

SUMMARY OF COMMENTARY

on

CURRENT ECONOMIC CONDITIONS

BY FEDERAL RESERVE DISTRICT

September 1992

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SUMMARY*

Economic activity has been improving slowly in most of the nation, but the pace of recovery has been uneven across regions and sectors. Cleveland, Dallas, Kansas City, Philadelphia, and Richmond report modestly improved conditions in their Districts since our last report. Some weakening of economic conditions is reported by Chicago, and in California by San Francisco. The remaining Districts generally report a continuation of slowly expanding activity. Retail sales are reported steady or slightly higher by most Districts, but auto sales are lackluster. Manufacturing activity has weakened in autos, aerospace, and defense-related industries. In manufacturing outside of these sectors, however, improvement is noted in orders, production, and sales. Residential construction activity appears to be improving slowly in most of the nation, particularly in low to mid-priced housing, but nonresidential construction remains weak. Agricultural conditions are good in most Districts. The clean-up and reconstruction from Hurricane Andrew is expected to stimulate economic activity in southern Florida and Louisiana. Little upward pressure on prices has been evident, except for products such as lumber and natural gas associated with storm-related damage.

Consumer Spending

Retail activity is mixed across the nation, with some Districts reporting steady or slightly improving sales, and others reporting sluggish conditions. Contacts in the Minneapolis, Philadelphia, and Richmond Districts indicate that sales picked up in recent weeks. Chicago and New York also report that, after accounting for the late Labor Day holiday, underlying sales growth rose in both August and early September. Chicago reports increased demand for appliances and home

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improvement items, while New York reports increased demand for fall clothes due to cool weather. Back-to-school sales in early September are reported strong by Cleveland, New York, and St. Louis. Dallas, however, reports sluggish conditions in most of its major markets, and Boston reports that two-thirds of its retail contacts experienced sales declines in the summer from year-earlier levels. Retailers in the San Francisco District also report weak demand for soft goods in most markets. In particular, retail activity in southern California is said to have declined. Outside of California, however, retail sales are reported to have improved. Inventories are at or below projections in most Districts.

Auto sales are reported as steady to rising by Dallas, Kansas City, Minneapolis, and St. Louis. Generally sluggish conditions, however, were observed by other Districts. Chicago and Cleveland report that major automakers are disappointed by these recent sales trends, and that dealers have cut orders below sales in order to prevent an unwanted buildup of new car inventories. While sales of light trucks outperformed those for cars during August, dealer orders for light trucks also began to lag sales in recent weeks. According to Chicago, one domestic automaker attributes the weak car sales to an erosion in consumer willingness to purchase, rather than to income trends. Showroom traffic has improved, but sales closures have weakened.

Several Districts said this has been a good summer for tourism. Atlanta reports good convention activity and moderate increases in tourism boosted by discounted air fares and an influx of European visitors responding to the weak dollar. Boston-area tourism also has benefited from an increase in foreign visitors, and Minneapolis reports a good summer tourist season at national parks in its District. Tourism in Hawaii, however, was reported down due to a large drop in California visitors, and contacts report that tourist-related retail and service sector jobs are down in Los Angeles.

Manufacturing

Auto production has fallen in recent weeks, and job losses continued to be reported in aerospace and defense-related industries. Outside of these sectors, however, several Districts report general increases in manufacturing activity.

Chicago and Cleveland report that due to disappointing sales and a recent labor dispute, auto production has failed to meet earlier expectations. Auto production in the fourth quarter is expected to remain near the relatively low third-quarter rate, even if the production losses due to the recent labor dispute are fully made up. Inventories remain lean, however, and production would respond quickly to any sales pickup. Cleveland reports that steel producers anticipate little change in production over the next few months, as the pace of new orders for October and November is slower than expected.

San Francisco reports that aviation production rates are dropping, and that layoffs among defense and aerospace manufacturers were announced in southern California and Utah. St. Louis reports that consolidation in the aircraft industry has preserved jobs in its District, at the expense of other regions. Boston and Cleveland also report cutbacks in orders and production among suppliers to the aerospace industry.

Outside of these sectors, most Districts report general improvement. According to Cleveland, manufacturing output appears to be picking up due to increased demand for high-tech products and a slowly reviving industrial equipment market. Increased production of non-military electronic equipment is noted by several Districts. Chicago, Cleveland, and San Francisco note increased production of heavy trucks to meet both domestic freight needs and export demand. Several Districts report increased demand for building products due to Hurricane Andrew, and Chicago and Dallas note that industries tied to single-family home construction are experiencing strong sales. Farm equipment demand and production, however, are reported to have fallen by Chicago, Minneapolis,

and San Francisco.

Construction and Real Estate

Several Districts note some improvement in residential real estate and construction activity. Boston reports that real estate sales have been fairly strong over the past few months, with first-time home buyers taking advantage of low interest rates and relatively low prices. Dallas, Kansas City, and Minneapolis report strong increases in housing starts and demand, and note increases in both building material costs and home prices. An increase in home sales and prices is noted in the St. Louis District, although construction activity is mixed. Atlanta, New York, Philadelphia, and Richmond also note increased sales activity. Ample existing home inventories, however, have kept prices stable in these Districts. San Francisco reports that while residential sales and construction activity is increasing in several states, residential markets in California are sluggish, with price decreases reported for higher priced properties. In general, Districts are observing that activity is strongest for homes in the low to mid-price range.

Weakness persists in nonresidential construction activity, according to most Districts. Demand for office space remains weak in Philadelphia, in part due to ongoing consolidation by local companies. Older buildings are said to be especially vulnerable to decreasing demand. New York reports that vacancy rates remain at high levels, so plans to construct four new office towers in Times Square have been put on indefinite hold. Office demand also remains weak in the Dallas District, where a turnaround in office construction is not likely to occur for at least three years. San Francisco reports that nonresidential construction activity in California continues to weaken. In addition, contacts in Oregon report that several major nonresidential projects are on hold until next year. Minneapolis, however, notes that contract awards for public school buildings are more than offsetting declines in commercial and industrial construction.

Financial Institutions

Financial institutions report that loan demand is generally flat, with some increase in mortgage lending, in part due to refinancings, offset by weakness in demand for consumer and commercial credit. Bankers in the St. Louis District describe loan demand as soft. Weak demand for auto loans is noted by New York, which cites competition from automobile financing companies as a reason. Dallas reports that the largest constraint on loan demand is the lack of qualified borrowers. San Francisco reports that low interest rates are improving the profitability of District financial institutions, but demand remains soft for commercial, industrial, and consumer loans in most markets. The weakest loan demand in the San Francisco District was found in California, where delinquency rates for commercial real estate also continue to rise. Several Districts note that currently low interest rates have increased the level of mortgage refinancings. While some Districts observe that the rate of refinancings is below that seen in early 1992, contacts in Atlanta expect that the volume may eclipse the record posted earlier this year.

Agriculture and Resource-Related Industries

Cool and damp weather has affected agricultural conditions across much of the nation. Slower maturing crops are delaying the fall harvest in the Midwest. In the absence of an early, crop-damaging frost, however, Minneapolis and Chicago expect bumper harvests of corn and soybeans in their Districts. Kansas City also expects above average yields of these crops in Kansas and Missouri, but reports crop damage in parts of Oklahoma and Nebraska due to heavy rains and hail. Dallas notes that cotton yields are likely to decline because of the cool weather.

