Summary of Commentary on ____________________

Current Economic Conditions

By Federal Reserve District

February 2009
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Reports from the twelve Federal Reserve Districts suggest that national economic conditions deteriorated further during the reporting period of January through late February. Ten of the twelve reports indicated weaker conditions or declines in economic activity; the exceptions were Philadelphia and Chicago, which reported that their regional economies “remained weak.” The deterioration was broad based, with only a few sectors such as basic food production and pharmaceuticals appearing to be exceptions. Looking ahead, contacts from various Districts rate the prospects for near-term improvement in economic conditions as poor, with a significant pickup not expected before late 2009 or early 2010.

Consumer spending remained sluggish on net, although many Districts noted some improvement in January and February compared with a dismal holiday spending season. Travel and tourist activity fell noticeably in key destinations, as did activity for a wide range of nonfinancial services, with substantial job cuts noted in many instances. Reports on manufacturing activity suggested steep declines in activity in some sectors and pronounced declines overall. Conditions weakened somewhat for agricultural producers and substantially for extractors of natural resources, with reduced global demand cited as an underlying determinant in both cases. Markets for residential real estate remained largely stagnant, with only minimal and scattered signs of stabilization emerging in some areas, while demand for commercial real estate weakened significantly. Reports from banks and other financial institutions indicated further drops in business loan demand, a slight deterioration in credit quality for businesses and households, and continued tight credit availability.

Upward price pressures continued to ease across a broad spectrum of final goods and services. This was largely associated with lower prices for energy and assorted raw materials compared with earlier periods, but also with weak final demand more generally, which spurred price discounting for items other than energy and food. With rising layoffs and hiring freezes, unemployment has risen in all areas, reducing or eliminating upward wage pressures. A number

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of reports pointed to outright reductions in hourly compensation costs, through wage reductions
and reduction or elimination of some employment benefits.

**Consumer Spending and Tourism**

Consumer spending remained very weak on balance, albeit with slight firming noted by
many Districts, particularly compared with holiday-season sales that were very disappointing.
About half of the Districts reported that consumer demand was softer than during recent
reporting periods or fell significantly below levels twelve months earlier. However, compared
with the preceding reporting period that included the holiday season, retail spending was
described as “mixed” in the Boston and Richmond Districts, “nearly steady” in Philadelphia, and
slightly improved in Cleveland and Dallas, while New York reported a reduced rate of decline
compared with the “steep” pace in December. But San Francisco characterized retail sales as
“anemic” and pointed to double-digit sales declines relative to twelve months earlier for many
retail outlets. As reported by Richmond, Chicago, and San Francisco, discount chains fared
much better than traditional department stores and specialized retailers, recording sales gains in
many cases as consumers continued to switch away from discretionary spending and luxury
items and toward basic necessities.

The weakness in discretionary spending was also reflected in relative sales by product
type. Sales of luxury goods such as jewelry, electronic equipment, and other big ticket items
were reported to be especially slow in the Philadelphia, Richmond, and Chicago Districts.
Demand for furniture, appliances, and other durable household items remained quite depressed,
according to Kansas City and San Francisco. Sales of new automobiles and light trucks
remained exceptionally sluggish, with Philadelphia, Richmond, and Kansas City reporting
further declines from an already slow pace of sales. Used vehicles fared better in general, with
Kansas City and San Francisco noting that they were selling well and Cleveland and Chicago
reporting improvement over the previous period. Reports of gains in retail spending were largely
limited to grocery stores and pharmacies, although reports from Philadelphia, St. Louis, and
Richmond indicated some pickup in sales of apparel, which the latter District attributed in part to
severe winter weather.

Travel and tourist activity continued to fall in most areas, as households reduced their
vacation travel and corporate travel spending was scaled back. Tourist visits and spending were
reported to be slower than in the previous reporting period or down from twelve months earlier for major tourist destinations in the Richmond, Atlanta, Minneapolis, New York, and San Francisco Districts, with the declines in the latter two characterized as “substantial” and “sharp,” respectively. Airline traffic fell in the Kansas City, Dallas, and San Francisco Districts. Business at restaurants dropped substantially in some areas, notably in the Kansas City and San Francisco Districts, with extensive layoffs and restaurant closures reported in the latter.

