

SUMMARY OF COMMENTARY ON CURRENT ECONOMIC CONDITIONS
BY FEDERAL RESERVE DISTRICTS

SEPTEMBER 1986

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SUMMARY*

All districts continue to report sluggish economic growth. Retail sales continued to improve over the summer with most districts reporting strong consumer demand. Prices are stable and largely unaffected by the lower value of the dollar. Manufacturing, however, generally remains weak. Homebuilding continues strong, but high vacancy rates and the provisions of the new tax legislation have caused nonresidential construction to lag. Both commercial and consumer lending have slowed, while mortgage lending remains strong. Crop yields will set new records in many Midwestern states, but will strain grain storage capacity. Recent rains have improved prospects for some crops in the drought-affected Southeast, but have arrived too late to help the corn crop.

Consumer Spending

Most districts report strong retail sales. This general strength represents an improvement over the last Beige Book. Boston and New York indicated sales above retailers' expectations. New York reported that merchants feel that the lower value of the dollar is responsible for increased sales to foreign visitors. Dallas indicated that, although sales remain depressed, retailers anticipate improvements later in the year. Inventories were reported to be at desirable levels. All districts reporting on prices signaled continued price stability and little or no evidence of increasing import prices due to the lower value of the dollar.

*Prepared at the Federal Reserve Bank of St. Louis

Most districts reported sluggish domestic auto sales.

Philadelphia and Chicago, however, reported strong sales. Sales of imported cars were strong in all reporting districts despite recent price increases.

Employment

Cleveland and Minneapolis reported declines in unemployment rates, while weakening labor markets were noted by Atlanta and St. Louis. The steel industry showed little improvement, with the month-long shutdown of USX lingering and a layoff of 2,000 workers in the Midwest.

Chicago indicated that work stoppages this year have held back production more than in recent years. Both New York and Chicago reported shortages of skilled labor for the homebuilding industry.

Manufacturing

Although Philadelphia and Richmond noted that shipments and new orders were up in August, widespread reports of flat or slightly decreased industrial activity suggest little improvement in the performance of the manufacturing sector in most parts of the country.

San Francisco indicated that the dollar's depreciation has had little impact on most manufacturers, while Atlanta reported that it has helped the pulp and paper industry by allowing higher prices for some of their products. Boston reported downward pressure on the prices of manufactured goods due to competition from both importers and domestic producers. Philadelphia and Atlanta indicated manufacturers in their districts expect improvement in the next six months; those in the Fourth District anticipate little change. Chicago reported that demand for steel for appliances and construction has increased this year, but is down for autos and the oil and gas industries.

Energy

Kansas City, Dallas and San Francisco reported lower levels of oil rig activity. All three districts, however, indicated that the recent increases in the price of oil may signal a bottom to the decline of oil drilling activity. Minneapolis also indicated lower production of oil, gas and coal in North Dakota and Montana.

Construction and Real Estate

Most districts continue to report healthy homebuilding activity. Contacts in Cleveland expect a robust residential housing market for the remainder of 1986 and into 1987. The Southern Florida and Atlanta markets are softening, and contacts in Kansas City anticipate housing starts to flatten or decline for the rest of the year.

Nonresidential construction is slowing in most areas. High vacancy rates reported by New York and Atlanta and concern over tax reform have affected commercial construction. Atlanta noted, however, that the national concern over the effects of tax reform on commercial real estate is not shared by local developers who feel that regional economic conditions will far outweigh any negative effects of tax reform.

Financial Sector

Total loans appear to be expanding at a slower rate than previously reported. The growth of commercial and industrial lending has slowed in most districts. San Francisco attributed this slackening to reduced loan demand for tax shelter and commercial real estate projects as a result of expected tax law changes. Philadelphia and St. Louis, however, reported strong commercial loan activity. Small- and mid-sized banks in the Second District indicated increased competition for commercial loans stemming primarily from the large regional banks and

smaller bank holding companies. Most districts noted that the rate of consumer loan growth is slowing. Philadelphia reported that the growth of credit card lending in particular has slackened and Third District bankers expect a further slowing in consumer lending. Cleveland, on the other hand, noted strength in consumer installment lending, expanding at an annual rate of 15 percent thus far in the third quarter. Residential mortgage demand remains strong in most regions with Atlanta attributing their real estate loan growth to heavy refinancing activity.

Agriculture

Very favorable growing conditions will result in record-breaking yields of corn and soybeans in Midwestern states. The expected large harvests and low prices have caused a shortage of grain storage capacity. Livestock producers in most regions are benefitting from low feed costs and higher livestock prices. Recent rainfall in the Southeast has improved prospects for the area's soybeans, cotton and pastures, but has come too late to help the corn crop. Reports from San Francisco suggest the lower value of the dollar has reduced imports of foreign seafood and has aided the increase in exports of forest products to Far Eastern markets.

FIRST DISTRICT - BOSTON

The pace of economic activity in the First District remains sluggish. Retail sales are up from a year ago; but, while results are considered satisfactory, the buoyancy of earlier reports is lacking. Reports of domestic auto sales are mixed. Some dealers continue to enjoy excellent volumes; others have seen a slowing in sales. The manufacturing sector continues to experience disappointing order rates. There are no signs of a pickup. Price competition remains very fierce. Attention to cost containment seems to have intensified.

Retail

Sales results of First District retailers were fair to good over the summer, with a strong back-to-school pick-up in late August. Most contacts are close to plan for the year to date. Prices are quite stable, even for imported goods, with the exception of furniture. Inventories are not regarded as a problem by the retailers contacted. Merchants remain optimistic about the second half of the year.

Most respondents reported sales growth this summer, but at slower rates than a year ago. For these stores, the verdict on the summer season is "satisfactory." Back-to-school items have sold quite well, at least partly because poor weather has brought customers into the stores and increased interest in clothing for "transitional" weather. In addition to school clothes, sales have been strong for summer seasonal items, microwave ovens, and electronics (TVs, VCRs, stereos, radios, and computers).

Several contacts commented that consumer sensitivity to promotional activity has increased, and one voiced concern that too many merchants are chasing too few consumer dollars. At least partly because of such competitive pressures, merchants are holding prices relatively steady, in some cases reducing margins. One noteworthy exception is a furniture retailer; this store successfully passed substantial import price increases on to its customers with only a brief slackening of demand. The other merchants contacted have not seen significant increases in the prices of imported goods since the dollar began to decline.

First District merchants expect a strong second half because of tax reform and the robust New England economy. Firms targeting moderate income customers are pleased with the tax relief for their customer group, while stores with more upscale customers expect an end to consumer uncertainty to encourage spending.