Hurricane Andrew damaged the lime, avocado, mango, and foliage plant crops in Florida, and the sugarcane crop in Louisiana. Except for limes, however, fruit and vegetable prices have remained relatively stable as lost supplies have been replaced by imports. Drought conditions are expected to lower farm income in Idaho and eastern Oregon. The unusually sunny weather, however,

has produced sharp increases in tree fruit crops in Oregon and Washington.

Several Districts report that lumber prices, which decreased in July, have rebounded to high levels as result of Hurricane Andrew. Dallas reports that hurricane damage to platforms and pipelines in the Gulf of Mexico has reduced the supply of natural gas and has boosted natural gas prices. Prices are likely to rise above their normal seasonal increase for the next three to four months as repairs take place. Elsewhere, electricity prices are up in the Pacific Northwest due to drought-related reductions in hydroelectric power. A 20 percent increase in wholesale electricity rates has been proposed in Oregon; this would increase average retail bills by 5 to 10 percent.

FIRST DISTRICT-BOSTON

Economic activity remains sluggish in the First District as both retailers and manufacturers await recovery. Most retailers contacted in mid-September experienced a mid-year lull after sales rose in the first quarter. Auto sales show no improvement, but housing activity has increased. Most manufacturing respondents report that sales and orders are equal to or slightly above 1991 levels, but a significant minority add that incoming business has weakened in recent weeks.

Retail

Two-thirds of First District retail contacts experienced sales declines in the summer from year-earlier levels. They attribute these declines to consumer uncertainty stemming from the regional employment situation and the upcoming election. Of those with sales increases, half believe that the economy is recovering; the other half attribute the sales improvement to discounting activity.

The cost of goods to retailers and prices offered consumers remain unchanged with one exception. Lumber prices are said to have risen significantly in response to heightened demand from areas hit by Hurricane Andrew.

Retailers still exercise tight control over inventories, although some indicated greater willingness to allow stocks to expand as declines in interest rates have lessened carrying costs. One-third of those contacted plan major increases in capital spending, while others report no change. Similarly, only one-third plan to expand employment; others will continue to reduce it by attrition. Retailers do not foresee any near-term change in prevailing conditions.

Representatives of the Boston-area tourism industry report that visitor totals and the foreign share were above last summer's levels. Although hotel occupancy rates are up, room charges have not changed for over two years. Contacts attribute Boston's increased traffic to exceptionally cool weather and the Tall Ships; thus, these gains may have come at the expense of the region's resort areas.

Automobile Sales

Auto dealerships report erratic but generally sluggish sales during the third quarter. Lacking confidence about the economy, consumers are reportedly stressing value: they are holding on to their current cars longer, responding to manufacturers' incentives when they do buy, and opting for used over new cars. The used car market is strong, and sellable used cars are said to be in short supply. Dealers are uncertain about the upcoming months.

Residential Real Estate

Residential real estate sales have been fairly strong over the past few months compared to a year ago. First-time home buyers account for the bulk of activity. Realtors attribute the increased sales volume to lower interest rates along with a perception among potential buyers that housing prices will not decline further. The condominium market continues to be weak. Realtors expect September and October to be busy, following the typical seasonal pattern.

Manufacturing

Most First District manufacturers contacted in the week after Labor Day report that sales and orders are even with or modestly above year-ago levels. However, one-third of the contacts experienced renewed weakness during July and August. Products for housing, health care, telecommunications and, until recently, the auto industry were described

as relatively strong. Office machinery and computer-related services also showed some small improvement, with interest in new products offsetting slow economic growth. By contrast, orders for aircraft-related products are down significantly from year-ago levels, as some aircraft makers and airlines postpone deliveries. Government demand and several foreign markets are also said to be weakening.

Since few manufacturers can count on significant sales growth, they report continuing efforts to cut costs and improve profits. Accordingly, they are keeping inventories tight and capital spending modest. In most cases, capital spending is equal to or below 1991 levels, and two contacts have delayed capital projects. Employment levels are generally flat to down from the beginning of the year, with declines ranging up to 10 percent. Almost half of the firms expect employment to continue to fall.

Input prices are generally stable; despite ongoing efforts, manufacturers are finding it increasingly difficult to wring price concessions from suppliers. The manufacturers' sales prices are flat to down, with low-end products priced aggressively and high-end products more stable. A minority have succeeded in raising selected prices.

While one manufacturer is more upbeat than at any time in the past two years, several describe themselves as more pessimistic than they were in early 1992. Most contacts expect little change from current near-stagnant conditions. They attribute the "anemic" pace of GDP growth to business reluctance to spend ahead of the recovery.

SECOND DISTRICT--NEW YORK

The latest developments in the District remained basically mixed but marginally more positive than in other recent months. Most department store contacts said sales were better than expected in July, and on or better-than plan in August. Office leasing activity continued at a moderate pace and the vacancy rate in midtown Manhattan declined, though the downtown rate edged higher. While still at high levels, District unemployment rates fell in August after increasing in July and reports from purchasing managers in Buffalo showed substantial improvement in both production and new orders. Conditions in the residential construction market remained mixed. Most senior loan officers surveyed at small and mid-sized banks noted no change in their willingness to lend but said that demand continued lackluster.

Consumer Spending

Most stores said sales were better than expected in July and on or better-than plan in August. Year-to-year changes ranged widely--from +2 to +14% in July and from -6 to 13.5% in August. While sales gains were reported to be somewhat smaller in August than in July, this was due, at least in part, to this year's late Labor Day, shifting much of the back-to-school buying into September.

Demand for women's and men's apparel was strong in both July and August and new fall styles and fabrics were said to have sold particularly well. Several contacts stated that the unusually cool summer may have been conducive to trying on and buying for the fall and winter since outerwear items also sold briskly. Respondents were generally satisfied with their inventory levels which, for the most part,

are on plan or slightly below. Contacts are cautiously optimistic about some modest sales improvement in upcoming months.

Residential Construction and Real Estate

Conditions in the residential construction market continued mixed in recent weeks with homebuilders in upstate New York reporting stronger buyer interest than those downstate and in New Jersey. Most builders anticipate some improvement this year relative to last year's dismal performance but nothing approaching a housing boom. An encouraging note for the future is that several projects which had long been stalled for various reasons are now being revived. In Westchester County, for example, the initial foundations have recently been poured at a 153-unit townhouse project which was mothballed some five years ago, while in Somerset County, work has begun on a 125-unit townhouse complex initially proposed 12 years earlier. In Monmouth County, new developers have already obtained some contracts for a 113-unit single-family project at a site reclaimed by the lending bank from the original developer.

Office leasing activity continued at a moderate pace since the last report and the vacancy rate on commercial buildings in midtown Manhattan declined. Downtown, however, the rate on primary buildings edged higher as downsizing at financial institutions continued. With the City's vacancy rates remaining at high levels, plans to construct four new office towers as part of the redevelopment of the Times Square area have recently been put on indefinite hold. Instead, the area is to be revitalized and renovated with major tourist attractions and retail establishments.

Other Business Activity

Although still at high levels, District unemployment rates declined in August after increasing in July. New York's rate fell to 8.5% in August from 9.4% in July and New Jersey's declined to 9.4% from 9.8%.