**Nonfinancial Services**

Reports on nonfinancial services indicated significant drops in activity accompanied by widespread job cuts. Providers of health-care services reported falling patient volumes, which were attributed in part to a drop in elective procedures in the Richmond, Minneapolis, and San Francisco Districts. Demand continued to fall for professional services such as business consulting and accounting services, legal services, and other professional services in various Districts. However, Dallas noted a modest increase, albeit less-than-expected, in demand for legal services due to increased bankruptcy proceedings. Providers of information technology (IT) services in the Boston District saw a drop in activity on average, although some firms have sustained strong revenue growth; activity among providers of IT services was reported as stable to up in Kansas City, and Minneapolis reported that some IT services firms have seen solid demand from companies that are intent on using the technology to reduce costs. Demand for staffing services weakened considerably. Boston reported that outcomes for providers of temporary staffing services were “dismal,” with revenue declines in the range of 20 to 50 percent compared with twelve months earlier. Chicago and Dallas also reported sizable declines in activity by staffing firms, and New York noted that activity by a major employment agency has “virtually ground to a halt.”

Demand for shipping and transportation services fell further. New York, Cleveland, Richmond, and Atlanta reported reduced activity and layoffs among trucking and rail companies, with the decline in activity described as considerable in some cases. Richmond also reported that shipping activity through ports in that District slowed further, as imports and exports both continued on a downward trend.
Manufacturing

Manufacturing activity fell on net in all Districts, with very sharp declines recorded for some sectors and only partial offsets provided by the few bright spots. Cleveland reported a drop in overall factory output of about 25 percent compared with twelve months earlier. For most Districts, the drop in activity was especially pronounced for makers of capital goods and construction-related equipment and materials, such as primary metals, wood products, and electrical equipment, along with consumer durables such as autos and furniture. Manufacturers of computers, semiconductors, and other IT products saw further declines in production and orders in the Dallas and San Francisco Districts. Slower export sales were cited as a source of weakness for various manufacturing sectors by the Atlanta, Chicago, and Kansas City Districts.

Manufacturing of biotechnology products and pharmaceuticals was one bright spot, with Boston reporting sales gains at a double-digit pace for biopharmaceutical firms, Richmond noting continued hiring of temporary staff among life sciences and pharmaceutical companies, and Chicago reporting continued strong demand for pharmaceuticals. Aircraft manufacturers in the St. Louis District are planning to expand existing production facilities; activity in this sector was largely stable in the Cleveland and San Francisco Districts, but contacts expect some slowing in the future as airlines reduce capacity due to a slowdown in air travel. Food processors and manufacturers of selected chemicals also saw further increases in demand during the reporting period, according to Philadelphia and San Francisco.

As a result of declining production, capacity utilization fell in most manufacturing sectors, with rates as low as 25 to 50 percent reported for some metal fabricators. Several Districts reported that capital spending plans were curtailed further during the reporting period, notably for companies in the retail sector and within manufacturing, which suggests the possibility of further reductions in orders for capital goods going forward.

Real Estate and Construction

Residential real estate markets remained in the doldrums in most areas, with only scattered, very tentative signs of stabilization reported. The pace of sales remained very low in most areas and declined further in some; most Districts reported small declines, but New York cited a sales drop of 60 to 65 percent in Manhattan compared with twelve months earlier. By contrast, Cleveland, Richmond, Dallas, and San Francisco each reported a rising or better-than-
expected sales pace for existing or new homes in some areas, attributed largely to falling prices and improved financing terms for some types of home mortgages. House prices continued to decline, reportedly at double-digit paces in some areas, with little or no signs of a deceleration evident. Builders in various Districts generally remain pessimistic regarding recovery prospects this year, and consequently the pace of new home construction declined further in most areas.

Demand for commercial, industrial, and retail space fell further during the reporting period, with some evidence of more rapid deterioration than in preceding periods. Vacancy rates rose and lease rates declined on a widespread basis; New York noted that commercial real estate markets “weakened noticeably,” while Atlanta described reports on commercial real estate that were “decidedly more negative” than in previous periods. Construction activity has declined commensurately, and assorted reports suggest that market participants expect this weakness to continue at least through the end of 2009. Cleveland noted that public works projects have shown stability of late, although they declined in the San Francisco District as a result of the budgetary struggles of some state and local governments there. Credit constraints and uncertainty were reported to be a drag on commercial construction and leasing activity in the Philadelphia, Chicago, Dallas, and San Francisco Districts.

