remained weak and that construction continued to decline in all Districts. Atlanta, Philadelphia, Richmond, and San Francisco reported that vacancy rates increased, while rates held steady in the Boston and Kansas City Districts and were mixed in New York. Boston, Dallas, Kansas City, Philadelphia, and Richmond commented that the demand for space remained weak. Commercial rents declined according to Boston, Chicago, New York, Philadelphia, and Richmond. Rent concessions were reported in the Richmond and San Francisco markets, and Richmond noted that some landlords had postponed property improvements in an effort to conserve cash. Construction remained at very low levels, with modest improvements noted in public construction in the Chicago, Cleveland, and Minneapolis Districts.

Nonfinancial Services

Reports on the demand for nonfinancial services were mixed. San Francisco, Philadelphia, and St. Louis noted that the demand for service sector business remained soft, although the pace of decline was described as having slowed in the latter two Districts. The demand for legal services remained relatively flat at low levels according to Dallas and Minneapolis. Kansas City and Richmond cited increasing demand for technology-related services. Healthcare services in Minneapolis also experienced an uptick in demand. Demand for transportation services were mixed, with some Districts noting stabilization at weak levels. Reports indicated that freight volume declines were moderating in Cleveland, while Dallas and Atlanta reported a modest pickup in rail shipments.

Banking and Financial Services

Most Districts reported that loan demand was weak and that credit standards remained tight. New York, Philadelphia, Cleveland, Richmond, Kansas City, St. Louis, and San Francisco observed further weakening in loan demand across most categories. Dallas noted scattered reports of improvements in loan demand. Contacts in Cleveland, Chicago, and Dallas noted an increase in demand for auto loans. Credit standards ranged from unchanged to tighter in most Districts. However, Chicago reported that credit conditions and availability had improved.

Mortgage activity declined modestly according to the Philadelphia, Cleveland, and Kansas City Districts, while Richmond reported increases attributed to improved demand for starter homes. Dallas noted an uptick in refinancing activity. Commercial and industrial lending declined in the Philadelphia and Kansas City regions, and was steady according to Richmond. The lack of available credit was cited as an issue for both residential and commercial contractors in Cleveland, and for commercial real estate borrowers in Atlanta. San Francisco reported an increase in venture capital investment.

Further deterioration in credit quality was noted by Philadelphia, Richmond, Dallas, and San Francisco, whereas Cleveland observed some improvement in credit quality. Chicago also cited improvements in credit quality, apart from home equity and commercial real estate. Dallas and Chicago noted increases in consumer bankruptcies, while rising delinquency rates were reported by New York and Cleveland.

Manufacturing

Most Districts reported modest improvements in the manufacturing sector. Philadelphia, Richmond, Atlanta, Cleveland, and Chicago all reported slight-to-moderate increases in new orders. San Francisco indicated that new orders increased for manufacturers of semiconductors and other IT products, while orders declined for metal fabricators and petroleum refineries. Dallas noted that orders held steady, while St. Louis reported that manufacturing output continued to decline, but at a slower pace. Richmond, Atlanta, Chicago, and Minneapolis reported increases or planned increases in automobile

and automobile-related production. Several Districts also noted increased production in the pharmaceutical industry.

The near-term outlook among manufacturers varied, but the majority of reports indicated that manufacturers were cautiously optimistic. Boston, New York, and Philadelphia reported that their contacts expect modest growth later this year or early 2010. Boston noted that while its contacts generally expect modest growth, several cost control measures would remain in place. Dallas reported increased uncertainty among construction-related manufacturers, while Cleveland noted that half of their manufacturing contacts expected weak demand into 2010.

Employment, Wages, and Prices

Labor market conditions remained weak across all Districts, but several also noted an uptick in temporary hiring and a decline in the pace of layoffs. Richmond reported that most service-providing firms continued to cut employees, while Minneapolis and New York noted additional layoffs in the manufacturing sector. Cleveland reported modest job declines in the banking, commercial construction, and coal mining sectors. Further job cuts are expected in auto manufacturing according to St. Louis, and Dallas indicated further staff reductions are anticipated in the airline, energy, and residential construction sectors. Staffing firms in a majority of Districts reported a modest increase in the demand for temporary workers, although industry contacts in Boston also questioned whether these gains will persist. New York cited a modest pickup in temporary hiring for the legal and financial industries. Chicago noted an uptick in demand for workers in the healthcare and information technology industries. St. Louis and Minneapolis reported that federal stimulus funds have had a positive impact on construction and local government jobs.

Wage pressures remained low across all Districts. Several Districts noted businesses and local governments imposing wage freezes or even reducing employee compensation in some instances. Boston noted that several manufacturers who have cut wage rates do not expect to restore pay levels until next year. Kansas City, Philadelphia, Chicago, Minneapolis, San Francisco, Dallas, and Richmond noted an increase in the cost of some raw materials, including fuel, metals, and steel. Chicago and Dallas mentioned

that excess supply was putting substantial downward pressure on natural gas prices. Retail prices were described as generally steady in most Districts, although Kansas City and San Francisco noted continued discounting and downward pressure on consumer prices.

Agriculture and Natural Resources

Reports on agricultural activity were mixed. Weather conditions were described as being favorable in St. Louis, Kansas City, and Atlanta. However, cold weather, crop diseases, and drought were limiting production of corn, cotton, and soybeans in the Chicago, Minneapolis, and Dallas Districts. Drought and weak market conditions were significantly affecting livestock industries according to Kansas City and Dallas. Dallas reported that some ranchers had liquidated portions of their cattle herds, while hog producers in the Kansas City District were said to be struggling as a result of lower pork prices.

Atlanta, Dallas, Kansas City, and San Francisco noted increased oil and gas inventories as a result of reduced consumption. Contacts in the natural gas industry noted that subdued demand continued to suppress prices and has led to cutbacks in extraction activity. Cleveland indicated that weak demand for electricity prompted coal producers to scale back production and capital investment. Kansas City noted that although coal production in Wyoming had risen, it remained below year-ago levels. Dallas and Atlanta remarked that oil and gas drilling activity continued to decline in the Gulf of Mexico, whereas Kansas City and Dallas reported that the number of rigs operating on land had increased.

FIRST DISTRICT – BOSTON

Many business contacts in the First District report recent signs of improvement, although most say activity remains below year-earlier levels. Contacted retailers, manufacturers, and software and IT services providers, while still reporting mixed results, are more confident about their companies' and the economy's eventual recovery. Staffing firms cite upticks in activity. Residential real estate sales rose in recent months, although prices continued to fall; commercial real estate markets remain very soft. Price pressures are mostly said to be modest and fewer firms say they plan layoffs than in the last round.

Retail

Contacted retailers in the First District report mixed sales results for the months of July and August. Several retailers attribute soft sales in part to inclement weather, while others note that consumers still seem to be cautious in their spending and focused on getting the best value for their dollar; some respondents feel this trend is going to be the "new norm" and that recovery will be a long and drawn out process. However, other respondents see signs of improvement, particularly in sales of items classified as discretionary, and many First District retail contacts are more optimistic than in recent conversations.

Retailers continue to manage inventory levels carefully, with several working to bring inventory more in line with sales. Capital spending remains carefully controlled. Contacts note that headcounts are stable. Selling prices are steady, but a few retailers express concern about potential price pressures.

Manufacturing and Related Services

Most manufacturing and related services contacts headquartered in the First District report that the pace of business has improved or exceeded expectations in recent months. Some contacts had higher sales in the second quarter than in the first and anticipate further growth in the third quarter. Several others indicate that their sales picked up slightly starting in the summer. Among the few respondents who report continued worsening in sales trends, one is hoping to see improvement as consumers broaden their spending increases beyond automobiles and electronic equipment. Despite the recent upticks, however, almost all manufacturing and related services respondents note that sales and orders have remained well below year-earlier levels. Some companies have temporarily shut factories in order to hold down inventories. Only the biopharmaceutical sector reports sustained sales growth during the past year.

Manufacturers say that materials costs are flat to down compared to a year ago. The only notable increases are due to foreign currency appreciation. Selling prices also are reported to be mostly flat to down, depending on the degree of market competition.

Apart from implementing previously announced restructuring programs, most of the contacted manufacturers and related services providers have no plans to increase or decrease their U.S. employment in coming months. Domestic hiring is limited mostly to offsetting attrition or expanding R&D and finance staffing. Many firms are continuing to hold down labor costs through furloughs, pay freezes, or suspensions of 401K plan matches. Several respondents that had cut employee pay 5 percent to 20 percent earlier this year say they are now planning to restore previous pay levels in 2010. Capital spending plans remain subdued, and center mostly on new product development or cost reduction.

Most manufacturers and related services providers are planning for modest revenue growth and continued cost controls over the coming six to 12 months. Many

indicate that their finances are in solid shape, with stable or improving cash flow. Some express lingering concerns about consumer spending.

Software and Information Technology Services

New England software and information technology firms report mixed results, with some experiencing continued slowdowns while others have begun to see modest improvement. Nevertheless, revenue changes from a year ago are largely in the range from zero to minus 15 percent. Contacts report continued interest from prospective clients but a hesitancy to commit due to budget uncertainties and a general lack of confidence. One respondent notes decreased maintenance revenues, as many clients have laid off employees and consequently have reduced maintenance needs. Most First District software and IT firms report managing expenses very closely to maintain profitability, through personnel reductions, salary freezes, the use of video conferencing instead of physical travel, and decreased spending on marketing. Meanwhile, other firms continue to invest in their workforces and in R&D, hoping to benefit when the recovery does occur. Selling prices are being maintained. Several New England software and IT services contacts report that positive signs they see in the economy are not yet reflected in their numbers; most respondents anticipate a long recovery and expect only modest growth in 2010.