Despite the August drop in District unemployment rates, nonfarm employment has continued to decline though the pace of decline appears to be slackening somewhat. With regard to the outlook, recent announcements have been for employment changes, up and down, that are rather modest in size. Fedders will be closing two New Jersey plants, affecting about 150 workers and Spaulding Composite will be idling about 300 when it closes its plant in the Buffalo area by yearend. On the other hand, an electronics firm near Syracuse will add about 100 workers as it expands into two new product lines and a Corning Inc. plant that makes converters for removing auto exhaust pollution may be expanding to converters for emissions from diesel engines and factory smokestacks as well. August reports from purchasing managers in Buffalo showed substantial improvement in both production and new orders.

Financial Developments

Most senior loan officers surveyed at small and mid-sized banks in the District indicated that their willingness to lend remained steady relative to two months ago. A majority of respondents reported that while overall loan demand remained soft, demand for residential mortgages increased. Consumer loan demand continued to be weak, attributed in part to a decrease in demand for automobile loans. One reason cited for this decline was the surveyed banks' inability to compete with the lower rates of automobile financing companies.

All respondents reported either maintaining or lowering loan rates. A majority of officers indicated that delinquency rates on mortgages and commercial and industrial loans have not changed during the past two months. Although deposits continue to shift from maturing certificates of deposit into more liquid savings accounts, the trend was not as prevalent among surveyed banks as two months ago.

THIRD DISTRICT - PHILADELPHIA

Economic activity in the Third District appeared to edge up slightly in August and early September, according to reports from area businesses. Manufacturers noted continued gains, on balance, with increases in orders and shipments. Retailers generally indicated that sales picked up in late August and early September from the summer pace although the year-over-year increase was slight. Bankers said loan volume outstanding has been virtually steady in recent weeks, with business lending flat, and gains in residential mortgage lending offset by declines in consumer installment lending. Realtors indicated that home sales continued to exceed last year's rate, but demand for office space remained weak.

Looking ahead, Third District business contacts expect little change from current trends. Manufacturers expect orders and shipments to continue to rise. Retailers forecast a seasonal increase in sales for the fall but only a small year-over-year gain. Bankers generally expect little or no growth in overall lending in the months immediately ahead.

MANUFACTURING

Manufacturing activity in the Third District continued on the rise in late August and early September, according to industrial firms contacted for this report. While a little more than half of the companies indicated their business was steady, just over one-fourth said they had stepped up activity in recent weeks. Activity appeared to be steady or rising in nearly all major industries in the Third District with the exception of transportation equipment where orders and shipments were reported to be falling. Overall, however, area manufacturers indicated that shipments and new orders were moving up although order backlogs were declining. Employment appeared to be steady as most firms were maintaining constant payrolls, and cutbacks at some plants were being offset by increases at others.

Looking ahead, a majority of Third District manufacturers expect business to remain on an upward trend through the coming winter. On balance, they plan to step up shipments and they anticipate an increase in orders that will boost backlogs. Employment increases are planned by approximately one-third of the firms contacted while half intend to maintain current payrolls.

RETAIL

Third District retailers generally indicated that sales picked up in recent weeks for the back-to-school shopping period, although year-over-year gains appeared to be slight; results varied among stores, and reported increases were 5 percent or less, in dollar terms. Merchants continued to cite lackluster economic conditions as a restraining influence on consumer spending.

In general, Third District retail executives expect sales to move up seasonally through the fall, but they anticipate only a modest increase for the period compared to last year. While several merchants said they planned expanded advertising and promotional campaigns for the balance of the year, they do not appear to be boosting sales plans. Most said they will attempt to keep inventories lean.

FINANCE

Total loan volume outstanding at major Third District banks was described as stable by bankers contacted in early September. Most banks gave similar reports indicating that commercial and industrial lending was flat, consumer installment loans were edging down, and residential real estate loan volumes were continuing to rise. Bankers noted increases in mortgage lending for new purchases as well as refinancings and home equity loans. Several bankers said their institutions were actively seeking new business borrowers but finding loan demand weak.

Area bankers anticipate little growth in lending ahead. Some speculate that consolidations and restructurings by business firms are resulting in fundamental reductions in their credit needs and that a significant increase in business borrowing will not occur until a trend of strong economic growth is well

under way. Consumer loan demand will pick up, according to bankers, with a resumption of growth in employment and incomes.

REAL ESTATE

Residential realtors reported that home sales during the summer were slightly above sales in the year-ago period, and the pace seemed to be continuing. However, they noted that there are a large number of homes on the market, keeping prices in check. There are few reports of price appreciation, and realtors indicated that there is a great deal of variation in trends from place to place, with prices firm in some areas and falling in others. In particular, real estate agents said prices are dropping for very expensive homes and for homes in some resort areas. Realtors said that both existing and new homes are selling at a better pace than they did last year, although it was noted that some builders who announced price increases in the past few months have seen traffic fall off at their developments.

Demand for office space remains weak, according to commercial realtors. They estimate that vacancy rates this summer reached about 16 percent in central Philadelphia and varied from 13 to 27 percent in suburban areas. Realtors said ongoing consolidation by local companies is continuing to reduce demand for office space. Older buildings are especially vulnerable to declining demand, according to realtors; they estimate that the vacancy rate in Class B buildings is about 22 percent and that rents are being reduced from 10 to 40 percent depending on the age and condition of the building.

FOURTH DISTRICT - CLEVELAND

Summary. Activity in the Fourth District shows scattered signs of picking up from the summer slowdown. Retailers report strengthening in early September sales, and manufacturers - except for automobile producers - note a recent spurt in their new orders. Third quarter housing starts in Ohio may have edged down from the second quarter, but mortgage interest rates dipped further. Except for home equity loans and mortgage refinancing, bank loans eased in August.

Consumer Spending. Retail sales in the Fourth District apparently showed reduced year-over-year gains in August, but some retailers report larger increases in early September, helped by back-to-school buying. Retailers have apparently cleared summer inventories and are planning to hold stocks of fall and winter merchandise close to estimated sales levels. General merchandise sales during the fall are forecast to rise by about 5% from a year ago, compared with a 4% increase in spring sales, according to a retail source. Retailers anticipate less-than-usual hiring in the months ahead in order to improve productivity.

Auto sources were disappointed by the unexpected drop in new car sales in July and by a further decline in August. They report that dealers have recently cut orders below sales in order to prevent an unwanted buildup of new car inventories.

Manufacturing. Output in the District appears to be picking up, except for automobiles. High-tech producers are benefiting from sizable gains

in orders and shipments, and more recently, total output is being supported by a slowly reviving industrial equipment market and by a spurt in heavy-duty truck business. Orders for heavy-duty trucks in July and August are said to have climbed to their best levels in recent years, although helped by some price-hedging. A producer of industrial equipment components notes a boost in July orders, but revival in recent months has been relatively small. An electronics producer reports double-digit increases for its products in recent months.

Shipments of major household appliances in July and August showed larger year-to-year gains than in preceding months, according to a producer. Nevertheless, not much more additional growth is anticipated during the balance of this year because of a flattening in housing starts since spring.