Auto Sales

Reports on automobile sales at New England dealerships are mixed. Sales of imports are generally strong. Some dealers also report excellent sales volumes for domestic models, but others have seen a recent softening in the market. Low-interest financing and the appeal of popular new models are cited as the factors behind strong sales, while slow sales are blamed on the vacation season. Dealers not doing well anticipate a rebound after the summer season is over. Truck and used car sales remain strong.

Manufacturing

The performance of the manufacturing sector remains lackluster. Orders are flat to down. The defense business remains very good, although

it is no longer increasing. Commercial aircraft activity is picking up. Sales of telecommunications equipment are up from a year ago, although not as much as earlier. Furniture sales may also be a little stronger than a year ago. However, sales to most industrial markets are down, in some cases very substantially. There has also been a pronounced weakening in the nonresidential building market.

A number of contacts are reducing headcounts. While attrition will take care of the excess in most cases, some layoffs may be necessary. For the most part, contacts are also taking a very cautious approach to capital spending. Several noted that it is very difficult to get projects approved; one respondent in the textile industry said that a payback period of less than two years is required.

Price competition is fierce, regardless of industry, and raising prices is seen as very risky. In some cases, the downward pressure on prices comes from domestic producers, in other cases from imports. A couple of contacts expressed concern about competition from Japanese-owned firms in the United States.

Faced with sluggish demand and strong price competition, the manufacturing respondents are emphasizing cost containment. Many also have recently been involved with acquisitions, divestitures and other changes in ownership and financial structure.

SECOND DISTRICT--NEW YORK

In general, the Second District economy registered a modest improvement since the last report. Most retailers had sales gains that were at or above plan. Residential construction remained strong, and business activity showed some pickup. Demand for office space was slack (as usually is the case this time of year), and few new projects were announced. Over the past year, small District banks have experienced increased competition from larger banking organizations in the market for business loans.

Consumer Spending

Consumer spending was stronger than had been expected at several District stores during July, and most retailers reported satisfactory gains in sales. As a result, inventories are currently at or below planned levels throughout the region. Higher priced stores registered sales growth of 11-19 percent, well above plan in some cases, while sales at medium-priced retailers grew between 6 and 12 percent. Discount stores were the only major group with lower-than-expected gains of just 3-4 percent.

While July is traditionally a month in which retailers clear out summer stock, sales of apparel were particularly strong during the recent period. In addition, a pickup in demand for consumer durables was also noted, with one store reporting "exceptional" sales of furniture and rugs. Continuing interest on the part of foreign visitors was cited as an important factor in the improved consumer spending, particularly in New York City. Industry sources attribute this increased foreign buying to the decline in the value of the dollar.

Business Activity

Economic conditions in the Second District were somewhat better in recent weeks. The percentage of Rochester purchasing managers reporting an improved business situation increased during July. Groundbreaking ceremonies were recently held at New Jersey's first trash-to-energy power plant. Electricity produced there will be purchased by a major utility in the area. A large pharmaceutical firm in New Jersey has also undertaken a multimillion dollar expansion of its research and development laboratory which should result in additional employment by 1987. Other recently announced plans include the construction of a frozen food factory in central New York, which a British food manufacturer will begin this fall, and the building of an aircraft parts facility on Long Island.

In upstate New York some 2000 of an expected 10,000 soldiers have already arrived at Fort Drum where a new Army division is being assembled. The Pentagon plans to spend some \$1 billion on construction in the area, and the addition of these soldiers and their families is expected to provide a significant stimulus to the regional economy. This should offset to some extent the impact of GM's recently announced plans to lay off or transfer 1200 of its foundry workers in that area over the next two years.

Construction and Real Estate

Homebuilders remain busy throughout the Second District, but conditions are somewhat less hectic than in the spring and early summer when buyer activity peaked. A major problem continues to be getting homes completed on time, since certain types of skilled labor are still in short supply. In some areas, particularly where the stock of suitable land is almost depleted, a substantial increase in home prices has also been noted. In Manhattan, however, where a large amount of apartment

building is underway (that was started prior to the November 1985 cutoff date for city tax abatement), some observers question the viability of the high prices and rentals that will be asked for the new units.

The Second District commercial real estate market has shown little change in recent weeks, and conditions remain somewhat mixed. Only a few major new projects have been announced as most areas adjust to the ample supply of office space currently available. Leasing activity has been seasonally slow in many areas, and the prolonged sluggishness in northern New Jersey persists. Some pickup has been noted in Manhattan, however, where a major brokerage firm recently announced that it will occupy the last of the World Trade Center buildings in its entirety. Throughout the District observers anticipate that the new tax reform bill will curtail the pace of speculative office building.

Financial Developments

Small and mid-sized banks in the Second District report that competition in the business loan market from larger banking organizations has increased over the past year. Most of the increase has been from large regional banks and smaller bank holding companies, rather than from money center banks. The responses from those surveyed suggest that only those banks large enough to service mid-sized companies have been affected. Moreover, the intensity of the competition seemed to increase directly with the size of the bank surveyed. While most banks indicated that all types of business loans were equally affected, a few felt that the commercial mortgage sector had received special attention. The competition has taken the form of increased advertising and direct solicitation of borrowers. Among the steps which the small banks have taken to preserve their share of the commercial lending market are faster handling and approval of loans, greater customer contact, and increased efforts to match, though not undercut, competitors' rates.

THIRD DISTRICT - PHILADELPHIA

Business conditions are improving somewhat in the Third District although there are some signs that the consumer sector may be backing off slightly. Industrial activity rose marginally from July to August. Retail sales are mixed, with back-to-school merchandise selling well, but the late summer lull holding down sales of other goods. Automobile sales are strong. Total loan volume at major Third District banks is growing at about the same healthy rate as it has during most of the year. However, bankers note a decelerating trend in the growth of consumer lending. Commercial and industrial lending, including construction financing, is described by bankers as showing good growth.

The outlook in the Third District business community is for steady or slightly improved conditions in the near term. On balance, manufacturers foresee some pickup in activity over the next six months. Retailers say the fourth quarter and year as a whole should show moderate gains from last year. Bankers expect continued strength in business lending in the region as long as the national economy does not weaken. However, they expect the growth of consumer lending to taper off further.

MANUFACTURING

The pace of industrial activity in the Third District has risen marginally in the last month. Twenty-three percent of the local manufacturers participating in the August Business Outlook Survey said they stepped up operations from July, while only 16 percent indicated slower business and 61 percent reported no change. Business conditions improved for makers of nondurable goods, but are essentially stable for durable goods producers.