Staffing Services

Nearly all New England staffing contacts report upticks in labor demand in recent weeks, but they are uncertain whether the increased demand will be sustained; yearly revenues generally show declines in the 10 percent to 40 percent range. Contacts report growth or its initial signs in the manufacturing and financial industries as well as in the information technology, pharmaceutical, and retail sectors. However, the increase in demand applies only to temporary labor, as placements for direct hires remain minimal; indeed, one contact does not anticipate demand for permanent labor to return until 2011. While there are plenty of job seekers, labor supply is still low for specialized positions.

Staffing contacts express continued concern over expected increases in health insurance costs and state unemployment taxes in 2010 and whether they will be able to pass those costs on to clients who may not yet be profitable. Contacts note that clients are currently hiring to fill vacancies, rather than hiring to expand. One contact indicates that many companies are trying to do their own sourcing instead of utilizing staffing firms, as hiring speed is no longer paramount. New England temporary services respondents are largely more optimistic than they were three and six months ago, but remain uncertain about the near term, as they anticipate a long, gradual recovery.

Commercial Real Estate

Commercial real estate contacts report no major changes in market conditions since last time. Leasing volume remains very low and downward pressure on rents continues to be intense across the region. Vacancy rates have not increased perceptibly since the last report, but net absorption is perceived to be negative. Landlords are reportedly trying to hang on to existing tenants “at all costs.” A large supply of sublease space is augmented by “shadow space” that many firms are not using but which they cannot readily sublet. Very little construction activity is in progress in the region: Speculative office construction is basically non-existent, but small condo conversion projects are under way in Cambridge and Boston.

In recent weeks, our Providence contact has seen an increase in foreclosure sales of commercial properties, all of which had been originally financed through commercial mortgage-backed securities (CMBS). Sale prices on these properties reflect discounts of

up to 60 percent from peak prices observed in 2007. A Boston contact has observed declines in property value ranging from 30 percent to 60 percent on various downtown office buildings. One contact predicts that the national commercial property value index will decline 50 percent peak-to-trough before recovering. In a number of cases, rents have fallen below the level that supports debt repayment. In light of these conditions, delinquencies and foreclosures are expected to increase further in the coming months. Underwriting standards in the commercial market remain very strict, with loan-to-value ratios largely below 70 percent. Small regional banks continue to support the bulk of financing activity in the region. Our regional banking contact reports that they have maintained a healthy balance sheet through conservative lending, and experienced higher profits this summer compared to a year ago as a result of increased market share in (commercial and residential) mortgage lending.

Over the next six months, contacts expect commercial market fundamentals either to decline further (in Boston and Providence) or to remain roughly flat (in Hartford). None expects a significant recovery of property values within the next year, and possibly longer depending on the extent of commercial foreclosures and the employment outlook. The recovery of deal volume, rental rates, and vacancy rates typically lag recovery in employment rates by up to six months. Therefore, contacts are watching the employment numbers closely and adjusting their forecasts accordingly.

Residential Real Estate

Residential real estate markets in New England showed some positive signs in June and July. All contacts report increasing year-over-year sales in either June or July, many for the first time in 2009. Home sales increased between 4 percent and 13 percent year-over-year across the region. Condos in Massachusetts also showed a small year-over-year sales increase in July. Most of the sales activity is said to be taking place at the low end of the market, partly because the first-time homebuyer tax credit has been successful in spurring activity for entry-level homes. The high end of the market, including second homes, is still very quiet. A New Hampshire contact reports that distressed properties, including bank-owned properties, are moving, although the sales process for these homes is complicated and the deals often fall through. Contacts say that although the June and July results are promising, they will not be confident that they have passed the bottom until sales increase for another month or two.

While sales were up, New England home prices continued to fall in June and July. Median home prices fell 5 percent to 14 percent year-over-year in July in the six states. An exception was the Boston area, where the median home price in July was only about 1 percent below what it was in July 2008. This Boston contact believes that sellers are pricing more realistically and “further price declines should be minimal.” Another contact attributes low prices to the large number of bank-owned property sales and also to the fact that prices at the peak were unsustainable; this contact does not believe that prices will return quickly to the pre-slump level. Respondents report the inventory of homes for sale in Massachusetts has fallen below a “balanced” market level, as potential sellers are listing their homes “only if they have to;” this seeming shortage should self-correct once prices stabilize.

SECOND DISTRICT--NEW YORK

The Second District's economy has been generally stable since the last report. The labor market remains soft with some signs of gradual improvement. Manufacturing sector contacts report some pickup in activity and remain optimistic about the near-term outlook. Auto dealers report a pickup in sales activity in recent weeks, but general merchandise retailers indicate that sales have remained fairly sluggish and well below 2008 levels, though on or close to plan. Consumer confidence improved slightly in August but is still at a low level. Tourism activity in New York City has been steady since the last report, though business travel is said to be down markedly.

Commercial real estate markets have been steady to somewhat weaker since the last report, while industrial markets have been stable. Housing markets in northern New Jersey and upstate New York have shown some signs of picking up, especially at the lower end of the market; however, the purchase and rental markets for New York City apartments continued to weaken, led by the high end. Finally, bankers report rising delinquency rates across all categories of loans, as well as some further weakening in loan demand and continued tightening in credit standards.

Consumer Spending

Retail sales were reported to be on or close to plan in July and August but still considerably lower than a year earlier, on a same-store basis. Contacts indicate that they are planning for holiday-season sales to be down by a bit over 5 percent on a year-over-year basis. Retail sales in New York City, which had reportedly picked up somewhat in June and early July, were said to be particularly weak in August. Contacts in western New York State note that Canadian customer traffic has picked up in recent weeks, but that sales overall have been steady and continue to run 5 to 15 percent lower than a year ago. Overall, inventories are said to be at favorable levels, and selling prices remain stable, though some retailers in

upstate New York say that their pricing has been a bit more promotional in recent weeks. Auto dealers in upstate New York report a substantial pickup in sales since the last report, which is partially attributed to the cash-for-clunkers program but also to other, more fundamental, factors. Overall, auto sales are reported to be up 10-15 percent from a year ago, though sales of used cars have weakened. Contacts report modest improvement in credit conditions for consumers.

Consumer confidence among residents of the Middle Atlantic states (NY, NJ, Pa) rose modestly in August, according to the Conference Board, but remains at a low level and below the nationwide average. Tourism activity in New York City has been weak but stable since the last report. Manhattan hotels report that occupancy rates remained in the mid 80s in July and early August—down only modestly from a year earlier. However, hotel room rates continue to run 25 to 30 percent below comparable 2008 levels—largely attributed to a shift from business travelers to leisure visitors, who tend to be more price sensitive. Broadway theaters report that attendance has held relatively steady since the last report, continuing to run about 10 percent lower than a year earlier; however, the average ticket price is up about 16 percent, keeping total revenue moderately ahead of year-ago levels in August.

Construction and Real Estate

Commercial real estate markets in the District were steady to somewhat softer since the last report. Manhattan's office vacancy rate rose moderately in July and August, while asking rents continued to decline—rents on Class A properties are down roughly 20 percent from a year earlier, and that does not include increased concessions by landlords. Elsewhere in the District, however, office markets have generally been stable: vacancy rates rose modestly in Long Island, northern New Jersey and metropolitan Syracuse but edged down in Westchester and Fairfield Counties and in the Rochester area; vacancy rates held steady in the Albany and Buffalo areas. Asking rents on Class A properties are down modestly over

the past year across most of the District. Industrial markets have been mixed but mostly steady.

The housing market has shown scattered signs of a pickup in parts of the District, though conditions have continued to weaken in New York City. A New Jersey contact notes signs of a mild pickup at the lower end of the resale market—helped by the homebuyer tax credit—but maintains that sales and starts of new homes remain flat at low levels. Prices are said to have firmed slightly in New Jersey’s resale market, though they remain substantially lower than a year ago. Similarly, Realtors across New York State report that prices rose in July but are running well below comparable 2008 levels.

In contrast, New York City’s multi-family market has continued to weaken. Manhattan co-op and condo prices have reportedly continued to fall in the current quarter. However, transactions activity, which had been exceptionally sluggish in the second quarter, has reportedly picked up in the current quarter, except at the high end of the market, where activity has evidently been constrained by tight credit. Prices of newly-constructed condominiums, which are mostly at the high end of the market, have been discounted steeply, reflecting a large inventory. The apartment rental market has also continued to deteriorate, especially at the high end: overall, asking rents are reported to be down 6 to 10 percent from a year earlier in August; moreover, landlords are typically waiving commissions and offering concessions, such as 1-2 months free rent.

Other Business Activity

A leading New York City employment agency specializing in mid-level office jobs notes a modest pickup in hiring in August, with the legal and financial sectors coming back somewhat. However, offering salaries are said to be down more than 10 percent from a year ago. While there are still reported to be a large number of applicants, the flow of newly unemployed people is said to have diminished noticeably. A contact in the financial sector

notes that merger-related layoffs are expected to continue for some time but that the general mood has improved noticeably—profits at trading firms have been strong this year, and a sizable number of middle-level workers are expected to see increases in compensation.

More broadly, business contacts across all industries, including manufacturing, report that employment continues to decline, but to a less widespread degree than in the first half of this year; moreover, a growing proportion indicate that they expect to increase employment at their firms in the months ahead. In assessing business conditions generally, both manufacturers and other firms report a pickup in activity for the first time in more than a year. Moreover, a growing proportion of both groups say they are optimistic about the business outlook. Firms across most sectors continue to report increases in prices paid but modest declines in prices received.

Financial Developments

Small to medium-sized banks in the District report a decrease in overall loan demand, though to a less widespread degree than in the last report. Bankers again report a decrease in refinancing activity. For all loan categories, respondents indicate ongoing tightening of credit standards. Respondents note an increase in the spreads of loan rates over costs of funds for all loan categories. The widening in spreads was most prevalent in the commercial mortgage category, where 37 percent of bankers report an increase in spreads and no banker reported a decrease. Finally, bankers indicate increases in delinquency rates, on net, across all loan categories. The percentage of bankers reporting an increase was roughly 30 percent in every loan category, while the percentage reporting decreased delinquency rates ranged from 0 percent in the residential mortgage category to 6 percent in the consumer loan category.