Near-term growth in manufacturing output may be restrained because of spottiness in auto output. Auto sources forecast that the annual rate of production in the fourth quarter will remain about unchanged from the third-quarter rate, even if the production loss of GMC is fully made up. They are concerned that dealer orders have been running below sales recently.

Steel producers anticipate little change in production over the next few months from the present 80% operating rate. According to one source, September orders are rebounding from the summer slowdown in July and August, but the pace of new orders for October and November is slower than expected.

District suppliers to the aerospace industry note that cutbacks in defense purchases as well as deferment of orders for commercial aircraft are dampening their orders and backlogs.

Manufacturers indicate that inventories continue to be lean. Some are adding slightly, while others are still cutting stocks as a result of

improving operating and inventory techniques. Industry sources anticipate continued intensive use of their existing work force, and do not expect either layoffs or worker recalls in the near term.

Residential Construction. Thrift institutions report some letup in new mortgage loans in August and early September, despite a further reduction in interest rates.

New housing starts in Ohio may be off a little in the third quarter from the second, according to a building official, with wide variations within the state. Building contracts in the high-growth area of Columbus sustained their strong pace through most of the third quarter. In Cleveland, however, a large builder of higher-priced, single-family housing reports a sag in consumer traffic and buying during August and early September, which, if continued, will result in layoffs. Home remodeling contractors, however, are said to be operating at capacity.

Banking. Several major banks in the District report that business loans declined again in August, mostly because the volume of new loans continued to fall short of repayments and write-offs. In their view, businesses have been generating sufficient cash flow in recent quarters to meet working capital needs. Some borrowers, however, assert that banks are unwilling to take risky loans that might damage their capital positions.

Bankers note recent declines in consumer installment credit and slower growth in credit card usage. Home equity loans are the major source of loan expansion, according to several lenders.

Some depositories have made further interest-rate cuts on deposits and mortgage loans in recent weeks.

FIFTH DISTRICT-RICHMOND

Overview

There were some signs of improvement in District business conditions over the past six to eight weeks. Retail sales and traffic were up, as were retail prices and wages. Manufacturing showed moderate improvement. Both retailers and manufacturers remained optimistic about the next six months. Residential real estate sales increased, while prices in that sector were holding steady. At District ports, imports were higher and exports steady over the previous month. Financial institution activity changed little, while tourism declined. Agriculture was generally in good shape, though heavy rains and cool temperatures were slowing crop development in some areas.

Consumer Spending

Our regular mail survey indicated that District retail activity improved in recent weeks. Sales and shopper traffic apparently increased, as did wholesale and retail prices. Retailers reported higher employee wages but steady employment.

Survey respondents were relatively optimistic about their prospects for the next six months. They anticipated increases in sales and in wholesale and retail prices. A large majority, however, expected no change in employment.

Manufacturing

Manufacturers indicated that District factory activity improved somewhat in past weeks. Respondents reported increases in shipments, new orders, exports, and raw materials prices and noted little change in other indicators. Government regulations and red tape, and also excess capacity, continued to be

major problems for many manufacturers.

Manufacturers were fairly optimistic about the next six months. They expected increases in most indicators, including employment, and suggested that finished goods inventories would fall.

Ports

Representatives at District ports--Baltimore, Charleston, and Hampton Roads (Norfolk)--indicated that imports were generally higher in August compared with July, while exports remained about the same. Compared with a year ago, both imports and exports were generally higher. Export activity was expected to increase at the Port of Baltimore but to remain the same at the Ports of Charleston and Hampton Roads during the next six months.

Tourism

Hotels, motels, and resorts throughout the District indicated that tourist activity for August and early September declined from July and from a year ago. Most respondents attributed the decreases to the weather, the economy, and a Labor Day weekend that fell later than normal in the season. Respondents who reported increases attributed them to a pickup in convention bookings. About half of the respondents reported that fall bookings were slightly above last year's while the other half reported little change. Over half expected tourist activity to remain about the same throughout the fall.

Finance

District financial institutions contacted by telephone indicated that credit conditions were little changed over the last six weeks. Respondents stated that commercial loan demand weakened slightly. Consumer loan demand was said to be steady. Banks noted that loan rates fell for commercial, consumer, and mortgage loans. Respondents reported that demand in the

mortgage sector picked up, but that the bulk of the activity involved the refinancing of home mortgages.

Residential Real Estate

Real estate agents contacted by telephone indicated that residential activity improved somewhat in much of the District over the past six weeks, but remained sluggish in some areas. Sales, on net, were up, while home prices were little changed. Many respondents suggested that sales of new homes were stronger than sales of existing homes, though respondents in the Baltimore area indicated otherwise. Several respondents noted that activity was strongest for homes in the middle to low price range. Meanwhile, those in some areas suggested that demand for upscale homes, although still the weakest market, was beginning to increase.

Agriculture

Our contacts reported that District farm conditions were generally favorable in most areas. Fall harvesting activity was underway with normal progress in all areas except parts of South Carolina and West Virginia where heavy rains from Hurricane Andrew had delayed activity. Crops were reported to be in generally good condition, but crop development was termed slower than normal in Maryland and West Virginia because of unseasonably cool temperatures. Also in West Virginia, moisture-related disease reportedly damaged some crops.

SIXTH DISTRICT - ATLANTA

Overview: Contacts in the Sixth District reported that economic activity expanded quite slowly through Labor Day. Merchants recorded steady to slightly higher sales, and factories were generally busier than earlier in the summer. Home sales and construction improved in most of the District, but apartment development and commercial construction was flat. Except for the recent surge in refinancing, business and consumer loan demand at District banks remains stalled. Wages have been relatively stable under conditions of job uncertainty, and attempts to raise product prices have met with little success. A summary of Hurricane Andrew's economic impact on south Florida and Louisiana is presented in the final section.

Consumer Spending: Retailers reported marginal sales increases in August compared with year-ago levels. Back-to-school sales generally met retailers' conservative expectations. Discount stores continue to post the best gains, led by sales of apparel and other nondurable goods. Looking ahead, merchants are not expecting significant gains over last year's lackluster Holiday season. Auto sales have been mixed to only slightly higher, but most dealers are comfortable with the relatively low inventories of 1992 models still on the lots.

Convention traffic in most states is exceeding year-ago levels and is expected to remain strong into next year. Tourism enjoyed moderate increases through late summer, bolstered by the air fare wars and an influx of European visitors responding to sharp declines in the dollar.

Manufacturing: A large majority of manufacturing contacts reported steady to higher orders, production, and shipments. However, only a quarter of these contacts added to employment rolls or lengthened the workweek in August. Inventories of material inputs and finished goods continue to drift downward, mostly by design.

However, firms that rely on NASA or defense contracts reported decreasing orders and are not optimistic about the outlook over the next six months. Petroleum industry suppliers stated that the energy business remains slow.

Construction: Most realtors noted sales gains for starter homes and some have seen increased interest in the trade-up market. Ample existing home inventories have kept prices stable even as the number of transactions has risen. Responding to market conditions, builders are putting up more low-to-mid priced homes and expect slow but steady improvement for the rest of the year. Although there have been some reports of rising occupancy rates and modestly increasing effective rental rates, multifamily construction has yet to respond. On the commercial side, some brokers sense that effective rental rates are beginning to firm. Even so, rental rates remain far below those required for speculative development.