Banking and Finance

Lending activity fell further on net, with mixed results across Districts and loan categories. Demand for commercial and industrial loans was reported to be lower in most Districts, although Philadelphia reported recent growth in this category. Consumer loan demand also fell in general, although Cleveland reported that it was “stable to up” during the reporting period. Demand for new mortgages remained depressed, but New York, Cleveland, and Richmond noted that refinancing activity continued at high levels or increased further. Boston and Cleveland reported that loan demand and the availability of funds were more favorable for community banks than for institutions with a national scope.

The availability of credit generally remained tight. Lenders continued to impose strict standards for all types of loans, with scattered reports of further tightening and particular scrutiny focused on construction projects and commercial real estate transactions. Despite stringent standards, Atlanta and Chicago noted that funds were available for well-qualified applicants, and Dallas cited contacts who reported that capital has become more readily available. Credit quality
fell for all loan categories, with declines cited by most Districts with the notable exception of Kansas City, where current loan quality was unchanged and expectations for future quality improved modestly. New York reported that the deterioration in quality was most pronounced for consumer loans, while Chicago emphasized deterioration in the quality of business loans as a result of rising bankruptcies. Scattered reports suggested improved liquidity in some credit markets and reductions in interest spreads, with Chicago noting that conditions for the commercial paper and corporate bond markets “improved significantly.”

Agriculture and Natural Resources

Conditions weakened for agricultural producers in various Districts, as demand fell and growing conditions were mixed. Sales slowed for a variety of tree and row crops, grains, dairy products, and livestock, and some product prices declined significantly. Dallas and Atlanta reported that sales were undermined by a drop in overseas demand, and the latter District also faced a sharp decline in demand for peanuts resulting from a recent salmonella outbreak at a processing plant. Planting and growing conditions were mixed within and across Districts, with adequate moisture and favorable temperatures reported for many areas but ongoing drought conditions and restricted water supplies noted by Dallas and San Francisco. Producers benefited from declining input prices on net, but these were not large enough to offset slower sales and lower product prices, which put downward pressure on profit margins and land values, according to Chicago and Kansas City.

Activity slowed significantly for producers of natural resource products. Reduced global demand and lower prices for oil have prompted a sharp cutback in oil extraction activity since last fall, with Dallas noting an “unprecedented” decline in the domestic rig count that was largely concentrated in their District. Respondents from the Kansas City District expect oil extraction activity to fall further as the year proceeds, and Minneapolis noted that natural gas and mining activities also faltered during the reporting period.

Prices and Wages

Upward price pressures were very limited during the reporting period, as a result of lower energy and commodity prices and weak demand for final goods and services across a wide range of sectors. The lower prices of energy and raw materials generally were passed on and contributed to downward pressure on the final prices of various products, according to Chicago
and Dallas. Prices dropped on selected retail items in the Philadelphia, Kansas City, and San Francisco Districts, as discounting was widespread. Selected food products were a notable exception to downward price pressures, with Philadelphia reporting that some food processors raised their product prices. Gas prices rose, but according to Chicago and San Francisco the increase was not large enough to substantially offset the ongoing effects of the net decline from last year’s highs.

Upward wage pressures eased in all Districts, as a rising incidence of hiring freezes and continued job cuts increased the degree of labor market slack. Contacts from various Districts pointed to a higher incidence of wage freezes resulting from the added slack, with a few noting outright wage reductions. Some employers also reduced compensation by lowering benefit costs, including reduced contributions to employee retirement programs, according to the Philadelphia, Chicago, Minneapolis, and San Francisco Districts.
Economic activity continues to slow in the First District, with most manufacturers tallying year-over-year revenue declines, some of which are substantial. Both residential and commercial real estate markets in the region saw some further deterioration in recent months, while staffing and software firms report ongoing declines in demand. Retail results, by contrast, are somewhat mixed. Respondents across sectors say they are restraining compensation in multiple ways, and many firms have cut employment. Although pressures are downward, only a few contacts indicate they are reducing their selling prices; manufacturers say they are avoiding general price cuts either to protect margins or because they foresee little demand responsiveness.

**Retail**

First District retailers report mixed sales results for January and early February, with same-store sales generally ranging from low single-digit percentage increases from a year earlier to single-digit percentage declines. Several contacts indicate that sales were not as soft as they expected, and a few respondents express more optimism, albeit cautious, than in previous conversations.