Specific indicators of manufacturing activity varied in August, either reflecting growth or showing no change. New orders and shipments were up, but the

level of unfilled orders was only steady. Employment was stable, with both payrolls and working hours virtually constant. Overall, prices of industrial goods in the region were flat during the month.

Looking ahead, Third District manufacturers are generally optimistic. Forty-nine percent of those contacted for the August survey expect business to pick up over the next six months, and only 23 percent anticipate a slower period ahead. Overall, survey respondents predict gains in new orders and shipments, and a slight increase in order backlogs. However, they expect employment to remain at current levels for the next six months, and plan to maintain capital spending at a steady rate.

RETAIL

Sales of children's clothes and other back-to-school items were brisk in August, and as the month came to a close, other goods were selling at about last year's rate. This represents a pause in the expansion of retail sales the region has been experiencing, but store officials say a slowdown at this time of the year is not of serious concern. They note that inventories are still at acceptable levels.

Third District merchants say there have been no developments that would cause them to alter the sales forecasts they made earlier in the year. These call for increases ranging up to 10 percent for the fourth quarter, and a similar increase for 1986 as a whole.

Automobile sales are strong, and dealers say the import share of the market appears to be stabilizing. However, dealers say people shopping for cars are concerned about potential changes in the income tax treatment of sales taxes and interest, and may move some purchases planned for 1987 forward to the end of this year. Such borrowing from next year could keep a lid on sales in early 1987.

FINANCE

Total loan volume outstanding reported by major Third District banks in early August was approximately 17 percent above the level of August 1985. Bank lending officers contacted in late August say that demand for commercial and industrial loans remains strong. Real estate and construction lending is also brisk in the commercial sector. Bankers attribute this strength to generally good economic conditions in the region; but recent indications of a less robust national economy have prompted some concern for the sustainability of healthy business conditions locally.

Consumer lending is still growing, but the rate of increase has diminished. The growth of credit card lending in particular has fallen off from its pace earlier in the year. Demand for residential mortgages has also fallen from its peak this spring. Third District bankers note a trend toward slower growth in consumer lending of all types, and they expect this to continue along with a slackening in consumer spending in the months ahead.

Total deposits at large Third District banks in early August were approximately 12 percent above the August 1985 level. Transactions deposits show the most growth currently, as they have throughout the year, and savings deposits show the least. The growth in market-rate deposits has slowed considerably, as interest rates have fallen.

FOURTH DISTRICT - CLEVELAND

Summary.

The economy of the Fourth District is continuing its uneven but overall slow growth. Retail sales growth continues to be strong. Employment in manufacturing continues to fall while employment in the services-producing sectors continues its solid growth. The manufacturing sector is stagnant and the two largest steel firms are experiencing major shutdowns. The housing boom is moderating, and overall loan demand at banks has weakened.

Retail Sales

Fourth district retailers generally report strong sales increases, in the range of 5.5% to 10%, for July and August. One major retailer reports particularly strong sales growth for the Cleveland area for August. The major retailers report that sales increased steadily throughout their second fiscal quarter and that the increases have been fairly even among merchandise categories. Inventory levels appear to be well under control as a result of strong sales. None of the retailers contacted report much price impact from dollar depreciation on foreign exchange markets, but one economist at a major chain expects higher imported prices for consumer durable goods will be noticeable in the fall as retailers pass on higher costs to consumers.

Most of the domestic-auto dealers contacted report generally flat sales of new cars. New car inventories remain at slightly higher-than-normal levels, but all of the dealers contacted report the desire to keep a tighter control on inventory levels. All of the dealers reiterate their belief that

cut-rate financing incentive programs have lost appeal, but the latest GMC sales incentive program caused a spurt in interest and sales of GMC cars the day following its public announcement. On the import side of the market, local dealers indicate that sales started to soften in August, following strong first-half performances. A few import dealers state that a cumulative 10%-11% price increase on 1986 model-year cars may be having some adverse affect on their sales.

Labor Market Conditions.

The unemployment rate for Ohio fell in July to 8.0% (s.a.), 1.3 percentage points below its level of July 1985. Total employment has increased 3.1% in the last 12 months, as employment in manufacturing has fallen 1.9% and employment in service-producing industries has risen 4.8%.

Manufacturing.

Manufacturing activity in this District is stagnant. Both production and new orders are down slightly. Order backlogs continue to decline, and more firms are reducing than are increasing employment. Firms are reducing their inventories of raw materials, components, and finished goods. Manufacturers report the prices they pay for commodities is, on balance, unchanged but transaction prices for their finished goods are up from a month ago. Manufacturers expect their sales to be better in the third quarter than in the second quarter but expect the second half of 1986 to be no better than the first half.

Cleveland-based LTV Steel Company, whose parent LTV Corporation filed Chapter 11 bankruptcy in July, recently announced layoffs of more than 2,000 workers as the firm closed bar and pipe facilities in Ohio, Indiana and

Illinois. The firm cited a continuing weakness of orders, despite a work stoppage at USX.

A strike against LTV over the issue of continuing certain benefits to retirees while the firm is in bankruptcy ended when the payments were resumed.

Steel industry analysts and industry officials predict a long and damaging shutdown as a result of the month-long work stoppage at USX Corporation (the nation's largest steelmaker).

Housing

The housing boom in this District is moderating to a more sustainable pace. Builders and realtors report that the pent-up housing demand that propelled the post Memorial Day housing boom has waned. Housing market participants are confident that housing activity will stay moderately robust throughout the balance of 1986 and into 1987 if mortgage rates continue to drift downward.

The backlog of mortgage applications was reduced by mortgage lenders in August, and mortgage application processing times have returned to the normal 60-day period. The volume of real estate listings is still ample and in August there was a resurgence of sales contracts being negotiated.

Lenders report they expect mortgage rates will drop soon by an additional 1/8% to 1/4%, which would bring the 30-year fixed rate mortgage to approximately 9 3/4%. Recent declines in mortgage rates have had less affect on mortgage demand than did comparable declines in the spring and early summer because of the lack of pent-up demand and because demand for mortgage refinancings has been weak.

Builders in this District report a seasonal slowing of single-family home building during August. Traffic and new orders are down about 10% from July. Builders anticipate that tax reform will reduce apartment construction, which eventually should have a positive effect on single-family construction.

Commercial Banking

Overall loan demand has weakened at District banks. Total loans outstanding at large banks fell over the past six weeks. The contraction in loan volume was primarily in commercial and industrial loans and reflected the recent softness in business loan demand. The demand for mortgage and installment credit, however, continues to be strong. Both real estate and consumer installment loans at large banks have been growing at an annual rate of more than 15 percent thus far in the third quarter.