Financial Services: Bankers around the region reported that consumer and business loan demand was generally flat in July and August. However, almost all contacts are seeing a deluge of mortgage refinancing that may eclipse the record volume posted earlier this year. Commercial loan activity was generally weak. Several business contacts noted that increased regulatory burdens and conservative lending practices continue to hamper access to credit. Consumer loans were mixed with some contacts reporting increases in auto loans in July.

Wages and Prices: Materials prices for most manufacturers were steady to slightly higher in August. However, firms have generally been unable to pass these through on final products because of sluggish demand and competitive pressure. Businesses across all sectors have not experienced upward wage pressures.

Hurricane Andrew: Hurricane Andrew devastated parts of southern Florida and sparsely populated south central Louisiana. However, after an initial period of disruption, a surge in economic activity is expected as rebuilding commences. South Florida will likely experience a local building boom. Retail sales will rise significantly in both states, and to a lesser extent, across the region. South Florida bankers are expecting new deposits and increased loan activity as insurance money and aid pours into the region to fund reconstruction.

The extent of damage to oil and gas platforms off the Louisiana coast is still being assessed. According to most recent reports, about 200 installations show storm-related losses. Decisions regarding restoration of the most seriously damaged structures are pending. Natural gas prices, which had already been trending upward, were pushed sharply higher by the interruption in supply.

In Florida, the lime, avocado, mango, and foliage plant crops were all severely damaged or destroyed. It will take several years to establish new production for many of the tree crops. Salt water intrusion into fields may delay planting of the winter vegetable crop. However, except for limes, fruit and vegetable prices have remained relatively stable as lost supplies have been displaced by imports. In Louisiana, 25 percent of the sugarcane crop was destroyed. The fishing and shrimping industries were also disrupted, and oyster harvesting has been suspended pending pollution test results. Although the affected areas may experience a net gain in jobs and income for one to two years, the stimulus from rebuilding activity is ultimately transitory and is not expected to displace the loss in agricultural and personal wealth incurred by large uninsured losses.

SEVENTH DISTRICT--CHICAGO

Summary. The pace of the recovery in the Seventh District slowed in August and early September, with some sectors, notably autos, actually weakening. District manufacturing activity generally continued to move higher, albeit slowly and less evenly than in recent months. Car production did not meet earlier expectations, and several auto parts manufacturers expressed concern about the possibility of a further slowdown in the fourth quarter. Retail sales and housing activity in the region have held up relatively well in the face of sluggish employment data. However, several contacts shared the perception that hiring, capital spending, and consumer durable goods purchases may have entered another "wait-and-see" phase. The prospects for bumper corn and soybean harvests have risen in recent weeks.

Manufacturing. District manufacturing activity edged higher in August, but at a slower pace than earlier in the summer. Purchasing managers' surveys indicated that expansion continued for a slim majority of District manufacturers. The index for the Chicago survey slipped slightly in August on a seasonally adjusted basis, but only after a relatively large increase in July, and the level of the index remained higher than in the nation as a whole. The overall results of the Detroit survey have been generally consistent with those in Chicago, although the Detroit index has been more closely linked to trends in auto production, which weakened in July and August. The Milwaukee survey had been providing the strongest results in the District earlier in 1992, but this survey's overall index also indicated a loss of momentum in recent months, reaching a level consistent with slow growth in production. Separately, an August survey of small manufacturers in Wisconsin indicated little change in expectations for business activity over the next 6 to 12 months, with a majority expecting moderate growth over this period.

Reports from individual manufacturers indicated that several sectors remained soft, although appliance production moved higher and the relatively improved heavy-duty truck market showed few signs of a slowdown. A large manufacturer of construction machinery reported that dealer orders for heavy equipment weakened further in August, although orders for light machinery have held up relatively well. A construction industry analyst reported that retail sales of construction machinery in the District were somewhat better than the national average. Retail sales of farm machinery continued to decline from year-earlier levels, and one District farm equipment manufacturer cut production plans for the third time this year. A large appliance producer reported a record July shipments month, and expected

continued improvement in the overall market in 1993. Positive signals continued to emanate from the heavy-duty truck market. A manufacturer of parts used in heavy-duty trucks reported that the market has been continuing to strengthen, citing pent-up demand, confidence in the future growth of the freight hauling industry, and sales incentives. Net orders slipped in August, but only after a sharp jump in July, and this producer expected continued gains in its own sales and production in 1993. A manufacturer of heavy-duty trucks reported that the improvement in District demand has exceeded the national average. A manufacturer of fluid power equipment used in a variety of heavy industrial machinery stated that the recovery in its markets had accelerated since the spring.

Autos. Major automakers in the District characterized recent sales trends as disappointing, and car production failed to meet earlier expectations. Increases in sales and production of light trucks continued to outperform those for cars during the month of August, but one large automaker stated that dealer orders for light trucks began to lag sales in recent weeks. Another domestic automaker said that erosion in consumer willingness to purchase cars has played a more important role than income trends in restraining car sales recently, and noted that showroom traffic continued to improve while sales closure rates weakened. Auto producers agreed that inventories generally remained lean, and production would respond quickly to any future sales pickup that might occur. An auto industry analyst stated that some, but not all, of the production lost due to a recent labor dispute would be made up in the fourth quarter. This dispute was resolved at modest short-term cost to District activity, but it reflected a deeper long-term problem facing the District economy. One auto parts manufacturer stated that inventory building prior to next year's renegotiation of the national labor contract could boost production in the first half of 1993.

Consumer Spending/Housing. Retail sales and housing activity held up relatively well in recent weeks. One large retailer stated that year-over-year sales comparisons in District markets showed a positive trend in recent months. This contact noted that sales gains were being led by big-ticket items. Inventories at this firm were reported to be again in line with plan, after reaching undesirably high levels earlier in the summer, and the firm has stepped up its purchasing. Another large retailer reported that, after accounting for the late Labor Day holiday, underlying sales growth rose in August and early September. Durable goods sales showed above-average gains, led by appliances and home improvement products. The late Labor Day holiday was often cited as a factor constraining August sales comparisons. However, a large retailer and a bank each noted that a renewed wave of mortgage refinancing also played a role, because upfront fees postponed improvement in borrower cash flow.

Renewed declines in mortgage interest rates have been accompanied by scattered signs of strengthening in housing activity, although the increase does not appear to be as robust as in the first quarter. A realtors association reported that sales activity among its membership had strengthened in recent months, but was uncertain about the importance of lower mortgage interest rates in the improvement. One of the largest realtors in the District reported that transaction volume slipped in August on a seasonally adjusted basis, but only after significant gains in June and July. Recent declines in mortgage interest rates were followed by a modest revival in housing activity in Western Michigan, according to banks and realtors in that area. A large producer of construction materials used in homebuilding reported that production increases prompted the use of second shifts at several plants. This contact noted that shipments gains in the District roughly matched the national pattern in recent months, after relative strength was noted in the District earlier in the year.