Retailers continue to manage inventory levels tightly and have cut 2009 capital spending plans, although a few say they are taking advantage of expansion opportunities. Most respondents have invoked hiring freezes and some have already reduced or are considering reducing headcount in the near future. Several contacts have also frozen wages or eliminated bonuses or retirement contributions, and note that employees have taken the news of these freezes and job cuts “remarkably well.”

Overall, First District retailers are watchful, as they expect consumers to continue to be cautious for the next several quarters.

**Manufacturing and Related Services**

Most manufacturing and related services contacts headquartered in the First District report that, based on evidence to date, their sales in the first quarter of 2009 are likely to come in below year-ago levels. About one-half of the respondents express concerns related to excess inventories or rising receivables, representing a deterioration from the last report. Many manufacturers indicate that revenues in some business segments have fallen at a double-digit rate; semiconductor firms and their suppliers say their total revenue drop has been 50 percent or more. By contrast with the general trend, biopharmaceutical sales continue to grow at double-digit rates. In addition, selected respondents outside of the biopharmaceutical industry note that their exports of innovative products or to some foreign markets have held up relatively well over the past year. Some of these exporters are seeing signs of slowdown, however.

Many manufacturers mention that various commodity prices have fallen, but in general these decreases have not been fully reflected in the cost of materials or purchased services. Manufacturers’ selling prices are under downward pressure, prompting some to offer selected reductions. On the whole, however, respondents express reluctance to implement broad price cuts—either out of a concern for margins or because they estimate that customer response would be limited under current circumstances. Biopharmaceutical firms are implementing price increases averaging in the single digits.

About one-half of the contacted firms have cut domestic employment and/or hours in the past three months. Apart from planned growth in the biotech industry, most contacts expect to keep their U.S.
headcounts stable in 2009. About one-third of responding manufacturers have cut employee pay rates. Most of the remaining firms expect to increase pay in the range of 3 percent to 4 percent this year.

Domestic capital spending plans for 2009 are mixed. Some firms intend to adopt labor-saving technologies or to expand their capacity, particularly for research and development or for making high-technology products. Others are cutting their capital expenditures, citing pressures to conserve cash.

Almost all of the contacted manufacturers express caution about their revenue prospects, albeit to varying degrees. Some firms anticipate that their sales will be depressed throughout 2009; reasons include falling automotive production and consumers “battening down the hatches.” Others are hoping for an improved economic environment by the second half of the year, or expect their own company to fare relatively well despite economic headwinds. Some respondents indicate that their strong cash position will provide some buffer against financial stresses in the year ahead.

Software and Information Technology Services

While year-over-year revenue changes reported by First District software and IT services firms range from modest declines to increases of over 25 percent, nearly all contacts indicate slowdowns in activity during the fourth quarter of 2008 and into the first quarter of 2009. Respondents say clients continue to be interested in their product lines but are financially unable or unwilling to commit to transactions. Despite softer demand, New England software and IT services firms have been able to maintain selling prices, although a couple of contacts note that clients are asking for new payment plans or are taking longer to pay. While some firms have reduced headcount and frozen wages, others are making selective hires and intend to give raises in the range of 3 percent to 4 percent. Almost all respondents indicate they are either reducing capital and technology spending or are more cautious regarding spending; for instance, multiple contacts report delaying the purchase of new computers, while others have substituted videoconferences for travel. The down economy is affecting all contacts, with many who had previously hoped for growth in 2009 now predicting flat revenues.

Staffing Services

Staffing contacts in the First District report “dismal” outcomes through the end of 2008 and into 2009, with one remarking that business activity “fell off a cliff in November” and remained slow through January. Revenues are flat to decreasing year-over-year, with declines in the range of 20 percent to 50 percent. Labor demand is reportedly low across all industries in New England, especially in the manufacturing sector; however, a few respondents report demand from state and local governments for skills such as civil engineers and road maintenance workers. Many contacts are witnessing a flood of labor supply, with one respondent receiving 100 resumes in an hour for an administrative position and another reporting that 80 percent of phone calls to his firm are from job seekers. Some contacts have been pressured by clients to reduce bill rates from 5 percent to 15 percent, with those reductions translating directly into decreases in pay.