FIFTH DISTRICT - RICHMOND

Overview

Manufacturing and retail sales remain sluggish, and producers and retailers expect only slow growth over the next six months. Service firms are experiencing gradual expansion and foresee continued improvement in their sales. Import and export activity at seaports is strong and is expected to increase. Business and financial executives expect only minor short-run effects on the economy from tax reform and from the August cut in the discount rate. Bankers are somewhat reluctant to reduce interest rates on deposits and are therefore experiencing a squeeze on their interest margins. State and local government officials and employees are becoming less optimistic about prospects for increased revenue. August rains have provided relief from drought and have improved the outlook for the agricultural harvest.

Retail Sales

Auto dealers, department stores, and other retailers report lower sales in August after generally flat activity earlier in the summer. Although 50 percent of retailers expect sales to increase over the next six months, that percentage has declined from 60 percent last month. On the other hand, only 8 percent now expect declines in sales, compared with 20 percent a month ago.

Manufacturing

Manufacturing remained generally weak in August. Capacity utilization rates averaged 76 percent, the same as in July, although shipments, new

orders, and the length of the workweek were up slightly in both durable and nondurable goods industries. Raw material and finished goods inventories declined marginally for the second consecutive month. Although most manufacturers expect the U.S. economy and their own businesses to improve in the coming months, the proportion of optimists is smaller than a month ago.

Manufacturers report that current prices for their raw materials and finished goods are generally stable. But the proportion of respondents expecting prices to rise over the next six months has increased. Thirty-nine percent of firms surveyed this month, as compared with 23 percent last month, expect increases in the prices of their finished goods; 50 percent this month, compared with 40 percent last month, expect the prices of raw materials to rise.

Services

Services sector growth has slowed. Forty-two percent of this month's respondents, compared with 53 percent of last month's, report an increase in sales. But 71 percent of the respondents expect increases in their sales over the next six months.

District seaport officials report increases in both export and import shipments. Industry spokesmen expect these increases to continue in the months ahead, unless shipping activity is interrupted by an unanticipated work stoppage. Longshoreman contracts expire in October.

Government

Survey respondents in state and local governments are less optimistic about funding than a month ago; 50 percent now foresee an increase in general revenue in the next six months while 19 percent expect a decrease. Last month, 71 percent expected revenue increases and 6 percent expected declines.

Agriculture

A stalled weather front provided some much needed rainfall across the District during mid-August. Soybean yields are expected to benefit, and tobacco and fruit are generally in good condition, but the rain came too late to help the corn crop. Pasture and hay conditions are still poor but have improved enough to lessen early marketings of livestock. The peanut yield is expected to be excellent, but the quality of the peanuts is now threatened by a mold that appeared with the August rains.

Policy

Most respondents expect only a slight stimulus to the economy from the August reduction in the discount rate. Bankers say their margins are squeezed when the discount rate is reduced. Competition, they say, rapidly forces down interest rates on loans but delays or prevents reductions in interest rates on deposits. The squeeze is especially severe when discount rate reductions come in rapid succession.

Respondents are about evenly divided on the short-run effects of tax reform on the economy. Half expect the effects to be expansive, and half believe they will be contractive.

SIXTH DISTRICT - ATLANTA

The pace of southeastern economic activity slackened toward the end of summer for most sectors. Unemployment rates continued to edge upward, consumer loan growth slowed, auto sales have not met expectations, and consumer spending has been mixed. High vacancy rates are slowing office construction, and residential construction has cooled in some areas. More positively, building permits are up and tourism has been strong. Textile employment has stabilized. Rains are helping to ease drought conditions. However, drought-induced damage to timber and crops has been substantial.

Employment and Industry. Labor markets weakened from June to July, according to available statistics. Double-digit unemployment rates continue to plague Alabama, Mississippi, and Louisiana. Florida's unemployment rate rose to 6.5 percent, its highest level in a year.

Manufacturing employment trends have been mixed recently. Roughly 1,000 persons have lost jobs at Florida's Space Center since the Challenger accident. More layoffs are expected by major space center contractors due to delayed shuttle flights. Although District petrochemical companies have been aided by the lower dollar and falling raw material costs, demand is weak for specialty chemicals used in the semiconductor and computer industry. Agricultural chemical production has taken a downturn as a result of slack demand for fertilizer.

Textile industry consolidation and restructuring programs initiated during 1985 are beginning to benefit producers by making firms more competitive, although product prices are still under pressure. Firms are focusing on products in low-labor-content niches such as home furnishings. District textile employment is currently slightly above that of last year.

The drop in the value of the dollar has benefited the pulp and paper industry by allowing higher prices for linerboard and packaging. Exports of paper products continue to rise.

Consumer Spending. Year-over-year retail sales growth varies widely across Sixth District states. Through May, Tennessee and Florida reported double-digit year-to-date sales increases, while sales in Louisiana were down from last year. Bargain-hunting consumers around the District have been shifting purchases from traditional department stores to discount retailers.

Domestic car sales during July and August were disappointingly below the year-earlier sales levels in most areas of the region. Dealers complain that the incentives offered by domestic manufacturers have gradually lost their appeal to consumers and that competition from imports is limiting sales, particularly in the subcompact market. Industry-wide, new vehicle registrations were still ahead of the District's year-earlier levels through June.

Construction. Southeastern single-family building permits (seasonally adjusted, three-month moving average) rose in June for the fourth consecutive month. Nashville's new home sales appear to be outpacing those of the rest of the District. Economic growth attributable to Nashville's General Motors' Saturn plant and the city's new role as a hub of American Airlines have led to a surge in home sales and construction.

The south Florida and Atlanta housing markets, however, are softening. Realtors in south Florida say their area is attracting ever smaller shares of Florida's in-migration. They describe their markets as flat with only moderate increases in sales over year-earlier levels. Similarly, Atlanta realtors note a slowdown. With mortgage rates declining, potential buyers seem inclined to delay loan applications.

The recent intense national concern over effects of tax reform on commercial real estate is discounted by commercial developers in the Sixth District, who believe that local economic conditions will far outweigh any effects of tax reform. Office construction in Nashville, Atlanta, and South Florida is expected to slow because of high vacancy rates. Market softness is causing lenders to enforce increasingly stringent preleasing requirements.

Financial Services. Total loan growth at large District banks edged upward from June to July. For the second consecutive month, real estate lending exhibited strong growth and led all other categories. District bankers report, however, that refinancing continues to be responsible for much of the gain. Following a national trend, the Sixth District experienced slowing growth of new consumer borrowing, resulting in a significant decline in consumer loan growth.