THIRD DISTRICT – PHILADELPHIA

Economic conditions in the Third District showed little change from July to August, although there were a few scattered signs of improvement. Manufacturers, on balance, reported a steady rate of shipments and a slight increase in new orders. Retailers indicated that sales of back-to-school merchandise had picked up, although the overall sales pace remained soft. Motor vehicle dealers indicated that sales of new vehicles rose from July to August, although they remained below the year-ago pace. Third District banks reported level loan volume, overall, and further declines in credit quality. Residential real estate agents generally noted steady sales of existing homes, although they noted that the sales rate remained below the year-ago pace. Nonresidential real estate leasing and construction activity continued to be slow. Service sector firms reported mainly steady activity at a slow pace. Business firms in the region reported mostly level input costs and output prices in August, although they noted some increases compared with July.

The outlook in the Third District business community was slightly better in August than at the time of the previous Beige Book. Although most contacts do not expect strong improvement in the immediate future, some now believe economic conditions are beginning to stabilize and that a slow pickup in activity might get under way in the near term. Manufacturers forecast a rise in shipments and orders during the next six months. Retailers are generally cautious, expecting only slight sales gains in the rest of the year. Auto dealers think sales will ease in the short term, but they believe that the sales rate might be better in the later part of the year than it was in the first half. Bankers anticipate demand for credit to remain soft as businesses and individuals continue to reduce indebtedness. Residential real estate contacts believe housing demand will continue to stabilize, although they expect only a slight improvement in market conditions during the rest of the year. Contacts in nonresidential real estate expect leasing and construction to remain weak during the rest of this year.

Manufacturing

Third District manufacturers reported a steady pace of shipments and a slight increase in new orders, on balance, from July to August. Although the rise in demand for area manufacturers' products has been slight, it has been fairly widespread among the

District's major manufacturing sectors. Some firms indicated that the increase in orders reflected inventory restocking by their customers, and some firms noted that they were gaining new customers as competitors have gone out of business.

Third District manufacturers forecast further gains, on balance. Among firms polled in August, slightly more than half expect new orders and shipments to increase during the next six months; less than one-tenth expect decreases. Although the number of firms expecting improvement has increased, most expect gains to be slight. For example, one firm said that "improvement will be moderate" and another remarked that "future projections are positive but we have no idea when overall conditions will improve." Capital spending plans among area manufacturers remain restrained. On balance, area firms plan just steady spending for new plant and equipment during the next six months. Manufacturers cited a variety of reasons for holding back on expansion plans, including slack demand for their products, difficulty in obtaining financing, and concern about possible future tax increases or federally legislated health insurance mandates.

Retail

Third District retailers reported a gradual rise in sales for the back-to-school shopping period in August. Sales of youth apparel were generally described as solid or strong, but sales of other lines of merchandise remained soft. Merchants said consumers' purchases have been "value-driven" and focused on immediate needs. Several retailers said consumers appeared to be cutting back on purchases of other goods to pay for back-to-school items. Most of the retailers contacted for this report said the late summer pace of overall sales has been below the sales rate during the same period last year. Third District retailers have mostly cautious views of the near term. They do not expect significant improvement in sales in the final months of the year, and they are strictly limiting inventories.

Third District auto dealers reported that the cash-for-clunkers program gave sales of new vehicles a strong boost in August compared with July, although sales for the month were below sales in August of last year. Dealers also said increased showroom traffic resulted in higher sales in August than in July of vehicles not eligible for the program. The sales spurt reduced dealers' inventories significantly. Looking ahead, dealers said sales could slip as a result of depleted inventories and the end of the rebate

program, but they expect manufacturers to step up production and introduce incentives to maintain sales momentum.

Finance

Total outstanding loan volume at Third District banks has been nearly level in recent weeks, according to bankers contacted for this report. There has been a small gain in consumer lending, but residential real estate lending and business lending have eased slightly. Most of the bankers contacted for this report said that demand for credit has been slack because both consumers and businesses are reluctant to add to indebtedness. However, some banks continued to tighten credit standards. One banker noted that “we are being more selective” in lending, and posting slower loan growth as a result. Most of the banks contacted in August said that credit quality continued to deteriorate for all categories of lending. Bankers generally expect demand for credit to remain weak in the near term as individuals remain focused on building up savings and businesses continue to reduce leverage.

Real Estate and Construction

Sales of existing homes in the Third District in July and August were fairly steady, according to local real estate agents. They generally indicated that a seasonally higher rate of sales that began in the spring remained on track; however, the sales rate remained well below the pace set in the past few years. The increase in sales has been more robust in the lower price ranges in most of the District, although agents in a few areas said there had been a recent upturn in sales of higher-priced homes. Nonetheless, throughout the District selling prices continued to run well below the levels achieved in the past two to three years. Real estate agents generally indicated that they believe the market is stabilizing, but they do not expect much strengthening in sales. One agent commented that “we’re just starting to see the market turn around,” and another said “I don’t see a big upturn in the rest of the year.” Residential builders reported a slight increase in sales from July to August. One builder’s comment was representative of most others: “Traffic at our sites hasn’t increased, but the people who show up are more serious about buying.” Builders believe consumer confidence is improving, bolstering the rise in home purchases. However, they expect the increase to be gradual. According

to area real estate contacts, prices of existing homes have been mostly steady, while prices of new homes have firmed up slightly in the past few months.

Nonresidential real estate firms indicated that leasing and purchase activity continued to be slow and that vacancy rates continued to rise for office, industrial, and retail buildings. There has also been an increase in sublease space coming on the market. Rents have declined. Several contacts noted that landlords have been focusing on maintaining occupancy and limiting rent declines in the face of “stagnant” or “nonexistent” demand for new space. Contacts also indicated that commercial real estate financing remained very difficult as secondary markets show no signs of recovery. Contacts expect nonresidential real estate leasing to remain weak into next year, and they see no signs that construction will strengthen in the near future.

Services

Service-sector firms reported little change in business conditions in August compared with July. In general, business services firms indicated that activity continued to be slow, although some that had reported declining activity earlier in the year said the slowdown appeared to be abating. Employment agencies reported a recent increase in demand for temporary workers, but they said demand for permanent employees had not yet picked up. The region’s service-sector firms generally expect very slow improvement in business conditions during the rest of this year and next year.

Prices

Reports on input costs and output prices have been mixed since the last Beige Book. Manufacturing firms noted some increases for the commodities they use, particularly metals and some other industrial materials. On balance, manufacturers have kept the prices of their own products steady. Retailers indicated that their cost of goods has been about steady, and they have kept selling prices in check, as well. Auto dealers reported some firming in transactions prices during the cash-for-clunkers sales rush. Some home builders reported rising construction costs due to increased local government permit fees.

FOURTH DISTRICT – CLEVELAND

The economy in the Fourth District has shown a slight improvement since our last report, though activity remains sluggish. Reports from factories indicated that production was flat to up slightly, with increases being attributed to new orders. New home construction remains weak, while nonresidential building activity was mixed. Credit availability continues to be an issue for residential and commercial contractors. Sales by District retailers were steady to down slightly. New motor vehicle sales received a substantial boost from the cash-for-clunkers program, whereas purchases of used vehicles slowed. Coal production fell, with little change noted in oil and gas output. Freight transport volume remains at low levels. Commercial and industrial loan activity was stable to declining. Consumer lending was generally characterized as soft, with indirect auto lending as the only bright spot in the consumer portfolio. Core deposits increased across the District.

Only modest employment declines were reported in commercial construction, banking, and coal mining. Reports from staffing firms showed that job openings were flat to up slightly. Given the weak labor market, wage pressures are contained. Increased prices for metals and lumber have moderated somewhat since our last report. Capital spending remains at low levels and little change is expected in the upcoming months.

Manufacturing. Reports from District factories showed that production was flat to up slightly during the past six weeks, with increases being attributed to new orders. On a year-over-year basis, factory output remains depressed. However, the year-over-year difference in output between this and previous reporting cycles is shrinking. Half of our contacts expect demand will remain at low levels going into 2010. While other contacts anticipate some improvement going forward, they are not expecting a return to 2008 levels. Most steel producers and service centers reported a slight pickup in shipping volume, which met or exceeded expectations. While no end markets stood out as being particularly strong, a few contacts anticipate a pickup in the auto industry. Our steel contacts expect current shipping trends to continue; nevertheless, they do not expect a substantial turnaround through year's end. District auto production fell modestly during July on a month-over-month basis. Production declines can be attributed, in part, to the aftermath of the GM and Chrysler bankruptcy proceedings and retooling for model changeovers. Production of both domestic and foreign nameplate vehicles in the District remained well below year ago levels.

Although capacity utilization remains below historic norms, several manufacturers noted improved utilization rates since our last report. In general, capital spending remains at low levels and little change is expected in the upcoming months. Reports show that increases in raw material prices (especially for metals) were beginning to moderate, though some upward

pressure on product pricing continues. There were only minimal reports of further cuts in payroll costs through layoffs, wage reductions, and curtailments in work hours. Wage pressures are contained.

Real Estate. The residential construction industry remains weak. Builders reported little change in activity during the past six weeks; nonetheless, two of our contacts said that sales are up on a year-over-year basis. Foot and Internet traffic was characterized as stable or increasing slightly, and sales trends are expected to remain at current levels or fall off slightly through year's end. Several builders told us they would like to construct a few spec houses, but they are unable to obtain financing. Sales of homes in the entry-level price category are doing well, which contractors attributed to the first-time home buyer tax credit. Lumber prices have declined from their seasonal high, while concrete prices remain elevated. General contractors continue to operate with skeleton crews, and subcontractors are available at competitive rates.