Several contacts say they believe the New England employment picture is slightly better than the national average, and one notes an increased willingness by candidates, particularly those working in the Midwest’s automotive industry, to relocate to New England. While a few respondents cite a slight uptick in activity in February, all are concerned about the uncertainty of the economy and many anticipate several months before a recovery occurs.
Commercial Real Estate

The commercial real estate market showed signs of further deterioration throughout the region in recent weeks. Contacts in Boston drew attention to the fact that rents are falling rapidly across the metropolitan area, for both office and retail space. One contact described a rental markdown of close to 25 percent for space in a downtown office building, just within the last two weeks. Another Boston contact estimates that downtown office rents are down 20 percent on average since September 2008. Contacts also point out that, in a growing share of cases, rental rates are not being published in property listings, a sign that rates are negotiable. The downward pressure on rents reflects a sharp increase in the supply of space for sublease even as official vacancy figures edged up only slightly. Office vacancy was estimated by one contact at about 12 percent downtown, 18 percent in close-in suburbs, and 27 percent in the outer suburban ring.

In Providence, the downtown office market is described as stable, but sublease supply is up and downward pressure on rents is mounting. Some retail closings were reported in Providence, and the industrial market is “drifting lower, but not in big trouble yet.” No major changes are reported for Hartford, but deal volume is close to zero for both leasing and sales. Office vacancy increased “marginally”, but sublease supply has doubled since December 2008. Retail vacancy has risen in the area, but not by as much as this contact predicted earlier in the year.

The credit situation is described as largely unchanged since last report. Financing continues to flow to deals under $10M but remains scarce for deals above that threshold and virtually non-existent for deals over $50M. The financing for the smaller deals is coming from community and regional banks around the region with healthy balance sheets. One Boston contact expects an increase in defaults on large commercial properties as risky loans come to maturity in the next 12 months; he says borrowers will be unable to refinance these large deals unless investors return to the securitization market.

Contacts expect further deterioration in the commercial market in the coming months due to ongoing weakness in the economy and ongoing disturbances in credit markets.

Residential Real Estate

Home sales and prices showed steep declines across the New England region in December 2008 and January 2009. Home sales in December declined year-over-year by 6 percent in Rhode Island, 16 percent in Maine, and 20 percent in Connecticut. In January, home sales dropped 12.5 percent year-over-year in Massachusetts and 35 percent in New Hampshire. Median home prices also continued to drop across the region. Inventory continues to decline in Massachusetts. By contrast, because of the low level of sales activity, New Hampshire had almost 23 months of supply in January 2009, up from 11 months of supply in January 2007.

Condo sales dropped more than 25 percent year-over-year in Rhode Island and Connecticut in December and in Massachusetts in January. While home prices saw large declines throughout 2008, condo price declines were much more modest until recently. In the New England states for which they are reported, median condo prices fell 10 percent to 26 percent year-over-year in December or January.

Contacts are generally optimistic regarding the tax credit included in the stimulus package. Even though the new $8,000 credit is still available only for new homebuyers, they are pleased that Congress removed the payback requirement that was part of the 2008 $7,500 credit.
The Second District’s economy has weakened noticeably since the last report. In general, contacts in both the manufacturing and non-manufacturing sectors report broad-based deterioration in general business conditions in recent weeks and most do not anticipate improvement in the months ahead. In particular, contacts report widespread softening in the labor market, especially in New York City. Retail sales were sluggish in January, though not down as sharply as in December, while consumer confidence remained near record lows. Tourism activity in New York City weakened substantially in January and in early February. Both residential and commercial real estate markets deteriorated since the last report, though housing markets in parts of upstate New York appeared relatively stable. Finally, bankers report that refinancing stabilized demand for home mortgages but that demand for other categories of loans declined further; they also report further tightening in credit standards and higher delinquency rates—especially on loans to the household sector.

**Consumer Spending**

Retail sales were sluggish in January, though year-on-year declines were less pronounced than in December. New York State reports that sales tax revenues for the month were down modestly from a year ago, following a steep decline in December. Retailers in western New York report that business from Canadian shoppers has weakened in recent months, partly attributed to a pullback in the Canadian dollar. Consumer surveys show confidence remaining near record lows. The Conference Board reports that consumer confidence among residents of the Middle Atlantic states (NY, NJ, PA) edged up from a record low in January. Similarly, Siena College’s monthly survey of New York State residents showed confidence edging up for the second consecutive month, after falling to a record low in November.