Tourism. Travel to the Southeast remains very strong. Lower gasoline prices are especially boosting auto travel. However, the dollar's decline has not stimulated domestic travel as much as expected. Travel agents report vacationers are shifting their destinations to areas that have not experienced currency realignment such as Canada, Mexico, and the Caribbean. Many are also choosing West Coast and Hawaiian locations. Still, for the Sixth District, the current trend reflects a 10 to 12 percent gain in tourist volume over last year.

Agriculture. Recent rain is helping pastures return to normal in drought-stricken areas and may prevent further crop losses, especially for soybeans and cotton. Even so, existing damage to major crops suggests that revenue of farmers in Alabama, Georgia, and Tennessee will fall far short of production costs.

In addition to severe crop losses from the summer drought, the Southeast is experiencing substantial damage to its timber industry. In Georgia and Alabama total forestry losses may exceed \$30 million.

At mid-year, the Federal Land Bank of Jackson, Mississippi, was one of four in the nation requiring a transfer of funds from the eight other FLB's to maintain solvency. The severe drought in the Southeast will likely increase losses to the Farm Credit System during the remainder of 1986. In response, the FCS has increased reserves for losses and instituted a number of belt-tightening measures, including office mergers and consolidations and reductions in personnel.

SEVENTH DISTRICT--CHICAGO

Summary. The Seventh District's economic performance continues to lag the nation, with no evidence of either a drop-off or an acceleration in the pace of overall activity. Total employment in the five District states has been about flat since early this year, with losses of manufacturing jobs about equaled by increases in other sectors. Consumer spending and residential building continue relatively strong. However, domestic automakers recently pared production plans as inventories of some models became excessive. Commercial construction continues at a high level, but important new projects have been postponed indefinitely. Most lines of mechanical capital goods remain weak. Labor disputes have cut output of steel and construction equipment. Bumper grain crops are exerting downward pressure on prices, and are expected to strain available storage capacity.

Labor Negotiations. Labor-management negotiations in the District in 1986 have been more prolonged and heated than in recent years in steel, construction equipment, meat packing, building trades, and local government. Workers in distressed industries are strongly resisting pay and benefit cuts. Unions are demanding job security guarantees. Managements are pushing for changes in restrictive work rules. Work stoppages have halted production to a greater extent than in recent years. USX, with a major plant in Gary, Indiana, was shut down August 1 after labor rejected a management proposal to cut wages and benefits substantially. The union called the shutdown a lockout after USX rejected a union offer to work under terms of the old contract while bargaining continued. Where courts agree with the union position, workers are eligible for unemployment compensation. Deere, the leading farm equipment producer, closed all its farm equipment plants (mainly in Illinois and Iowa) after three facilities were struck. Farm equipment inventories are described as larger than normal. A strike at a Caterpillar parts plant caused layoffs at other facilities. A strike by Detroit municipal workers was settled in early August, after 19 days.

Steel. The strike at the USX Gary Works has cut steel output in the District sharply, and

shifted orders to other producers. One District steelmaker is operating at 85 percent of capacity, compared with the low 50's for the industry. Cold-rolled sheet orders have been extended 6 to 8 weeks beyond normal leadtimes at this producer. Encouraged by the USX strike, several large steelmakers announced selective price increases. Demand for steel has increased this year for appliances, furniture, construction, and grain storage facilities. Buying of steel by the auto industry is about 5 percent below last year. Steel for oil and gas, and for the railroads, is off sharply.

Capital Equipment. Output of mechanical capital goods is generally weak, even below last year's low level. Farm equipment output was extremely low, even before the Deere strike, with good used equipment in ample supply. Sales of replacement parts, to keep existing agricultural equipment operating, are described as good. A leading producer of industrial robots is cutting employment due to cancellations of orders by automakers. Railroad equipment output continues at a very low level. Oil and gas equipment output has fallen near zero. Two manufacturers of diesel engines, faced with depressed demand, recently announced an agreement to combine those operations. Some types of construction equipment have improved, supported by strong residential and highway work. The latter consists mainly of repair and upgrading of existing routes. Reports indicate that defense equipment orders come in spurts, but apparently are increasing overall.

Motor Vehicles. Sales of cars and trucks are near last year's high levels, supported by cut-rate financing as low as 2.9 percent and rebates from domestic producers, with imports accounting for a larger share of the market. A credit union trade association is asking the FTC to determine whether below-market financing programs of the automakers' captive finance companies constitute unfair competition. Domestic car and truck makers have scaled back production in the current quarter from earlier plans through temporary plant closings and slower line speeds. Light truck sales are still strong, particularly imports. One industry analyst projects sales of medium trucks in 1986 slightly ahead of last year, but expects sales of heavies to be down 12 percent. Sales of both mediums and heavies in 1987 are expected to be near 1986 levels. Competition is fierce for heavies, with prices below last year and at unprofitable levels. Further

consolidations and employment cuts by heavy truck makers are expected by analysts. There is an unusually large supply of good used truck tractors and trailers, partly reflecting the sharp increase in failures of trucking firms under deregulation.

Nonresidential Construction. Commercial construction activity in major District centers remains at a high level. But a large amount of prime office space in the Chicago area, downtown and in suburban centers, is vacant with more coming on the market. Some major projects have been delayed awaiting anchor tenants. Furthermore, proposed tax treatment of "passive income" is said to be discouraging equity investors. Demand for suburban office space is up from last year. There has been some pickup in the Chicago area in construction of strip shopping centers, small industrial warehouses, and a variety of smaller business projects.

Residential Construction. Housing construction and resales continue at good levels in many parts of the District. Residential building permits for 7 months are 27 percent above last year in the District states, versus a rise of 7 percent for the U.S., with particularly large gains in the Chicago, Indianapolis, and Milwaukee areas, and in parts of Michigan. Average prices of homes in the Chicago area rose 12 percent in the first 6 months of this year, according to a realtor's analysis, with increases of 15-20 percent reported in favored suburbs. Similar increases are been reported for portions of the Detroit area. Rates on 30-year fixed-rate mortgages have fallen to about 10 percent, according to a survey of Chicago-area lenders, down from 10.6 percent in mid-June. Despite improvement, residential building in the District as a whole is still well short of the pace of the late 1970s. Shortages of skilled tradesmen--including bricklayers, carpenters, and drywall installers--are reported in the Chicago and Detroit areas. One District lender describes several steps taken earlier this year to restrain loan applications (including refinancings) which had overwhelmed processing capacity. These included higher application fees, elimination of rate lock-ins, and higher mortgage rates. A newspaper survey points to a 5-10 percent rise in apartment rents this fall.