Reports on nonresidential construction were mixed, with some improvement seen by contractors participating in public works projects. Activity in private commercial and industrial building was characterized as slow due to declining inquiries and backlogs. All of our respondents said that business has fallen on a year-over-year basis. Looking forward, most contacts expect construction activity will be very weak during 2010. We continued to hear numerous accounts of difficulties in obtaining financing for private-sector projects. On balance, little change in construction materials prices was noted. A few general contractors reported laying off employees, while subcontractors are readily available.

Consumer Spending. July sales for District retailers were steady to down slightly on a month-over-month basis and were lower than a year earlier. Reports show that consumers continued to focus on purchasing necessities rather than discretionary items. Retailers' expectations for fourth-quarter sales were decidedly mixed. On balance, vendor and retail pricing has been stable. A few retailers noted that they have increased markdowns to move inventory. Reports from auto dealers indicated that, for the most part, new vehicle sales were up during July and early August due to the cash-for-clunkers program. Several dealers told us that sales equaled or were greater than those made in July 2008. However, we also heard reports of dealers not participating in the cash-for-clunkers program due to its complexities and delays in payments from the federal government. The cash-for-clunkers program and higher prices were cited as reasons for a slowing in purchases of used vehicles. Most dealers are uncertain about future sales due to weak economic conditions and difficulties in obtaining credit. On balance, there has been little change in staffing levels at retailers and auto dealers.

Banking. Demand for commercial and industrial loans was stable or declining, although a few community banks reported a continuing stream of business from refinancing loans that

were turned away by regional banks. Interest rates and credit spreads are either holding steady or increasing slightly. On the consumer side, loan demand is best characterized as soft, with interest rates holding steady for the most part. Indirect auto lending (new and used) has been the only bright spot in the consumer portfolio. Several bankers attributed part of the boost in indirect lending to the cash-for-clunkers program. Residential mortgage applications have slowed considerably since the second quarter, and most applications are for refinancing. Core deposits continued to grow across the District. Most bankers characterized loan applicants' credit quality as good or improving, especially on the consumer side. There continues to be a slight upward trend in delinquencies, with residential mortgages and consumer loans being the biggest contributors. Higher lending standards remain firmly in place, with no easing expected. Staffing levels are stable or decreasing, but most reductions have occurred over time through controlled attrition.

Energy. Coal executives reported a sharp decline in production, which they attributed to very weak demand from electric utilities. One executive noted that a boost to domestic producers may come from the Chinese, who have begun to import coal. Another executive said that contract prices for coal have dropped 50 percent on a year-over-year basis. Little change in oil and gas output was reported, though drilling activity has fallen off substantially or stopped. Spot prices for natural gas and oil continued to trend downward. Almost all of our energy contacts expect that production will remain flat or decline further in the near future. For the most part, the cost of production equipment and materials has fallen. Capital spending by coal producers has been put on hold, while expenditures by most oil and gas producers remain as projected. Employment levels in the oil and gas industry were largely stable, although coal executives reported workforce reductions and cuts in overtime.

Transportation. Freight transport executives reported that, for the most part, shipping volume has stabilized at low levels or continues to decline. Any pickup cited was attributed to competitors exiting the market. Shipping rates remain very competitive. Looking forward, a majority of our contacts expect slight incremental improvements in volume, based on increases in auto production and spending on infrastructure projects. They also anticipate continuing downward pressure on shipping rates. Several transport executives reported having difficulty renewing or increasing their lines of credit. Capital spending remains substantially below historic norms and is expected to remain at low levels for the next several months. On the labor front, most hiring is limited to driver turnover and a few management positions that opened due to attrition.

FIFTH DISTRICT-RICHMOND

Overview. While economic reports from Fifth District business contacts continued to indicate a relatively weak economy, continuing signs of improvement were apparent in many sectors. Manufacturers reported solid increases in shipments and new orders, while manufacturing employment stabilized. The rate of change in raw materials and finished goods prices also picked up a bit. Residential real estate agents across the Fifth District observed general improvement in home sales, particularly for low-to-middle priced houses, but reported declines in house prices. Mortgage lenders mentioned a pickup in purchase loans that was concentrated in low-to-middle tier homes. On the other hand, commercial real estate conditions softened further as leasing and sales activity remained weak and vacancy rates continued to rise. Demand for commercial loans remained subdued. Meanwhile, contacts at services firms noted a slight increase in revenues since our last report, while retail firms reported falling sales. Contacts across the service sector observed contracting employment and wages.

Retail. The retail sector continued to struggle, although exceptions were also noted. Contacts at home and garden businesses, department stores, and retail establishments said sales declined in recent weeks. In contrast, contacts reported some improvement in sales at grocery stores, a few building supply retailers in South Carolina, and a discount chain department store in central North Carolina. Automobile dealers said the cash-for-clunkers program had increased foot traffic and boosted sales, but most were uncertain about the sustainability of the increase. Two dealers told us that sales had risen so much across all lines of cars and light trucks that they were “scrambling” to rebuild inventory. However, dealers also complained that the delays in processing paperwork had reduced their cash flows. Retail merchants around the District generally continued to reduce inventories and payrolls; they also reported an overall decline in average wages. The moderate pace of increase in retail prices was little changed since our last report.

Services. Revenues at services firms grew slightly in recent weeks. Contacts at financial services firms told us that the improvement in the stock market had helped business. In addition, an executive at a central Virginia airport and executives at professional, scientific, and technical services firms all reported higher revenues since our last report. Despite the recent uptick, most contacts at services-providing firms continued to cut the number of employees. A recruiter of technical professionals in central North Carolina said that he was receiving numerous resumes, but “companies are hiring slowly and selectively.” Wages at services businesses continued to decline while prices edged down slightly.

Manufacturing. District manufacturers reported that activity continued to expand in late July and August. Contacts reported solid increases in shipments and new orders, and noted that employment stabilized after nearly two years of steady decline. A spark plug producer in West Virginia attributed a “huge increase in new orders” to the cash-for-clunkers program and indicated that his company expects to

see continued improvement. Similarly, a manufacturer of automobile seat covers in North Carolina said that business had improved at his firm, and a machinery parts manufacturer in South Carolina observed a pickup in demand for automotive parts and components. Moreover, an aerospace and broadcasting equipment producer in Virginia mentioned an upturn in new orders, which he attributed to increased federal government spending on space and missile defense coupled with heightened demand for commercial satellite-based services. Contacts indicated that both raw materials and finished goods prices increased at a somewhat quicker pace than in our last report.

Activity at District ports generally improved in recent weeks, but remained notably below year-ago levels. Contacts noted an increase in both auto imports and exports in July, as well as strengthening in certain niche products such as power generators. However, port officials stated that retail imports for the holiday shopping season were down from the previous year, and that several ship lines had recently consolidated service routes or reduced vessel capacity.

Finance. Residential mortgage lenders reported slow but steady activity in recent weeks. Contacts noted a pickup in new mortgages, while demand for refinances continued to dwindle. Purchase loans were generally for lower-end homes, although some lenders reported an increase in loans for middle-tier homes. Credit standards at a number of District institutions were unchanged, while other institutions tightened guidelines further, increased scrutiny on appraisals, and allowed for “less leniency in gray areas.” On the commercial front, recent lending activity was on pace with June and early July. Contacts noted that demand remained soft, with companies hesitant to make capital expenditures and take on additional debt. Loan terms and conditions continued to tighten at some institutions; others reported no recent changes and expressed a “growing appetite” to lend to good-quality customers. Credit quality of existing clients deteriorated further since our last report, although lenders noted the pace of deterioration had abated somewhat.

Real Estate. Residential real estate agents reported generally improved housing market conditions in recent weeks. Realtors in Washington, D.C., Fairfax, Va., and Richmond, Va., reported increased sales since our last report, with the Richmond agent adding that first-time homebuyers and the expiring federal tax credit were driving the increase in his market. Agents in North and South Carolina also reported generally improved housing markets. In Greenville, S.C., a contact reported a “nice surge” in sales, and increased foreclosure sales fueled activity in the Greensboro, N.C., market. While the low-to-middle priced houses sold the fastest overall, contacts in Richmond and Washington, D.C., reported increased house sales in the higher price brackets as well. House prices decreased across much of the District, which an agent in Asheville, N.C., “hoped” would help to reduce inventory in his market.

In commercial real estate, leasing activity remained weak. Agents reported that deals were continuing to be completed, but clients were slow to make decisions. Effective rental rates softened further in recent weeks and asking rates began to decline in the Raleigh, N.C., market. Concessions –

particularly free rent – remained prevalent throughout the District, although tenant improvements were less common as landlords reportedly sought to conserve cash. Vacancy rates climbed higher across office, industrial, and retail space in most District markets, while the amount of available office sublease space remained fairly steady since our last report. On the sales side, very little activity was reported in recent weeks. Contacts reiterated that tight credit conditions were dampening sales prospects. Sales price trends were difficult to detect in most markets due to a lack of activity, although prices did reportedly edge lower in Richmond, Va., and Charlotte, N.C. Reports of commercial foreclosures were generally scarce, although agents in Washington, D.C., Richmond, Raleigh, and Charlotte reported a few instances of clients “turning in keys.”

Tourism. Tourist activity was generally stronger since our last report. Along the coast, contacts from Virginia Beach, Va., Myrtle Beach, S.C., and the Outer Banks of North Carolina all noticed an increase in occupancy rates. An hotelier in Virginia Beach told us that they were having an “amazing summer” with 99 percent occupancy, while a contact from Myrtle Beach attributed his increased bookings to continued discounting and aggressive packaging. In contrast, the contact on the Outer Banks of North Carolina reported little discounting at hotels and motels, but noted huge markdowns for rentals. Tourist activity at mountain resorts varied. A manager at a mountain lodge in Virginia reported stronger bookings compared to our last report and to a year ago, and credited the increase to families “staying regional.” In contrast, a respondent at a mountain resort in West Virginia reported a 10 percent decline in bookings, noting a very wet summer with record-breaking rainfall.