Labor Markets. Recent employment reports have been subject to a variety of special factors, but still suggested a slowing recovery in District labor markets. Both establishment survey and household survey data indicate that the recovery in total District employment lost some momentum in recent months, although the underlying trend in household survey data has signalled a more robust rebound than the establishment survey. Employment changes in Illinois and Michigan have been weak relative to those in other District states, largely due to a continuing downturn in the two largest metropolitan areas in the District. Excluding these areas, employment has reached pre-recession levels, although the upward momentum slowed during recent months. Private surveys suggested that hiring plans have weakened since the second quarter, but not significantly, and hiring in the Midwest remained stronger than the national average. Temporary help firms reported rising sales gains, and placements in the District continued to run ahead of the national average, but one firm expressed concern about recent economic trends. This contact also stated that demand in smaller metropolitan areas has significantly exceeded demand in large cities.

Agriculture. The fall harvest will be delayed this year due to slower maturing crops, but the prospects for a bumper harvest continue to improve as concerns for an early frost ease. The latest weather forecasts discount the likelihood of an early, crop-damaging frost. If that is the case, the fall corn and soybean harvest in District states is likely to be the second largest on record and up a sixth from last year.

EIGHTH DISTRICT - ST. LOUIS

Summary

District economic activity continues to increase slowly. Retailers and car dealers report increased sales from one year ago. Manufacturing reports indicate growth, while nonmanufacturing reports are more mixed. Residential construction activity still is up substantially from one year ago in some areas, while it has slowed in others. District loan demand remains weak, with large banks reporting a slight decline in loans outstanding during the past two months. District farmers report favorable harvest prospects, but concern over an early frost is mounting.

Consumer Spending

Retail sales are generally above those of last summer. Back-to-school sales in St. Louis and Louisville are up noticeably from last year, and contacts across the District report generally higher year-to-date sales as well. Price cutting by retailers was reported to be similar to last year's efforts. Inventories are at or below desired levels. Car and light truck sales are up moderately from last summer, and dealers expect to see slight increases through year-end.

Manufacturing

Employment opportunities at District manufacturing firms appear to have improved as reports indicate more hirings than layoffs. For example, a new poultry processor will move into Arkansas, initially employing 150 workers. In addition, a printing company will employ 100 people in its new eastern Mississippi plant. A Memphis steel processor will add up to 150 jobs as it expands its facility. Also in Memphis, a

tire manufacturer has recalled 140 workers because of increased sales, and a chewing gum manufacturer has added 170 jobs in its expansion.

Cutbacks continue to occur in the defense industry. In particular, a St. Louis-based defense contractor announced its consolidation of six divisions into two, eliminating 170 St. Louis jobs immediately. The jobs of 7,000 St. Louis employees of this firm, however, became more secure with an announcement by the President of his support for the firm's aircraft sale to a foreign buyer. Unrelated to defense, a plant manufacturing jeans in northwestern Mississippi will close this month, releasing 550 employees.

Nonmanufacturing

District nonmanufacturing employment reports can be characterized as mixed. An anticipated loss of 400 jobs occurred at a Louisville health care provider and insurer. Potentially offsetting these losses, however, are a travel agency's expansion of 100 jobs because of a new contract and a supermarket chain's addition of 200 employees this month because of a new store. Southern Illinois will gain 250 jobs when a new federal prison opens, and St. Louis will likely gain some jobs when it becomes one of the U.S. Postal Service's new regional headquarters under a reorganization plan.

A recent survey of Eighth District firms reveals that almost half of those surveyed experienced no change in sales during the second quarter and do not expect to change their inventory levels during the third quarter. In an unrelated survey by a temporary employment agency, half of the Memphis firms surveyed indicate that they will increase employment in the fourth quarter of 1992, a proportion more than double the national average.

Construction and Real Estate

District residential construction activity is mixed. Single-family home permits in July were substantially above their year-ago levels in St. Louis and Little Rock, but were down in Memphis and flat in Louisville. New and existing home sales, meanwhile, remain above their year-ago levels throughout the District. Contacts note that the average selling price of new and existing homes has risen in recent months. One Memphis realtor interprets recent sales trends as evidence that consumer confidence has improved, noting that purchases have been spread evenly between first-time homebuyers and the move-up market.

Banking

Total loans outstanding at 12 large District banks declined slightly in July and August after remaining flat in May and June. Business and real estate loans declined over the period after increases in the prior period. Consumer loans, which had declined 0.8 percent in May and June, increased 2.2 percent in July and August. Bankers continue to describe loan demand as soft.

Agriculture and Natural Resources

While crop prospects are mostly favorable throughout the District, cloudy and cool weather in August has hampered maturity in many areas. As a result, farmers are increasingly concerned about the effects of an early frost, particularly for corn in Illinois, Indiana and Kentucky. Although Hurricane Andrew caused minor damage to the corn, cotton and soybean crops in some Mississippi counties, it brought beneficial moisture to many areas of Arkansas and Tennessee. Southern pine lumber producers report that production and exports remain well above last year's vigorous pace. They also report that inventory rebuilding is occurring in anticipation of a relatively strong fourth quarter, partly in response to rebuilding in the aftermath of Andrew.

NINTH DISTRICT--MINNEAPOLIS

Late summer economic conditions in the Ninth District were steady after slight declines reported in the previous *Beige Book*. General merchandise, auto and home sales show signs of strength. Tourism was reported to be strong. Construction is running above last year's levels. These positive factors are offset to some extent by weak labor markets, with layoffs in manufacturing and mining reported in late August and early September. Finally, cold, wet weather threatens District crop production.

Consumer Spending

General merchandise spending in the District is showing some signs of strength. The opening of the Mall of America in a Minneapolis suburb was a retailing milestone. One of the largest malls in the United States, the facility attracted more than 1 million shoppers in its first week.

Further signs of strength include a regional electronics retailer reporting August year-to-date sales 15 percent above the same period in 1991. Sporting goods stores in the Upper Peninsula of Michigan towns of Ishpeming and Marquette report late summer sales 10 to 20 percent above last year. Minnesota sales tax remittances for August are reported to be "as projected," somewhat above levels a year earlier.

Automobile sales are strong, with new car titles issued in Minnesota in August up 13 percent over 1991. A manufacturer reported that year-to-date car sales were even with 1991 but that truck and pickup sales were up substantially.

In spite of unusually cool weather, the summer tourist season was reported to be good. Montana experienced a very strong season with visits at 14 top attractions, including Yellowstone and Glacier national parks, running 7 percent above 1991's rates. In South Dakota, tourism was reported to be down slightly from the previous year, but still rated as "great" by an official of an industry association. Crossings of the Mackinac and Sault Ste. Marie bridges ran above 1991 levels.

Home Sales and Construction

Both residential and non-residential building activity are up. August single-family home sales are reported up 15 percent from a year ago for Minneapolis/St. Paul. New residential construction also is reported to be good in South Dakota and Montana. In July, in Minnesota and the Dakotas, contract awards for new public school buildings were up substantially from a year ago, more than offsetting declines in commercial/industrial building.

Manufacturing and Mining

Several new manufacturing plants opened. These include a 220-employee glass plant in Menomonie, Wis., an electronics assembly plant and a boat factory in North Dakota, and a small furniture factory near Billings, Mont. Hurricane Andrew increased demand for building products, especially oriented-strandboard, a plywood substitute that is produced at several plants in Minnesota and Wisconsin.

But these expansions are offset to some extent by recent layoffs. About 100 employees of a paper mill in Ladysmith, Wis., were laid off in a permanent closure. Other layoffs included tractor manufacturing workers in Fargo, N.D., and computer assemblers in Minneapolis/St. Paul.