Consumer Spending. Most large general merchandise chains reported seasonally-adjusted dollar sales records in July. Strongest lines have been appliances and home furnishings. Hot

weather in July boosted sales of air conditioners and apparel. Credit sales continue to account for a near-record share of total sales at one large chain. Delinquencies have declined since spring, but remain relatively high. With inventories described as moderate, the improved pace of sales is expected to stimulate orders to suppliers soon. Airline traffic is very strong, helped by discount fares.

Agriculture. District crop prospects remain excellent. Record per acre corn yields are forecast in each of the five District states. Three of the states are likely to reach new highs in soybean yields. Abundant harvest prospects and record stocks from previous harvests threaten a storage crunch this fall. This has triggered a flurry of activity for bin manufacturers. The prospective shortage of storage space has pushed grain prices down further as farmers, leery of even lower prices when the large crop is harvested, sell existing stocks to make room for the new crop. A change in government regulations permitting increased use of temporary storage facilities will ease, but not eliminate, the distortions that arise from a storage crunch.

EIGHTH DISTRICT - ST. LOUIS

Summary

Economic conditions in the District remained sluggish in the most recent period with growth of employment, construction and retail sales trailing national growth. Bank lending expanded moderately. Agricultural conditions vary widely due to dryness in the southern regions and nearly ideal conditions in northern parts of the District.

Outlook

A survey of small businesses in the District revealed that most respondents expect business conditions to be unchanged for the remainder of the year, and planned little change in their work force, prices or inventory levels. A survey of corporate purchasing managers in Missouri indicated that new orders were down sharply in the second quarter.

Construction

The value of District residential building contracts awarded in the three months through July declined by 8.5 percent compared with a 1.9 percent national expansion. While down from the pace of earlier this year, single family construction remained above last year's levels; multifamily building, however, declined from a year ago. District nonresidential construction contracts declined by 4.8 percent and were 4.8 percent below the level of the same period last year.

Employment

District nonfarm employment grew at a 0.6 percent rate in the second quarter compared with the national rate of 1.8 percent. Recent

gains continue to be concentrated in the services, financial, and trade sectors; losses have been primarily in manufacturing. An automaker announced that, due to excess inventories, the three-week closing of a St. Louis area assembly plant will be extended by a week. The closing of the plant, originally shut down for model changeover, will affect 5,000 workers. Contrary to regional and national trends, Memphis has experienced employment gains in manufacturing in recent months while service-producing sectors have contracted. The District unemployment rate increased to 7.8 percent in June from 7.5 percent in May.

Consumer Spending

Despite strong April growth, District retail sales decreased at a 6.3 percent rate in the February-April period compared with a 2.3 percent national growth rate. Nevertheless, sales during the three-month period were 2.6 percent above their year-ago levels. Based on reports from automobile dealer associations, year-to-date sales have grown at an 8 to 14 percent rate. Despite substantial price increases, foreign auto sales have grown faster than sales of domestic cars. Inventories of new cars have decreased but remain slightly higher than desired.

Banking

Total loans at large District banks grew at an 11 percent annual rate for the three-month period ending July, compared with a 5.5 percent rate for the same period last year. Commercial lending expanded at a 5.4 percent rate in contrast to a 3.8 percent rate of decline for the same period last year. Month-to-month changes, however, indicate a slowing in the rate of growth of commercial loans. Consumer loans expanded at a

17.6 percent rate for the three months through July versus 25.6 percent for the comparable period in 1985. Real estate lending has picked up in recent months, growing at an 8.6 percent rate, compared with 6.2 percent for the same three-month period last year.

Agriculture

Nearly ideal weather in northern parts of the District have resulted in predictions of record-breaking yields of corn and soybeans. Crops in Missouri, Illinois and Indiana are reported in good to excellent condition and have progressed one to two weeks ahead of schedule.

Southern parts of the District report significant degrees of drought-related stress. Counties in northern Mississippi have requested federal disaster relief for drought-affected soybean crops. Arkansas farmers are estimated to have lost up to \$200 million due to the impact of dry weather on livestock and crops. Yields of major Tennessee crops are estimated to be 25 to 35 percent below last year. While less severe than in Tennessee, Kentucky agricultural officials also report lowered yields of most crops.

NINTH DISTRICT - MINNEAPOLIS

During recent months, economic conditions in the Ninth District held steady. In some areas, employment grew better than seasonal norms. Both consumer spending and tourist activity made some gains. Resource-related industry performance remained mixed. Although crop conditions have generally been excellent, higher yields will probably lead to lower market prices.

Employment

The most recent data indicate that the Ninth District's labor markets continued to improve. Seasonally adjusted employment in the district rose in June, driving the unemployment rate down from 5.9 to 5.6 percent. For the first time in several months, the Minneapolis-St. Paul metro area's unemployment rate fell below its year-earlier level, and even manufacturing employment there rose for the first time in over a year. In South Dakota, employment in the service industry hit a record June high. Among district states, only North Dakota failed to post employment gains during June. And despite growth in June, Montana's second-quarter employment was lower than its 1985 level.

Consumer Spending

Scattered reports suggest that over the summer, retail sales of general merchandise may have strengthened a bit. One retail chain reports a July sales increase of 10 percent, with no inventory accumulation. Another retail chain reports August sales to be a bit stronger than sales earlier this year. Both chains had successful back-to-school promotions, and both noted a pickup in cash sales relative to proprietary credit card sales.

Motor vehicle sales in the district have been good in metro areas but poor in rural areas. One large domestic manufacturer reports that its district sales of cars and trucks are still above last year's levels. Another manufacturer says that its sales in farm communities were flat in July but expects sales to increase after the harvest. Neither manufacturer has high inventories. One Bank director reports slow auto sales in Bismarck, North Dakota, while another reports increased sales during June and July in parts of western Wisconsin.

Homes are still selling well in many parts of the district. Both the unit and dollar values of Twin Cities home sales exceeded their year-earlier levels by over 35 percent in July. However, a logjam of closings has slowed the cash flow to realtors. Building permits in the Twin Cities were 25 percent higher in the second quarter than they were a year earlier. A Bank director from the Upper Peninsula of Michigan reports that new home sales in the Iron Mountain area have been good. In contrast, both building permits and home sales in Montana have been substantially lower than last year's.

Tourism

Tourist spending in the district's hard-pressed nonmetro areas has been good, although not as good as expected this spring. Crossings over the Mackinac Bridge into Michigan's Upper Peninsula reached a record high in June, rising 5 percent above last year's level. Also, travel to that area's Keweenaw Peninsula has been exceptionally good. While statistics aren't available yet, summer tourism looks good so far in northern Wisconsin. Tourist activity is up somewhat in the Dakotas, but not by nearly as much as many had hoped. In Montana, visits to campgrounds have been quite popular, although attendance at the state's national parks has been mixed.