Temporary Employment. Agents at temporary employment offices continued to report generally sluggish demand for workers since our last report. A contact in Hagerstown, Md., described demand as “very weak,” adding that he did not expect much improvement over the next several weeks. Several contacts, however, noted some improvement and were optimistic about demand over the next few weeks due to the improving economy and an increase in manufacturing orders. In addition to machine operators, experienced supervisors and administrative staff, workers most in demand included those in sales, IT, and other technical disciplines.

Agriculture. Agricultural conditions were mixed since our last report. In South Carolina, climatologists indicated that some areas of the state approached drought-like conditions, and analysts in North Carolina and West Virginia reported that some places were still in need of rain. In other areas however, widespread rainfall significantly improved field crops and hayfields. In Maryland and Virginia, the vegetable harvest was underway and the peach harvest was nearing completion in South Carolina. Moreover, the soybean crops in Maryland and South Carolina were reported to be in good condition.

SIXTH DISTRICT – ATLANTA

Summary. Sixth District business contacts in several industries reported signs of stabilization in economic activity through August. Retail merchandise and tourism-related spending was described as being little-changed. However, auto industry contacts cited a sharp increase in sales as a result of the cash-for-clunkers program. Reports from real estate contacts indicated that the pace of decline in home sales continued to moderate in most areas compared with the same time a year earlier, while Florida Realtors noted continued sales gains from very low levels. The inventory of unsold homes remains elevated, in part because of the continuing supply of foreclosed properties, and this is said to be keeping downward pressure on home prices. Commercial real estate activity softened further as vacancy rates rose, rents declined, and more projects were delayed. Manufacturing activity continued to improve as reports of new orders and production levels increased. Banking contacts reported that credit availability remained tight. The pace of layoffs broadly slowed, but few contacts outside of temporary staffing noted any plans to expand payrolls in the near term. Prices remained generally stable. Most business contacts reported that they had no plans to hike prices or raise wages in the current environment.

Consumer Spending and Tourism. A majority of District retailers cited that sales and traffic continued to remain moderately below year-ago levels, and this was largely in line with their expectations. Most retailers mentioned that they had adjusted inventories to lower levels that were in line with expected sales. The outlook among merchants remained largely unenthusiastic with regard to a near-term upturn in retail sales.

Auto dealers from across the District indicated that the cash-for-clunkers program significantly helped stimulate traffic and sales from late July to mid-August. Many dealerships reported that the demand for fuel-efficient vehicles outpaced availability. Many also noted concern over the sustainability of the recent pace of sales now that the cash-for-clunkers program has ended.

According to most hospitality industry contacts, travel-related spending remained sluggish in most parts of the region. Hotel reservations were down for both leisure and business-related travel, with bookings supported by aggressive discounting. Most industry contacts reported lower revenues, and reduced profit margins. They generally expect subdued activity to persist over the next few months.

Real Estate and Construction. Reports from most District homebuilder and Realtor contacts indicated that the pace of decline in home sales continued to moderate in July and early August from a year earlier. In Florida contacts actually experienced year-over-year gains in sales, particularly for existing homes. However, downward pressure on home prices persisted. Both Realtors and homebuilders noted that increases in supply because of foreclosures and short-sales were partially responsible for the price declines even as sales increased. Georgia homebuilders also cited difficulty competing with foreclosed home prices. Demand for starter homes remained relatively strong across the region and a pickup in sales of mid-market homes was also noted in some areas. The majority of homebuilders and contractors reported that new home construction remained at very low levels. The outlook among both builders and Realtors continued to rebound, with the majority anticipating positive year-over-year sales growth over the next several months.

Commercial real estate activity continued to trend lower since last reported. Most contacts characterized activity as weakening. Vacancy rates increased further, with greater downward pressure on rents noted among contacts. Developers also continued to report fewer projects in the pipeline overall, and delays in existing work. However, contacts in Alabama and the Mississippi coast did note some projects that had been on hold have recently moved ahead. Most contractors continued to anticipate that the level of commercial construction will continue to decline into 2010. Similarly, commercial Realtors anticipate continuing weak demand for existing space – particularly in the office sector.

Manufacturing and Transportation. Several manufacturing contacts noted increases in new orders and production levels. In particular, auto plants throughout the region reported a sharp rise in production. Most manufacturers indicated that their outlook for future production and sales improved. However, most contacts also anticipated that employment would likely remain at low levels, with any extra demand absorbed using existing staff.

Trucking contacts reported that most regional companies are continuing to experience weak freight demand, lower revenues, and excess trucking capacity. However, year-over-year declines in rail shipments of metal ores, scrap metals, and chemicals were said to have moderated in July and early August.

Banking and Finance. Banking contacts continued to remark that credit availability remained tight. Several reports mentioned that the commercial real estate market continued to be affected by tighter lending standards. Banks were cited as remaining cautious on loan approvals,

subjecting borrowers to increased equity requirements, continued scrutiny of appraisals, and generally applying stricter credit standards.

Employment and Prices. District business contacts noted that the pace of layoffs decelerated in July and August. But few contacts noted any plans to increase payrolls. Some employment services contacts reported a modest increase in placements, however. Few reports cited any pressure to raise wages.

Construction and manufacturing firms reported that raw material prices had generally moderated by mid-August after having increased in late spring. Most business contacts also noted that they were unsuccessful in attempts to pass on any increased input costs to their customers. District retailers reported that retail prices remained stable relative to year-earlier levels.

Natural Resources and Agriculture. Drilling activity in the Gulf of Mexico continued to decline in July and August, with the number of rigs in operation almost 50 percent lower than a year earlier. Crude oil and gasoline inventories in the Sixth District remained well above their seasonal averages, with declines in drilling and refining only partially offsetting weakness in domestic energy consumption.

Most District farms benefited from precipitation that improved soil moisture conditions. However, weak domestic and international demand continued to trouble the near-term outlook for the region's cotton and poultry industries.

SEVENTH DISTRICT—CHICAGO

Summary. The decline in economic activity in the Seventh District leveled off in July and August. Contacts generally agreed that activity had stabilized at a low level, and were cautiously optimistic for a recovery over the remainder 2009. Overall, consumer spending increased from the previous reporting period, and the decline in business spending slowed. Manufacturing and construction remained at low levels, although both sectors showed signs of improvement. The pace of job loss slowed, and credit conditions improved. General price and wage pressures were minimal, and agricultural prices retreated further.

Consumer spending. Overall consumer spending increased in July and August. New auto sales were strong in large part due to cash-for-clunkers with Illinois among the top five states to make use of the program. Greater showroom traffic also led to an increase in sales of used autos. Some contacts indicated that the program created demand that otherwise would not have existed, while others suggested that it had simply pulled forward demand. Several dealerships suspended their participation in the government program over concerns about the slow rate of reimbursement. Inventories of all qualifying vehicle segments were significantly reduced to low, but comfortable levels. Retail sales excluding autos decreased slightly from the previous reporting period. Consumers continued to spend on essentials like health and personal care items, but sales of big-ticket items such as electronics, appliances, and furniture remained weak. Retailers also reported planning to maintain low inventories as they expected spending to continue to be weak.

Business spending. The decline in business spending slowed in July and August. Inventory reductions ebbed. Firms remained cost-conscious, limiting spending and hiring. Several contacts indicated that low levels of working financial capital along with tight credit markets would continue to constrain business investment. In addition, contacts in the manufacturing sector expressed reservations about how quickly they could increase production when conditions warranted given the degree to which they had cut back on workforces. Labor market conditions continued to be weak. Hiring was limited outside of healthcare and information technology. However, the rate of job loss slowed, and not as many contacts noted layoffs or reducing hours this reporting period. In addition, a large staffing firm indicated that billable hours had increased in recent weeks. In the auto industry, several contacts reported bringing back previously laid off workers as well as increasing hours or the number of shifts. However, some contacts questioned the sustainability of this ramp-up.

Construction/real estate. Overall, construction activity in the District remained weak in July and August. Residential construction increased from the previous reporting period, with builders indicating cancellations had declined and contract signings had increased. However, the level of activity remained low with housing inventories elevated (but coming down) and credit still tight for developers. Single-family home sales increased and prices stabilized. In contrast, significant reductions in condo prices were reported. The availability of financing continued to be a concern for potential condo buyers. Contacts also noted that many unsold condos were being converted to apartments, putting downward pressure on residential rents. Private nonresidential development and construction were weak. Contacts were concerned about sharp declines in commercial real estate prices, elevated vacancy rates, and the rising inventory of buildings for sale, all of which contributed to a decline in commercial rents. Commercial real estate developers also noted the limited availability of credit. Contacts indicated that the fiscal stimulus program was having a limited impact on public construction with the exception of road building and repair.

Manufacturing. The decline in manufacturing activity in the District flattened out in July and August. Overall activity remained low, but contacts noted an increase in orders. It was unclear, however, the degree to which orders were increasing due to a sustained increase in final demand or the need to replenish lean inventories. For instance, a chemical manufacturer reported that orders had been rising for several months and that this increase was more indicative of a broad-based recovery in demand. On the other hand, a contact in the steel industry said that increased activity stemmed mostly from lean service center inventories, with final demand expected to increase only gradually through the rest of 2009. More generally, other metals-related manufacturers indicated weak, but firming activity. Automakers reported plans to increase production and automotive suppliers saw this showing through in higher orders. Power generation, medical devices, and pharmaceuticals all remained bright spots for manufacturing. Furthermore, exports to Asia, Mexico, and Europe were reported to have increased. In contrast, heavy equipment manufacturers continued to struggle, as did manufacturers with ties to residential housing. Demand for heavy and medium duty trucks also remained low, with contacts noting that excess capacity combined with upcoming EPA regulations had resulted in greater demand for used equipment.