Tourism activity in New York City has slowed substantially since the last report. Manhattan hotels report marked weakening in business thus far in 2009, following a moderate pickup in December. Revenues per room are reported to have fallen by a record 30 percent from a year earlier in January and appear to be
running nearly 40 percent lower in February. Occupancy tumbled roughly 15 percent from a year earlier in January, while average room rates fell 15 percent. While much of the weakness reflects softening demand, an industry contact notes that about half the decline in occupancy rates is due to new hotels opening; the total number of hotel rooms in Manhattan is expected to increase by roughly 7,000 (10 percent) in 2009, or more than triple the net increase in 2008. Broadway theaters report substantial slowing in both revenues and attendance since the last report, in part reflecting the closing of an unusually large number of Broadway shows (13) in January. In the first half of February, revenues were down nearly 20 percent from a year ago, while attendance fell by close to 25 percent; this compares with single-digit percentage declines in January and slight increases in December.

Construction and Real Estate

Housing markets in the District have been mixed but generally weak since the last report. Manhattan’s residential rental market continued to soften in January, with asking rents reported to be down 3 to 9 percent from a year earlier; in addition, a growing number of landlords are offering one or more months of free rent and are paying any rental fees. Perhaps as a result, rental vacancy rates, which had been rising steadily in the second half of 2008, edged down in January. A major appraisal firm reports that Manhattan co-op and condo prices have continued to decline since the beginning of the year and are down by an estimated 20 to 25 percent from last summer; the number of transactions thus far in 2009 has been running 60 to 65 percent lower than a year ago. A contact reports seeing very few transactions at the high end of the market in Manhattan, and that most of them seem to be all-cash deals. Inventories are rising seasonally from an already-high level and that backlog is said to be accompanied by a large and growing amount of “shadow” inventory in new developments.

The market for single-family homes in and around New York City has also weakened, though market conditions were reported to be more stable in upstate New York. Contacts in northern New Jersey report little or no discretionary activity in the resale market—almost all transactions are either foreclosed
properties or distress sales by owners that need to move. In this environment, market prices are difficult to
gauge, but an industry expert estimates that they are down 15 to 20 percent from the 2007 peak, with steeper
debt at the high end. Separately, a real estate industry contact notes a rising number of “short sales,” for
which the mortgage holder agrees to accept less than the full principal balance upon the sale.

Commercial real estate markets in the District weakened noticeably in January. An industry contact
notes that New Jersey’s office and retail markets have deteriorated substantially in recent months.
Manhattan’s office market has also slackened markedly: the vacancy rate jumped nearly a full point in
January, to 11.3 percent—up from 7.6 percent a year ago. Most of the increase was concentrated in
Midtown, particularly in the financial sector. Asking rents for Class A space fell 2 percent in January and
are down more than 13 percent from a year ago, though an industry contact notes that this understates the
weakness because rents are increasingly negotiable and landlords are offering more concessions. There has
been virtually no activity in Manhattan’s office sales market. New York City’s retail rental market has also
softened, except at the low end (groceries, drug stores, etc.). Demand for retail space has contracted
substantially, particularly in the banking sector—until recently, banks had been substantial users of space.
Also, the bankruptcy of a major electronics retail chain, as well as of other retailers, has added a good deal
of available space, and landlords are concerned about the outlook for other retail chains.

Other Business Activity

Labor market conditions have deteriorated markedly. Both manufacturing and non-manufacturing
firms in the District report increasingly widespread cutbacks in their employment levels in February, and a
sizable proportion expect further retrenchment in the next six months. Separately, a major New York City
employment agency reports that hiring activity has virtually ground to a halt since the beginning of the year,
during what is usually a busy season. Large financial firms, as well as legal firms, have all but stopped
hiring; some demand from smaller firms has appeared sporadically, but they are skittish about filling job
openings unless essential. Weakness in the labor market is said to be reminiscent of 2002, but more disconcerting, because this time it is seen to be more broad-based and more structural.

In assessing overall business conditions, manufacturers and other firms report widespread deterioration in general business conditions in February and flat to declining selling prices. Moreover, a large majority of respondents do not anticipate any noticeable improvement in conditions in the next six months. New York State reports a sharp decline in personal income tax revenues in January, compared with a year earlier, evidently reflecting sharp declines in bonus income in the financial sector.