Resource-Related Industries

The performance of the district's resource-related industries continues to be uneven. Wood product industries are still generally a bright spot. Paper and waferboard plants are outperforming lumber mills, though, and loggers are dissatisfied with the slack poplar market. A Bank director thinks that the poplar market may be stimulated by new plywood and waferboard operations in Michigan's Upper Peninsula. Declines in oil, gas, and coal production continue to plague North Dakota and Montana. In Montana, construction has started on a gold mine near Helena, while a copper mine has reopened in Butte.

Agriculture

Crop conditions in the district still look good, but market crop prices have continued to fall. Minnesota's farm price index fell in July, dropping to 3 percent below last July's level. The decline may help stimulate export sales, while government deficiency payments will help insulate many farmers from the falling prices. Some isolated snippets of good news apply to the district's farm sector. Hog and cattle operations have benefitted from lower feed prices, and prices for these animals rose. Dairies in Minnesota and Wisconsin shipped milk to drought-stricken southeastern states, helping firm dairy prices here. And a two-week marketing trip to the Orient resulted in signed contracts for the export of bee pollen products produced on the southern edge of Montana's Flathead Indian Reservation.

TENTH DISTRICT - KANSAS CITY

Overview. Economic activity in the Tenth District remains generally sluggish. While housing activity continues to be stronger than a year earlier, starts are expected to flatten or decline for the rest of the year. Retail sales are up slightly from a year earlier and some further improvement is expected. Auto dealers are not optimistic, however. Both retail inventories and manufacturers' inventories of materials inputs are generally regarded as satisfactory. Large additions to supplies of wheat, corn, and cattle on feed have occurred or are expected. Savings and loan institutions expect a leveling off of both mortgage demand and savings inflows. Loan demand at district commercial banks decreased in the past month while deposits increased.

Retail trade. Retailers report that year-to-date sales are moderately better than levels established a year ago. Sales in coming months are expected to run slightly higher as well. Prices have been stable and are expected to remain stable. Inventories are generally satisfactory. No unusual sales or promotions are anticipated, and inventory purchases should be only slightly below last year's levels.

Automobile sales. Most dealers report that auto sales have been slow during the last month. Financing is readily available, but favorable credit conditions have not stimulated sales. All dealers report that inventory levels are high. Most dealers are not optimistic that sales will improve in the near future.

Purchasing agents. In general, purchasing agents report slightly higher input prices, satisfactory inventory levels, and adequate availability of materials. Most purchasing agents surveyed report that input prices are slightly higher than a year ago but are expected to remain stable for the

remainder of the year. With some trimming behind them, firms are now satisfied with current materials inventory levels.

Housing activity and finance. Area homebuilders report starts of single family dwellings up over a year ago, with starts of multifamily dwellings also up but to a lesser degree. However, most homebuilders expect housing starts to remain flat or fall slightly during the remainder of the year. Sales of new homes are near year ago levels, and new home prices have remained steady. Builders generally report good availability and steady prices of materials.

Savings and loan institutions have been experiencing slightly lower savings inflows compared to those of a year ago. Most expect savings inflows to remain flat in the near future. Demand for mortgage funds has been declining lately after large increases earlier in the year. Expectations are for a leveling off of mortgage demand in the near future. Mortgage interest rates have been falling slightly and are expected to continue to do so over the remainder of the year.

Energy. The district's energy industry remains beset both by the substantial drop in world crude oil prices earlier this year and by recent price volatility. The average weekly number of operating drilling rigs in the District was 188 in July, compared with 550 in January and 200 in June. Despite an agreement by OPEC members to cut output temporarily, domestic exploration and development activity is expected to remain depressed. The OPEC agreement has caused oil prices to firm in recent weeks, however, possibly stalling the decline in drilling and production in district states.

Agriculture. Following a winter wheat harvest that was average to above average throughout the Tenth District, agricultural lenders report that most wheat farmers have been able to service operating loans on schedule. The rate of loan paydown has improved since last year except in northcentral Oklahoma,

where wheat yields were well below average. Some farmers in this area are now refinancing operating debt.

Storage space for the wheat harvest was generally adequate. A severe shortage of storage space is expected to develop with the harvest of the milo and corn crops. Farmers unable to secure sufficient storage space for their crops will be forced to store grain in temporary facilities or to sell grain at very low harvest-time prices.

District agricultural bankers report that the ranching industry remains depressed. Nonetheless, most cow-calf ranchers have been able to maintain solvency. Ranchers with adequate cash flow are expected to hold spring-born calves through the winter to be sold as yearlings next spring. Cattle feeding activity in the district has increased over that of one year ago, and feedlots are expected to be filled to capacity by yearend.

Banking. Loan demand at Tenth District banks fell during the past month, largely due to a decrease in commercial and industrial loans. Agricultural loans were also down slightly. Among the remaining loan categories, residential real estate loans rose while consumer and commercial real estate loans were flat. Most banks lowered their prime rate one-half percentage point and expect further declines. Consumer lending rates fell at one-half of the respondent banks and remained constant at the other half. Further changes in the near term were expected by one-half of the respondents and not expected by the other half. Deposits rose at the respondent banks, largely due to an increase in MMDA's. NOW and passbook savings accounts also rose slightly. Demand deposits, IRA's, large CD's, and small time deposits were flat.

ELEVENTH DISTRICT--DALLAS

The District economy continues to suffer from the weakness in energy and construction, but there is some evidence that the rate of decline in economic activity has slowed. The drilling rig count hit a low in June and has increased slightly since. The value of construction contracts grew during the three months ending in July, but remained well below a year earlier. The manufacturing sector is still sluggish overall, owing to weakness in construction and energy, but there are signs of improvement in some industries. Falling retail and automobile sales reflect the overall deterioration of the District economy. The level of liabilities in the District's large banks is declining. Ranchers in the District are expected to benefit from higher meat and poultry prices, but agricultural credit conditions continue to deteriorate.

Although District manufacturers generally note continued sales declines, reports of reductions are less widespread than earlier in the year. Makers of electrical and electronic machinery and of transportation equipment note some expansions in sales, but they expect little growth for the rest of the year. Orders are up for paper and allied products and for fabricated metal products. Among apparel firms, sales are flat to slightly higher, as import competition abates. Prices for lumber and wood have been deteriorating recently due to large supplies, but District respondents express optimism that strikes and possible tariffs may reduce the strong competition from Canadian producers. Orders for chemical and allied products are mixed, with no pronounced pattern either of increase or decline. Sales by stone, clay, and glass producers are falling from a year

earlier, as a result of continuing weakness in the construction sector. Orders of primary metals and of nonelectrical machinery are dropping due to decreases in demand from energy and construction firms.