Banking/finance. Credit conditions in the District improved from the previous reporting period. There was a general improvement in the cost and availability of credit for businesses and consumers. Demand for auto loans increased considerably with the rise in sales. Consumer loan

quality improved further, with the exception of home equity loans. A contact noted, however, that consumer bankruptcies continued to increase. Banking contacts indicated that the number of creditworthy borrowers had increased, and in response they were making credit more available than in recent months. In addition, a contact noted that even though Treasury yields had risen, borrowing costs for a number of area corporations had declined as credit spreads had narrowed considerably. Contacts in banking also reported less deterioration in loan quality. Commercial real estate was an exception and remained a source of concern with many loans coming due for refinancing in 2010. A contact noted that his bank had been aggressively pursuing modifications of these loans to avoid potential problems in the future. In addition, credit conditions for agriculture deteriorated.

Prices/costs. Price pressures were not significant on balance in July and August. Contacts reported increases in several metals prices including steel, copper, and nickel as well as higher rail freight shipping costs. In contrast, utility costs softened a bit, and the price of natural gas remained very low. A contact indicated that cooler weather in the Midwest, a surplus of stored gas, and a mild hurricane season all suggested that natural gas prices would remain low. Contacts also noted continued declines in food and paper prices, and retailers reported that wholesale prices were still low. Wage pressures were not significant, although downward pressure on non-wage pay and benefits was subsiding. Pass-through of wage and price pressures to downstream prices was minimal as contacts indicated pricing power remained limited.

Agriculture. The conditions of the District's corn and soybean crops were about the same as a year ago. Cool temperatures slowed maturation and both crops continued to trail the pace of normal development. However, in most of the District there is adequate moisture to produce strong yields. However, contacts were concerned about diseased soybeans cutting yields. Corn and soybean prices decreased further during the reporting period, although soybean prices recovered some in August. With the drawdown of stocks before the upcoming harvest, the premium on old over new crop forward contracts increased. Hog prices declined, heightening pressure to renegotiate long-term contracts. Dairy prices received support from the U.S. Department of Agriculture. A source reported that with prices remaining insufficient to cover costs for many producers the livestock industry was getting "killed." Margins moved up in the ethanol industry due to lower input costs. With agricultural income down a lot from last year, operating budgets were tighter.

Eighth District - St. Louis**Summary**

Economic activity in the Eighth District remained weak, but the pace of decline has moderated since our previous report. Both manufacturing and services activity contracted at a slower pace. Retail and auto sales in July and the first part of August were down from a year ago. Residential and commercial real estate markets conditions continue to be weak. Overall lending activity at a sample of large District banks decreased moderately in the three-month period ending in July.

Consumer Spending

Contacts reported that retail sales in July and the first part of August were down, on average, over year-earlier levels. About 58 percent of the retailers surveyed saw decreases in sales, 33 percent saw increases, and 8 percent saw no change. About 37 percent of respondents reported that sales levels met their expectations, 42 percent reported that sales were below expectations, and 21 percent reported that sales were above expectations. Lawn and garden products and less-expensive items were strong sellers, while apparel and big-ticket items moved more slowly. About 46 percent of the contacts noted that inventories were at desired levels, 42 percent reported too-high inventories, and 12 percent reported too-low inventories. About 46 percent of the retailers expect sales for September and October to increase over 2008 levels, 46 percent expect sales to decrease, and 8 percent expect sales to be unchanged.

Car dealers in the District reported that, compared with last year, sales in July and the first part of August were down slightly, on average. One-third of the car dealers surveyed reported large decreases in sales, one-third reported increases in sales (mostly attributed to the cash-for-clunkers program), and the remaining one-third reported no change in sales. About 37 percent of the car dealers noted that new car sales had increased relative to used car sales, while 25 percent reported the opposite. Also, 33 percent reported an increase in low-end vehicle sales relative to high-end vehicle sales, while 8 percent reported the opposite. About 46 percent reported more rejections of finance applications, but 12 percent reported more acceptances. Two-thirds of the car dealers surveyed reported that their inventories were too low,

while 12 percent reported that their inventories were too high. About 46 percent of the car dealers expect sales for September and October to increase over 2008 levels, 37 percent expect sales to decrease, and the remaining 17 percent expect sales to be unchanged.

Manufacturing and Other Business Activity

Manufacturing activity continued to decline since our previous survey, but at a slower pace. Some contacts in petroleum refineries/coal manufacturing reported an increase in production and opened new facilities. One firm in chemical product manufacturing announced plans to upgrade existing facilities and hire new workers. Some firms in furniture manufacturing and rubber tire manufacturing reported plans to hire additional workers. In contrast, contacts in the animal slaughtering/processing, tobacco, household appliance, rubber products, transportation, and machinery manufacturing industries reported plans to lay off workers and decrease operations. A firm in auto parts manufacturing announced that it will close a plant in the District, while another auto parts manufacturing firm announced plans to lay off employees.

The District's service sector continued to decline in most areas, but at a slower pace. Contacts in business support services and social services reported plans to close facilities and lay off workers. In contrast, government service jobs continued to be added because of the fiscal stimulus plan.

Real Estate and Construction

Home sales continued to decline throughout the Eighth District. Compared with the same period in 2008, July 2009 year-to-date home sales were down 8 percent in St. Louis, 12 percent in Little Rock, 13 percent in Louisville, and 15 percent in Memphis. Residential construction also continued to decline throughout most of the District; 2009 year-to-date single-family housing permits fell in most District metro areas compared with the same period in 2008. Permits declined 19 percent in Little Rock, 28 percent in St. Louis, 30 percent in Louisville, and 49 percent in Memphis.

Conditions in the commercial and industrial real estate markets were mixed throughout the District. Compared with the first quarter of 2009, second-quarter 2009 industrial vacancy rates increased

in Little Rock, Louisville, and Memphis and decreased in St. Louis. During the same period, suburban office vacancy rates increased in Little Rock and Louisville and decreased in Memphis and St. Louis. Downtown office vacancy rates remained fairly constant in St. Louis, increased in Louisville and Memphis, and decreased in Little Rock. Commercial and industrial construction markets continued to decline. One contact in Memphis reported that new commercial construction is minimal. A contact in Louisville does not expect nonresidential construction to improve until 2011.

Banking and Finance

A survey of senior loan officers at a sample of large District banks showed a moderate decrease in overall lending activity for the three-month period ending in July. Credit standards for commercial and industrial loans were somewhat tighter for both large and small firms, while demand for these loans was moderately weaker. Credit standards for commercial real estate loans were also somewhat tighter, while demand for these loans was moderately weaker. Meanwhile, credit standards for consumer loans were basically unchanged, while demand for these loans was mixed, ranging from moderately weaker to moderately stronger. Credit standards for prime residential mortgage loans remained basically unchanged, while credit standards for nontraditional residential loans tightened. Demand for all types of residential loans ranged from about the same to stronger.

Agriculture and Natural Resources

The overall condition of the corn, soybeans, rice, cotton, and sorghum crops in the District has improved slightly: No more than 10 percent of each crop obtained a rating of poor. As of August 1, yields for most of the major crops in each District state were expected to be at least 94 percent of last year's yields, although sorghum yields and winter wheat yields were expected to be 84 percent and 80 percent of last year's yields, respectively. Since our previous report, soil moisture ratings and pasture conditions have improved in most District states.

NINTH DISTRICT--MINNEAPOLIS

Overall economic activity in the Ninth District was flat since the last report. Modest decreases in activity occurred in consumer spending, agriculture, and commercial real estate and construction. Tourism was mixed, while activity in services and residential construction was flat. The manufacturing, energy, mining and residential real estate sectors saw moderate increases. Labor markets were mixed, and wage increases were subdued. Prices remained relatively stable since the last report.

Consumer Spending and Tourism

Overall retail spending remained soft, except for auto sales, which were boosted by the cash-for-clunkers program. A major Minneapolis-based retailer reported that same-store sales in July were down 7 percent compared with a year earlier. Same-store sales at two Minneapolis area malls were down 4 percent and 8 percent, respectively, compared with last year. A Minnesota-based bed retailer reported that same store sales edged up in July, but the slight growth was supported by a number of closings of lower-performing stores during the past year. In addition, contacts noted back-to-school shoppers were focusing on value.

The cash-for-clunkers program jump-started auto sales across the District. A representative of an auto dealers association in North Dakota reported that most recent activity at showrooms was associated with the program. Auto inventories were low in Minnesota as a result of rebate-driven sales, according to a representative of an auto dealers association. Contacts noted some concern about the program's impact on future sales—that the incentives drove sales that would have occurred in the fall into a condensed period of time.

Tourism was mixed, as visitor numbers were solid, but spending was soft in some areas. The number of visitors in July to Yellowstone National Park was up 11 percent compared with a year ago; however, spending at nearby restaurants and retail stores has been slow. Visits to attractions and overall highway traffic were up about 10 percent compared with a year ago in western South Dakota, while business at hotels was flat, according to a tourism official.

Services

Overall activity was flat in the professional business services sector. Contacts who provide professional services to the commercial real estate sector noted a downturn in business. Architects reported extremely low activity levels—the same as the last report. Contacts from the legal sector also reported that activity was the same, but many customers were asking for lower fees. Professional services firms that support the health care and government sectors noted an uptick in activity.

Construction and Real Estate

Commercial construction activity mostly decreased, with some bright spots noted in public construction projects. Few office, retail or industrial projects were under way. However, road construction was strong throughout the District. Runway reconstruction was in progress at the Minneapolis-St. Paul airport. Residential construction was stable at low levels. July building permits were about even with a year earlier in Rochester, Minn., and Sioux Falls, S.D.; however, the value of permitted units fell 46 percent in Minneapolis-St. Paul.

Commercial real estate was weak. According to a commercial real estate firm in Minneapolis-St. Paul, retail vacancy reached its highest level on record; industrial absorption was at record lows. A commercial broker in Fargo, N.D., said market activity there was stable though slightly lower than in recent years. Residential real estate showed continued improvement. July home sales in Minneapolis-St. Paul were up 16 percent from a year earlier, but median sale prices were down 18 percent. Home sales also increased in Duluth, Minn.; however, they decreased in Sioux Falls, S.D., and Michigan's Upper Peninsula. Meanwhile, sales of vacation properties were down significantly from last year across the District, particularly in western Montana.