Recent layoffs also trouble the mining sector. Some 760 workers were laid off at an Eveleth, Minn., taconite mine triggering furloughs for 50 railroad workers. Montana gold mining is reported to be slow. Coal shipments from Duluth-Superior for this year are down 20 percent relative to 1991, due to reduced demand at generating plants in the Detroit area.

Labor Market Conditions

Labor markets are weak. Unadjusted non-farm numbers suggest employment was steady through July, though the layoffs noted above may point to District employment declines in August and September. Non-farm employment numbers are above the same period a year earlier.

Agriculture

Cool weather continues to trouble the agricultural sector. Grain harvesting in North Dakota is running some 50 percent behind normal due to continuing rain. Actual or expected yields are very good for most crops across the region with the exception of the Upper Peninsula of Michigan, though crop maturity has been slowed significantly by the cool weather. All reports stress the need for a late first frost to avoid crop damage, particularly to corn, soybeans and sugar beets.

TENTH DISTRICT - KANSAS CITY

Overview. Economic growth in the Tenth District appears to have improved slightly over recent weeks. Retail sales, including new car sales, increased slightly. Both new home sales and housing starts strengthened in response to falling mortgage rates. Some manufacturers continued to benefit from export sales. Energy activity improved modestly, but prospects for farm incomes remained dim. Retail prices stayed generally stable, while prices for manufacturers' inputs increased slightly.

Retail Sales. Most retailers report a slight improvement in sales over the past month, with notably strong sales of apparel and most soft goods. In the coming months, however, sales are expected to improve only marginally. Stable to lower retail prices have put downward pressure on profit margins. Most retailers intend to hold prices relatively constant through the remainder of the year. Retailers are satisfied with current inventory levels, but most retailers plan a seasonal expansion before the holiday season.

Automobiles sales over the last month were steady to rising, and most dealers are optimistic about future sales. Financing is generally available for both dealer inventories and potential buyers. As the new model year opens, dealers are trimming inventories.

Manufacturing. Most purchasing agents report higher input prices over the past month and expect prices to rise slightly next month. Nevertheless, materials are readily available and lead times remain constant. While some firms are expanding inventories, others are trimming. Firms are generally operating below capacity with no bottlenecks. Exports are rising as firms become more aggressive in marketing their products to foreigners and as the dollar weakens.

Energy. Energy activity in the district appears to be improving modestly. The average number of operating drilling rigs in district states increased from 217 in July to 222 in August, leaving the rig count only 6 percent below its year-ago level. Chiefly responsible for the recent improvement in drilling are higher natural gas prices and tax incentives, which are scheduled to expire at the end of the year.

Housing. Housing starts remain significantly higher than a year ago and have been strong over the last month. Builders expect starts to remain strong for the rest of the year and into next year. New home sales also remain significantly higher than a year ago, causing a low inventory of unsold homes. Mortgage demand is strong in response to lower interest rates, with much of the strength due to refinancing. Respondents expect mortgage demand to level off over the rest of the year as mortgage rates stabilize. Sheetrock and concrete prices have increased in the last month, and builders expect the price of lumber to rise as wood is diverted to hurricane-stricken areas. The increases in building material prices and continued strong housing demand have contributed to rising home prices in the district.

Banking. Loan demand showed no clear pattern last month, with roughly equal proportions of respondents reporting declines, increases, and no change in demand. Most categories of loan demand were also mixed, although demand was stronger for home mortgages, home equity loans, and residential construction loans than for other categories. Loan-deposit ratios moved about in line with loan demand.

None of the respondents reported changing their prime rate in the last month, and only a few expect to lower the rate in the near term. Most respondents lowered consumer loan rates, however, and more decreases are expected. Lending standards were unchanged.

Deposits were up last month at most respondent banks. Demand deposits and NOW accounts showed gains at most banks, while most banks reported little or no change in other categories of deposits.

Agriculture. A relatively lackluster year is expected for district farm income overall. Unexpected strength in cattle prices has offset the sharp decline in crop prices since the beginning of the year. Consequently, farm income is likely to be about unchanged from a year ago.

District cattle feeders have held down inventories, providing support for cattle prices despite a surge in supplies of pork and poultry. Meanwhile, district cattle ranchers continue to enjoy excellent pasture conditions due to the district's abundant rainfall.

The abundant rainfall in recent weeks has also been generally beneficial for district crops. In Kansas and Missouri, above-average yields of corn, milo, and soybeans are likely. But in parts of Oklahoma and Nebraska, heavy rains and hail have damaged crops. Adequate soil moisture will encourage timely planting and development of winter wheat in the district.

The repayment rate of many farm operating loans hinges on when wheat farmers sell this year's crop. Some farmers sold their wheat shortly after harvest and used the sale proceeds to reduce loan balances. But a recent uptick in wheat prices--after a long decline since the beginning of the year--has encouraged many wheat growers to delay selling their grain in anticipation of further price gains. As a result, the pace of loan repayment has slowed.

ELEVENTH DISTRICT--DALLAS

Economic activity appears to have improved slightly since the last survey. While overall growth remains sluggish, many respondents note increased optimism about the outlook. Few respondents report declining activity. Respondents from several manufacturing industries report significant sales gains. Service sector respondents say that demand has increased slightly and many report increased employment. Little growth is reported in department store sales although auto sales are generally reported to be up from year-ago levels. Residential construction is increasing strongly. Declines in the energy industry have abated and respondents say that it is likely that the bottom has been reached. Banks report flat to slightly growing loan demand. Agricultural conditions are mixed.

While most manufacturing respondents note flat or slightly increasing orders, respondents from several industries report strong gains. Respondents generally report increased optimism about the outlook. Industries which are tied to single-family construction report strong sales. One brick manufacturer reported that production was running at full capacity and that backlogs of unfilled orders were growing. Most lumber and wood producers note strong gains in demand and prices due to continued growth in regional home building and the effects of Hurricane Andrew. Orders for cement and concrete, which are tied mostly to road construction, have slowed recently but remain significantly above levels of 6 and 12 months ago. Several producers of electrical equipment say that while growth in new orders recently has slowed, production continues at full capacity. Producers of primary and fabricated

metals report flat to slightly improved orders. Oil field equipment manufacturers note a slight improvement in orders. Conditions in the petrochemical and refining industries remain weak. Paper producers generally note slight gains in orders although a manufacturer of corrugated boxes says that orders are strong and that production is at full capacity.

Growth in the service sector has improved slightly but remains modest. Accounting and legal firms report an increase in activity for transactions type business such as mergers and acquisitions, real estate purchases and new business start-ups. The increased activity along with an improved outlook has motivated employment gains. Respondents in the amusement industry report strong summer sales. Temporary services report flat demand. Many respondents note that businesses are in a wait-and-see attitude until after the election.

Retail sales at general merchandise stores are reported to be sluggish in most of the major markets. Sales are particularly weak in the Houston area. Respondents say that sales in the Dallas/Ft. Worth area are sluggish while sales have improved moderately in the San Antonio/Austin area. Sales along the Mexican border remain strong. Respondents in the auto industry report that sales generally have remained higher than year-earlier levels.