The drilling rig count continues to register slight increases after the decline was arrested in June. The number of well permits being issued and the seismic crew count are still falling, although the rate of decline for well permits has slowed. Respondents say that OPEC's current attempt to raise oil prices is not likely to lead to a significant resurgence in drilling.

Auto and retail sales remain depressed. The largest declines are in the weak, energy-dependent portions of the District. Auto dealers do not expect sales improvement this year. They believe that the high sales levels of recent years mean that replacement sales will continue to be weak. Retailers, who generally expect the District economy to begin to recover later in the year, anticipate some growth in their business.

The total value of construction contracts increased in July for the third consecutive month, but it remains well below a year earlier. Gains in nonresidential and nonbuilding construction stimulated the recent upturn. Nonresidential construction has shown some vigor, despite a significant decline in the value of contracts for office buildings and retail space. Recent strength in virtually every other category of nonresidential construction has helped to sustain contract values. The value of residential construction contracts continues to slip, in response to the overall weakness of the District economy and to past overbuilding of multifamily housing. The rate of decline has been very small. Increasing vacancy rates have left the number of permits issued for multifamily

building 40-percent below the first quarter level. Further declines in residential contracts are likely as soon as the weakness in multifamily permits begins to be reflected in construction contract values.

Single-family construction remains fairly steady. Although all types of construction remain below a year earlier, the difference has narrowed to the 20-percent range from 40-percent earlier in the year.

The balance sheets of the District's banks reflect the overall weakness of the District economy. At the large banks, lending activity is declining in all categories, with the exception of real estate. The rate of increase in real estate lending, while positive, has slowed dramatically. The level of total liabilities is slipping. The largest decline has been in large time deposits. In a reflection of the lackluster economic activity in the District, transaction deposits at all District banks have diminished, despite double-digit growth rates in the nation as a whole.

District farmers and ranchers are expected to earn higher incomes in the second half of the year because of increased payments from government programs and higher meat prices. In July, the index of prices received by Texas farmers and ranchers was above a year earlier for the first time in almost two years, largely owing to strength in meat and poultry prices. Nevertheless, agricultural credit conditions continue to deteriorate. Many farmers and ranchers are still in financial trouble as land values continue to decline sharply. Agricultural bankers expect 5 percent of their farm and ranch borrowers to leave agriculture in 1986 because of financial stress, up from 4 percent in 1985.

TWELFTH DISTRICT - SAN FRANCISCO

Summary

The Twelfth District economy continues to present a mixed picture. Consumer spending and residential real estate activity continue to buoy most local economies, while the manufacturing, oil, agriculture, and commercial real estate sectors remain weak. The reduced foreign exchange value of the dollar has yet to produce widespread improvements in trade dependent sectors, although producers of some forest and seafood products have noted positive developments. Weakness in commercial real estate and tax shelter activity is attributed partly to pending changes in the tax code. These economic conditions are reflected in weak commercial and industrial loan demand, but strong demand for residential real estate loans.

Consumer Spending

Overall, moderate growth in consumer spending continues to provide an economic boost to most parts of the Twelfth District. Moreover, a paper products manufacturer reports that box shipments, which depend primarily on retail sales, were up nearly 8 percent in June over their year-earlier level. Despite the overall strength, the volume of retail sales in some economically troubled areas continues to languish.

The overall growth in consumer spending is not reflected in car sales. Compared with last year's pace, car sales are down 60 percent in Kern County (California), where problems in the agriculture and oil industries have combined to weaken the area's economy, and 10 to 15 percent in San

Diego. In Utah, domestic car sales are reported to be sluggish, although foreign cars continue to sell well.

Manufacturing

In most parts of the Twelfth District, manufacturing activity continues to stagnate. The reduced foreign exchange value of the U.S. dollar has yet to affect most manufacturers. Indeed, one respondent reports that in the Pacific Northwest the dollar volume of imports has risen 22 percent during the past year, while the dollar volume of exports has risen only 13 percent. One sign of a possible improvement in the U.S. trade balance is that a Japanese car company reportedly has the highest inventory-to-sales ratio in the car industry. If this is any indication of future activity, auto imports can be expected to decline during the next few months.

Respondents throughout the District report that some firms are delaying investment plans pending passage and study of the new tax law. Exceptions include companies with strong cash positions and those with longstanding investment plans.

Agriculture and Resource Industries

Prices of most agricultural products remain weak, and the reduced value of the dollar has done little to stimulate exports of these products as yet. Almond growers expect to harvest only about half as much product as they did last year due to poor weather during pollination, and almond prices have strengthened as a result.

Fisheries in Oregon and Alaska are reportedly selling a large volume of product at high prices. Moreover, the reduced value of the dollar

appears to have improved some firms' positions. For example, although exports of seafood products from Alaska remain stagnant, domestic producers are benefitting from reduced seafood imports. In Seattle, one food exporter reports increased volume to Pacific rim countries, and renewed Japanese interest in taking on more products.

Timber producers in Alaska report that their exports to Japan and Korea have risen. Moreover, total lumber exports (measured in board-feet) for the first half of the year were 22 percent above the same period a year earlier, despite falling 9 percent in June. Linerboard exports have risen and newsprint imports are down, but paper imports from Europe are holding steady because suppliers have cut prices to maintain their U.S. market share.

Oil related industries continue to suffer from low oil prices. For example, one major oil company's budget for Kern County has been slashed from \$100 million to \$13 million, just sufficient to maintain the company's fields. Moreover, the county's drilling rig count has reached a record low, with only 27.5 percent of rigs operating, although some local respondents report that rig activity appears to have bottomed out.

Construction and Real Estate

Homebuilding activity continues to be strong in most parts of the District. However, in some states, including Alaska and Idaho, weak economies have slowed residential construction activity.

Respondents throughout the District report that some apartment and commercial real estate developers have cancelled projects or put them on hold due to questions regarding tax reform. Moreover, some banks are

reluctant to lend for real estate projects because they are concerned about their future profitability. In the Puget Sound Area, where vacancy rates reportedly are lower than they are in most large cities, tax reform appears to be having a less detrimental effect on office construction than it is in most other areas.

Financial Sector

Business lending volumes are low in many parts of the District. Weakness in agriculture and manufacturing sectors is aggravated by widespread caution that is attributed partly to uncertainty about tax reform legislation. Loan demand for tax shelter and commercial real estate projects has fallen off particularly sharply.

Mortgage lending continues to provide a source of strength in many areas. For example, mortgage lending volume at one Utah bank was about 30 percent higher during the first half of 1986 than it was during the first half of 1985. Continued strength in mortgage lending is also reported in Oregon and California.