Manufacturing

Manufacturing activity was up slightly. A July survey of purchasing managers by Creighton University (Omaha, Neb.) indicated that manufacturing production was flat in Minnesota but increased in the Dakotas. A Minnesota plastic injection company expanded production, and an auto assembly plant plans to expand output. In Montana, a bridge parts maker is building a factory. A seed oil processing plant is planned in North Dakota. A South Dakota generator component producer plans to open a new facility.

Energy and Mining

Activity in the energy and mining sectors increased slightly. Mid-August oil and gas exploration edged up from early July. An oil services company is building a facility in North Dakota. Two large wind energy projects were approved in North Dakota. Due to increased demand, an iron ore mine in northern Minnesota plans to start up three previously idled production lines.

Agriculture

Agricultural conditions declined since the last report. Results of the Minneapolis Fed's second-quarter (July) survey of agricultural credit conditions indicated that lenders expect overall

agricultural income and spending to decrease in the third quarter. Due to wet weather, the Montana wheat harvest is behind schedule. Farmers are nervous about an early frost, as the progress for the District corn and soybean crops is behind its five-year average pace. The western part of the District experienced scattered grasshopper infestations, and parts of northwestern Wisconsin were in severe drought.

Employment, Wages and Prices

Overall labor markets were mixed. In Minnesota a defense contractor laid off over 300 workers, a boat manufacturing plant also cut over 300 workers, about half of its labor force, and a medical device manufacturer announced plans to reduce staff by 200 companywide. A meatpacker in South Dakota laid off 30 workers. Competition for seasonal work was much greater this summer compared with a year ago in many areas of the District.

In contrast, month-to-month gains in employment were recorded in Minnesota, Montana and South Dakota during July. Federal economic stimulus funds have created a number of road construction jobs. For example, the state of Montana estimated that stimulus spending created 140 jobs by the end of July, which does not include any indirect jobs at businesses that provide goods and services to construction projects and construction workers. In North Dakota, 120 workers will be added to a coal-fired power plant construction project during late August and September.

Wage increases were subdued. For example, the state of Montana has frozen wages for two years. Several architectural firms reported decreased employee compensation.

Prices remained relatively stable since the last report. Minnesota gasoline prices were only slightly higher at the end of August compared with early July, but were \$1.15 per gallon lower than a year ago. Tuition will increase about 5 percent this fall at Minnesota state colleges and universities; federal stimulus dollars will cover 2 percentage points of that increase. Metal prices increased a tad during July, but remained mostly level during the month of August; metal product prices were well below year-ago levels.

TENTH DISTRICT - KANSAS CITY

The Tenth District economy generally held steady in late July and August. Consumer spending was supported by seasonal and automotive incentives, while restaurant and hotel spending was subdued. The manufacturing sector held steady and plant managers expected a modest rise in production in coming months. Residential real estate activity softened and commercial real estate contacts indicated market conditions remained fragile. Banking conditions remained tepid partly due to moderately declining loan demand and a negative outlook for loan quality. Activity in the energy sector stabilized with a slight rise in the number of active drilling rigs. Falling grain prices and weak livestock exports put downward pressure on agricultural profits. Even though input prices were expected to rise, producers did not anticipate passing additional costs through to retail prices. Wage pressures remained low and few firms planned to hire new workers.

Consumer Spending. Consumer activity since the last survey period was generally stable. Retail sales were supported by consumer purchases of seasonal products, especially apparel, during the back-to-school season. Increased customer traffic led some District retailers to expect a rise in sales. Auto dealers reported that the cash-for-clunkers program, along with other dealer incentives, stimulated sales of new, fuel efficient cars, but hindered used car sales. Still, vehicle inventory levels declined. In addition, fewer dealers reported difficulty accessing credit. Restaurants reported weaker sales partly due to a decline in average check size. Tourism spending remained solid but was expected to wane as the vacation season ends. Even though hotel occupancy rates have fallen, average daily room rates rose slightly.

Manufacturing and Other Business Activity. Since late July, activity in the manufacturing sector was mostly flat, while activity in the transportation and high-tech sectors strengthened. Durable goods production dropped while non-durable goods production held steady. After further inventory reductions, manufacturers expected production to strengthen in coming months. In addition, plant managers anticipated current employment levels would hold and capital spending would remain stable. Several transportation contacts noted improved

activity partly from an uptick in raw material shipments. Technology-related firms reported stronger sales, supported by federal government contracts and stimulus spending. Some manufacturing and transportation contacts felt input price increases could trim profit margins because of limited opportunities to pass through additional costs.

Real Estate and Construction. After strengthening in the last survey period, the residential real estate market softened, while commercial real estate conditions weakened further. While residential real estate agents noted increased buyer traffic, building suppliers reported slower sales to builders for new home construction. Demand remained weak for high-end properties, although the first time homebuyer tax credit boosted sales of entry-level homes. Following seasonal trends, home inventory levels were expected to rise in coming months. Mortgage activity slowed, largely due to a drop in refinancings. Commercial real estate conditions continued to erode, with reductions in completions and construction underway. Vacancy rates were little changed since the last survey period, but remained well above year-ago levels. Absorption rates declined further, placing additional downward pressure on rents. Access to credit remained tight. District contacts were concerned that lower commercial real estate values would hinder upcoming loan renewal and refinancing activity.

Banking. Bankers reported weaker loan demand, increased deposits, and a continued negative outlook for loan quality. Overall loan demand declined at a slightly faster pace than in the previous survey. Demand for commercial and industrial loans and commercial real estate loans fell moderately, while demand for consumer installment loans continued to edge downward. Bankers also reported lower demand for residential real estate loans for the first time since late last year. Some banks continued to tighten credit standards on commercial real estate loans, but credit standards for other loan categories were little changed. Loan quality remained substantially lower than a year ago, and about half of respondents expected loan quality to decline further over the next six months. Deposits rose moderately after showing little change in the previous survey.

Energy. Energy activity stabilized in late July and August. After substantial declines during the last year, the number of active drilling rigs in the District rose slightly. Drilling

activity was expected to hold steady in coming months due to ample oil and natural gas supplies, subdued demand, and limited availability of financing for exploration. Though some natural gas producers expected prices to rise as the winter heating season approached, others felt high inventory levels would restrain price increases. Wyoming coal production rose during the survey period but remained below year-ago levels. Ethanol profit margins stabilized with higher crude oil prices and lower corn costs.

Agriculture. While agricultural growing conditions remained positive, income projections weakened slightly since the last survey period. Favorable growing conditions and an upward revision to crop estimates contributed to a decline in corn and soybean prices, trimming expected profits for producers. Despite a slight improvement in fed cattle prices, an extended period of negative profit margins coupled with declining cattle inventories prompted some feedlot consolidations. Income losses steepened for hog producers amid sluggish domestic and foreign demand for pork products. Farmland values stabilized at or above year-ago levels. Demand for non-real estate farm loans rose, and the rate of loan repayments declined. Fewer District contacts reported that collateral requirements remained elevated, and farm interest rates were little changed.

Wages and Prices. Producer prices generally held steady while consumer prices eased, and soft labor markets kept wage pressures low. Though manufacturers reported that input prices leveled off since the last survey period, some plant managers anticipated an increase in the cost of raw materials, especially fuel and steel. Still, most firms did not plan to raise prices on finished goods. Builders noted higher costs for petroleum-based materials such as roofing shingles, and transportation industry contacts also commented on rising oil prices. Retailers continued to discount prices and anticipated further price reductions, while restaurants held menu prices steady. Few contacts reported difficulty hiring workers, and the majority of firms did not plan to raise wages.

ELEVENTH DISTRICT—DALLAS

Economic activity in the Eleventh District firmed somewhat over the past six weeks, with contacts in several industries suggesting a pickup in demand. Despite the slight improvement, several contacts expressed disappointment that conditions had not improved more. While outlooks are less gloomy than earlier in the year, most contacts are hesitant to predict a significant turnaround in the near term.

Prices Excess capacity in many industries kept a lid on price pressures. Most contacts said prices were holding steady although a few noted continued declines, as firms make concessions in order to get business. Raw materials prices were mostly stable, but contacts noted higher fuel costs continue to squeeze margins. There were reports by metals producers and construction industry contacts that prices for steel and aluminum were ticking up.

Crude oil prices strengthened in late July and have remained near \$70 per barrel since then. Gasoline prices rose by about 10 cents a gallon during the reporting period and diesel was up 15 cents per gallon. Natural gas prices moved up to over \$4 per Mcf in early August but more recently fell under \$3 per Mcf for the first time since 2002. Historically high inventory levels are putting downward pressure on natural gas prices.

Labor Market Employment levels remained steady overall as most respondents have already right-sized their staff levels. Some said they prefer to work current employees overtime, rather than hire new workers, only to let them go if conditions worsen. Staffing firms noted a slight improvement in demand, and there were reports from high-tech and paper respondents that temporary hiring had edged up. In contrast, consolidation in the airline, residential construction and energy industries led to further reductions in headcounts. Wages remain unchanged and there are no signs of upward pressure. Firms continue to institute wage and hiring freezes, and there were additional reports of freezes on company 401(k) contributions.

Manufacturing Construction-related manufacturers said orders held steady at extremely low levels. A few respondents noted disappointment that prior expectations of recovery had not been met. There has been a sluggish start to the “shovel-ready” projects covered under the stimulus plan, and funding has been slow to materialize. Most contacts expressed uncertainty in their outlooks as both residential and commercial construction activity remain depressed, and there is little evidence that conditions will improve in the near-term.

Respondents in high-tech manufacturing said orders increased moderately since the last report. One respondent noted orders were stronger than expected because customers were no

longer sharply paring back inventories. Another contact said demand for electronic components used in automobiles had increased at a strong pace. In general, respondents expect demand to continue to grow at a mild pace over the next three months, yet uncertainty remains prevalent.