Single-family home construction has rebounded from a brief respite in May and June. Respondents say that inventories of new homes remain low mostly because financial institutions will not lend for speculative purposes. For the first seven months of this year, seasonally-adjusted single-family building permits averaged 5,547 permits per month which is an increase of 25.7 percent from 1991 but still 30.8 percent below the average for the first half of the 1980s. Office demand remains weak overall and any significant

turnaround in office construction is not likely to occur for at least three years. Industrial construction remains weak, although respondents in El Paso expect a pickup due to increased trade with Mexico.

There is a growing consensus that the bottom has been reached in oil and gas drilling. Respondents say that stronger natural gas prices and the Energy Bill, if passed, will provide increased cash flow for drillers. An existing tax credit for tight sands gas drilling which is set to expire at the end of the year should continue to stimulate drilling through year end. Hurricane Andrew caused extensive damage to platforms and pipelines in the Gulf of Mexico. The damage has temporarily reduced the supply of natural gas and has boosted natural gas prices. Cool spring weather and depleted storage had already caused a rebound in natural gas prices from lows reached last winter. Respondents say that without Andrew, natural gas prices would have taken their normal seasonal increase this winter but with repairs in the Gulf taking as long as three to four months, prices are likely to rise above the normal seasonal increase.

Half of the respondents in the banking industry report that loan demand has been flat while the other half say that loan demand has increased slightly. Respondents say that the largest constraint on growth is lack of loan demand from qualified borrowers.

Agricultural conditions are mixed. Respondents report that livestock prices are still considered good, but are below last year's prices. District cotton income is uncertain. Continued cool and damp weather has hindered cotton farmers. Cotton yields are likely to decline but respondents say it is too early to predict the amount of damage.

TWELFTH DISTRICT -- SAN FRANCISCO

Summary

Economic weakness persists in California, and conditions are mixed in other District states. In California, cutbacks continue to be announced in aerospace and defense-related manufacturing. Furthermore, cutbacks in state and local government spending are expected to reduce employment growth in that sector. Outside of California, moderate improvement is reported in retail trade, non-defense manufacturing, and residential construction, with the strongest conditions reported in Utah and Idaho. Drought is threatening agriculture in certain sections of the Pacific Northwest. Overall business sentiment continues to decline. Little upward pressure on wages and prices is reported.

Business Sentiment

Pessimism is increasing among Twelfth District business leaders. Less than 20 percent of our respondents now expect the real economy to expand during the next four quarters at a rate of at least 2.5 percent. This proportion is down from one-third in July and one-half in June. Three-quarters of our respondents expect real output to expand, but at a rate below 2.5 percent.

Wages and Prices

Contacts continue to report little upward pressure on prices in District markets. Grocery prices are reported flat, with meat prices reported down 3 percent from a year earlier and produce prices reported down 9 percent. General merchandise and pharmacy price increases are running at 3.5 percent versus the 6 to 9 percent annual increases seen in 1991 and 1990. Aluminum prices are dropping due to weak demand and large inventories. Lumber prices, which decreased in July, however, have rebounded to high levels as result of Hurricane Andrew. Also, electricity prices are up in Oregon due to drought-related reductions in hydroelectric power. A 20 percent increase in wholesale electricity rates has been proposed in that state, which would increase average retail bills by

5 to 10 percent.

Wage increases appear modest in most District industries. Increases in the retail sector are reported in the 3 percent range, while contacts in banking expect small increases in wages during the next 12 months. Little upward pressure on manufacturing wages is reported due to cutbacks in production and employment.

Retail Trade and Services

District retailers report sluggish conditions for soft goods in most markets. Most retailers are reported to be working to reduce inventories. Major grocery chains are reporting flat sales and declining earnings. Contacts in Oregon report that retail business has been slow, but still profitable, and retail sales in Arizona are reported to have improved. Retail activity in southern California, however, is reported to have deteriorated. Contacts report that tourist-related retail and service sector jobs are down in Los Angeles due to the riots.

Some increases in auto sales in Oregon were reported for August, and contacts in Utah report good summertime new auto sales. A moderate rebound in auto sales is reported in Arizona. However, farm equipment sales are off 50 to 60 percent in Idaho due to the drought.

The recent state budget settlement in California has reduced uncertainty about financing among local governments, but significant cuts in state assistance are expected to result in layoffs. Local governments in Washington have announced a hiring freeze, and state government employment is off in Oregon. Law firms are growing very slowly, and net job losses are expected in accounting. Health care employment continues to increase. Tourism in Hawaii for July was reported down due to discounted air fares within the 48 contiguous states that caused a large drop in California visitors. The effects of the recent Hawaiian hurricane are not yet known, but major damage was confined to the lesser populated island of Kauai.

Manufacturing

Job losses continued to be reported in defense, aerospace, and high-tech manufacturing. Major additional layoffs in these sectors were recently announced in southern California. Layoffs by defense manufacturers and airlines also are reported in Utah. Aviation production rates are dropping, with a small avionics manufacturer in Washington expecting a 10 to 15 percent reduction in its production over the next 12 months. In Washington, contacts report that Boeing's backlog of orders appears to be softening due to weak worldwide economic conditions. The company continues to win a large share of world-wide orders, however.

Outside of these sectors, some modest improvement is noted. In Washington, contacts report improvement in food processing and non-military electronic equipment. In Oregon, heavy truck production is expanding to meet demand from Latin America. Production of computer printers is expected to expand in Washington and Oregon.

Agriculture and Resource-Related Industries

Drought conditions in Idaho are expected to lower farm income by 20 percent this year. Contacts from eastern Oregon report that drought and hot weather have resulted in a short supply of livestock pasture. Wheat yields are anywhere from 15 to 50 percent below a year earlier and are resulting in reduced grain shipments bound for Pacific Rim markets. However, the unusually sunny weather has produced sharp increases in tree fruit crops in Oregon and Washington. Lumber demand and prices have been boosted by reconstruction activity in Florida and Louisiana. Wood products production and employment, however, continue to deteriorate due to the lack of raw timber sales from public lands.

Construction and Real Estate

Construction activity is mixed across District markets. Contacts report that construction activity is stable in Washington and Alaska, but is weak in California and Hawaii. Homes and ranch

properties are selling well in Oregon. One contact in Oregon, however, reports that several major nonresidential projects are on hold until next year. In the Puget Sound area, single family construction is 10 percent above a year earlier, but multi-family construction is 60 percent below a year earlier. Residential construction activity in eastern Washington and northern Idaho continues to rise in response to strong demand. Construction activity in California, however, continues to decline, particularly in nonresidential sectors. Residential markets in California are sluggish, with price decreases reported for higher priced properties.

Financial Institutions

Low interest rates are improving the profitability of District financial institutions, but demand remains soft for commercial, industrial, and consumer loans in most markets. The weakest loan demand is reported in California. Delinquency ratios for commercial real estate in California continue to rise. Deposit growth is reported relatively strong in Arizona, but loan demand has been sluggish except for increased interest in mortgage refinancings. Relatively stronger demand for consumer loans is reported in Oregon, and demand for both consumer and mortgage loans remains brisk in Utah and Idaho. Currently low interest rates have increased the level of mortgage refinancings across the District, but refinancings are still below the levels seen in early 1992. In California and Oregon, contacts report that conventional sources of financing have been almost completely out of the market for construction financing and long-term financing of commercial real estate.