Conditions in the paper industry were weak but stable. Several large box manufacturers said orders held steady over the past six weeks and were above levels seen at the beginning of the year. The exception was for producers that sell to the construction industry where demand remains quite poor. Food manufacturers noted a slight increase in the pace of sales in recent weeks, although the level of demand remains moderate. Transportation manufacturing contacts said weakness in the commercial airline industry kept demand for aircraft parts at low levels.

Petrochemical demand was mixed. Producers that sell to domestic manufacturing or auto-related markets cited an increase in demand, but manufacturers of vinyl products such as PVC said domestic sales remained weak, despite some improvement in the housing market. Some producers said export demand from Europe and Asia was strong due to the cost advantage of domestic natural gas-based products over oil-based products. Refiners said demand for oil-based products rose since the last report but remains well below the peak in early 2008. Inventories for most products are high and refiners cut production slightly due to poor margins. Demand for energy-related products such as bits and drill pipe was weak and manufacturers continue to operate facilities at very low capacity.

Retail Sales Retailers report that consumers remain cautious, keeping overall sales flat at low levels. Value-based respondents noted sales were not as robust as expected given the back-to-school season. Texas-based department stores said August sales trailed the national average but strengthened during the state's "tax-free" weekend. While contacts say "things are up off the bottom," outlooks suggest it will be some time before we see a consumer-based rebound.

Auto dealers said demand was boosted by the cash-for-clunkers program, but they expect sales to drop back down to lower levels now that the program is over. The increase in sales drew down inventories, putting dealers in a better position. Several contacts noted a delay in receiving checks from the government and difficulty with the program's stringent paperwork.

Services Staffing firms report a broad-based uptick in contract activity but say that "it is nothing to get excited about," and demand for direct hires is still extremely slow. The pickup in orders for contract work has improved contacts' assessments of current conditions, but the outlook continues to be cautious. Demand for legal services held relatively flat at depressed

levels with the exception of energy-related activity. Contacts in accounting services say demand is “muddling along,” and apart from a seasonal uptick in early fall they do not expect improvement in the near term.

Demand for air travel remains weak but conditions have stabilized and the outlook is more optimistic than in previous reports. Small parcel shipping firms said a pickup in demand from the transportation and non-durable retail sectors led to positive growth in volumes, which they expect will continue through the third quarter. Container trade volumes rose in August, although the forecast is for a year-over-year decline in 2009. Railroads reported a modest, broad-based increase in shipments, and a rise in contract prospects has improved company outlooks.

Construction and Real Estate Sales of low-to moderately-priced homes continued to improve over the past six weeks as buyers took advantage of the first-time homebuyer tax incentive. Sales of higher priced homes and condos remained slow according contacts. New home construction ticked up, but some respondents said it was more related to inventory replacement than sustainable improvement in demand, as builders had depleted most of their standing inventory during the downturn. Home values continue to hold up better in Texas than in many other areas of the country, and respondents were pleasantly surprised by recent figures that suggest prices may be firming. Despite some positive signs, contacts are hesitant to suggest a sustained recovery in the housing industry in the near term.

Commercial leasing activity remains sluggish. Some contacts said owners were offering early renewal of office and warehouse space, but tenants were hesitant to commit. Investment property sales are “dead in the water,” although there were still reports of increased investor interest. Contacts continue to express concern about the large share of commercial real estate loans up for renewal, but for now lenders appear to be extending the loans. Commercial construction activity is at historically low levels, and many contacts said the stimulus funds were not expected to help much. Most contacts don’t expect conditions to improve until 2011.

Financial Services There were scattered reports of improvement in loan demand over the past six weeks, although contacts remain cautious about the future. Most respondents noted an uptick in residential mortgage demand, largely due to refinancing activity. Some contacts reported an increase in demand for auto loans, saying they were unsure how much of it was a result of the cash-for-clunkers program. Commercial real estate loans were the exception and continue to be mostly nonexistent. Credit quality continues to deteriorate. Mortgage bankruptcies remain high and consumer bankruptcies are rising. Lenders also expect more write-

downs related to commercial real estate. Many contacts said they had seen a significant inflow in deposits over the past month.

Energy Eleventh District drilling activity increased since the last report. Improvement in the rig count has been driven primarily by oil-directed drilling in response to rising oil prices. The pickup in the rig count is not enough to change the weak position of the energy industry, according to contacts. Low demand and rising inventories are putting downward pressure on natural gas prices. Companies are realigning activities and employment in areas where they won't need future capacity, including the Permian Basin, south Texas and the more mature Barnett shale. Drilling has slowed sharply in the Gulf of Mexico, including deep water drilling. There is growing pessimism in the outlook for the natural gas industry.

Agriculture Reports on agricultural conditions were mixed. The severe drought in central and south Texas has wiped out large portions of dryland crops. Contacts say ranchers have liquidated as much of their cattle herds as they can and are now looking for ways to save what they have left. Milk prices remain below production costs leading to financial losses for dairy farmers. In contrast, favorable moisture and growing conditions in northern parts of the state have resulted in excellent crop yields. In particular, cotton yields are above year-ago levels.

TWELFTH DISTRICT–SAN FRANCISCO**Summary**

Economic activity in the Twelfth District showed continued scattered signs of firming but appeared to be little changed on net during the reporting period of late July through the end of August. Upward price pressures remained quite modest overall, and upward wage pressures were largely absent. Retail sales in general stayed anemic, while demand for services continued to erode. District manufacturing activity remained stuck at very low levels, although conditions improved further for manufacturers of information technology products. Demand was solid for agricultural producers but remained weak for providers of natural resource products. Home sales strengthened further in most areas, but demand for commercial real estate continued to weaken. Banking contacts reported that District lending activity eased on net and credit quality continued to deteriorate.

Wages and Prices

Upward price pressures remained quite modest on net during the reporting period. Commodity prices in general were stable, although the prices of oil and selected other commodities such as steel rose. Final prices for assorted retail goods continued to be held down by extensive discounting and promotional activity, and weak demand further reduced the prices of various categories of services. About two-thirds of the contacts reported that they expect prices for the goods and services sold in their respective industries to remain largely unchanged through the remainder of 2009.

Little or no upward pressure on wages was reported. Hiring remained quite restricted, and high levels of unemployment held down wage pressures throughout the District. Contacts noted that, despite an anticipated improvement in economic conditions, they expect hiring to remain subdued for a prolonged period as companies focus on maintaining recent productivity improvements rather than expanding employment; accordingly, they expect upward wage pressures to remain muted for some time.

Retail Trade and Services

Retail sales overall remained very sluggish, although there was a substantial pickup in the sale of new autos resulting from the cash-for-clunkers program. Consumers continued to restrain

their spending on large discretionary purchases and luxuries, resulting in weak demand at department stores and specialty retail outlets. Conversely, retailers who focus more on necessities, such as discount chains and grocers, saw further sales gains. In response to the implementation of the cash-for-clunkers program, sales of new automobiles rose substantially compared with the prior survey period; however, contacts cautioned that sales are likely to return to their earlier low levels at the conclusion of the program. Demand for used automobiles stayed strong, although the limited supply of suitable inventory continued to restrict sales.

Demand for services eased further since the last reporting period. Contacts in the restaurant and food services industry noted weak demand and further declines in revenues. Providers of health-care services reported a small drop in patient volumes, reversing the slight uptick in the prior period. Demand weakened further for providers of professional services such as business consulting and also for transportation services, although the pace of decline has reportedly moderated. Travel activity in the District was mixed: it fell further at major destination markets in California and Nevada, but contacts in Hawaii reported a slight increase in visitor arrivals and hotel occupancy rates from prior low levels.

Manufacturing

District manufacturing activity generally remained weak during the reporting period of late July through the end of August. Demand weakened further for metal fabricators, causing capacity utilization to fall from existing low levels and resulting in additional layoffs. Activity at petroleum refineries continued to decline as a result of producers' efforts to reduce excess inventories. Makers of commercial aircraft and parts saw further significant declines in new and existing orders, and they reduced production activity accordingly. By contrast, conditions continued to improve for manufacturers of semiconductors and other information technology products, as reflected in rising orders and capacity utilization. Food manufacturers saw further sales gains.

Agriculture and Resource-related Industries

Demand for agricultural products stayed solid, while demand remained somewhat weak for extractors of natural resources used for energy production. Sales for most types of agricultural products

continued to expand, and input costs, in particular transportation costs, stayed largely stable. Weak demand caused inventories to rise further for oil extractors, reaching levels close to earlier highs from a decade ago. Similarly, weak demand for natural gas continued to constrain extraction activity and put downward pressure on prices.

Real Estate and Construction

Housing market activity in the District remained weak but showed continued signs of improvement, while demand for commercial real estate eroded further. The pace of home sales in many areas of the District, though still at relatively low levels, continued to edge up, spurred by price declines and low mortgage rates. However, contacts in some areas, including lower-cost areas such as Idaho and Utah, noted that steep rates on nonconforming “jumbo” loans and a scarcity of lenders willing to offer them have restricted sales of higher-priced homes. Moreover, new home construction remained at very low levels throughout the District. Conditions continued to deteriorate in the commercial real estate market, with vacancy rates for office and industrial space increasing in many parts of the District and rent concessions rising in frequency. Contacts reported that limited availability of financing continued to sharply curtail construction activity and investment transactions for commercial properties.

Financial Institutions

District banking contacts reported that loan demand softened further during the reporting period. Consumer loan demand stayed weak on net, and commercial and industrial loan volumes fell further as business owners remained very cautious about their capital spending. Lending standards remained relatively restrictive for consumer and business lending, and credit quality deteriorated further as corporate and household borrowers’ balance sheets continued to weaken. Venture capital financing was one bright spot, with contacts noting increased investment amounts and declines in covenant violations for existing arrangements.