A trucking-industry contact reports that shipping volume fell sharply in December, dropping roughly 15 percent from a year earlier; this followed a modest uptick in November, when the 12-month decline was under 10 percent. With the ongoing weakness in trucking, and given that the first quarter is typically a slow season anyway, layoffs have been widespread, and a glut of used trucks (especially tractor-trailers) for sale has developed. Truckers have seen some relief from diesel prices, which have fallen even more precipitously than regular gas prices recently.

Financial Developments

Small to medium-sized banks report weakening demand for loans in all categories except residential mortgages, for which demand was little changed. The percentage of bankers reporting weakened demand ranged from 39 percent in the consumer loan category to 45 percent in the commercial and industrial loan category. Bankers reported an increase in the refinancing rate; 42 percent of bankers reported an increase while 8 percent reported a decrease. For all loan categories, respondents indicate tightening credit standards—most notably in the residential mortgage category. No banker reported an easing of credit standards for any loan category. Respondents note a decrease in the spreads of loan rates over cost of funds for the residential mortgage category but increased spreads for the commercial mortgage segment. Spreads were generally steady for all other loan categories. Contacts indicate a decrease in the average deposit rate. Finally, bankers report increased delinquency rates across the board, but most notably for consumer loans.
Business conditions in the Third District remained weak in February. Manufacturers, on balance, reported declines in shipments and new orders. Retailers indicated that sales were nearly steady but below the level of a year ago. Motor vehicle dealers reported continued declines in sales. Bank loan volume has risen very slightly in recent weeks, but credit quality has continued to deteriorate. Residential real estate sales and construction remained low but appeared to be close to steady. Commercial real estate investment and construction activity have been moving down. Service-sector activity has generally declined in recent weeks. Business firms in the region reported decreases in most input costs and output prices in February.

The outlook among Third District businesses is generally not bright, although there has been some improvement since the last Beige Book. Manufacturers forecast increases in shipments and orders during the next six months. Retailers expect sales to remain slow while consumers remain concerned about job security. Auto dealers see no indications of improvement in sales. Bankers expect lending to move up slowly during the year. Residential real estate agents and home builders expect sales to remain slow through most of the year. Contacts in commercial real estate expect leasing and purchase activity to fall further this year, and they expect vacancies to rise. Service-sector firms expect activity to be slow through most of the year.

Manufacturing

Third District manufacturers reported continuing declines in shipments and new orders, on balance, from January to February. Around one-half of the manufacturers surveyed noted decreases in those measures, and around one-fifth reported increases. The balance of negative over positive reports increased from January to February. However, much of the recent worsening in the region’s manufacturing sector has been among producers of primary metals and electrical equipment. Demand for industrial equipment and materials has been especially weak because, as one manufacturing contact said, “customer purchasing for capital projects is on hold.” In contrast, demand has increased for food products, chemicals, some finished products, and testing and measuring instruments.

Despite poor current conditions, the outlook among Third District manufacturers has improved since the last Beige Book. Among firms polled in February, nearly one-half expect
new orders and shipments to increase during the next six months, and one-quarter expect decreases. However, capital spending among area manufacturers is being reduced, on balance, as the number of firms planning to cut outlays for new plant and equipment continues to exceed the number planning increases.

Retail

Third District retailers generally reported nearly steady sales during February, although the year-to-year comparison remained negative for most. Merchants said sales of basic apparel and household items have been steady or rising, but sales of most other lines of merchandise have been weak. Reflecting the comments of most area retailers, one store executive said, “The consumer is focused on the basics, and sales of big ticket items are still falling.” Merchants indicated that sales of big ticket appliance and electronics items and jewelry have been falling steeply. In contrast, sales of some apparel items were up. The outlook among the region’s retailers is not positive, but some contacts believe consumer spending could gather strength if employment conditions show signs of stabilizing.

Third District auto dealers reported further slowing in sales in February. Demand has fallen for all makes and models. Dealers said the availability of financing for car purchases continued to limit sales, as well. Dealers also reported continued difficulty in obtaining inventory financing. Looking ahead, dealers see no signs of an upturn, and they expect the financial difficulties of domestic manufacturers to negatively affect demand for those companies’ vehicles and the business operations of dealers selling them.

Finance

Total outstanding loan volume at Third District banks has edged up slowly in recent weeks, according to bankers contacted for this report. The gain has been mostly the result of modest growth in commercial and industrial lending. Residential real estate loan volume outstanding has been practically flat, and consumer loan volume has declined. Commercial bank lending officers attributed the slowness in lending to falling demand for credit. “The weakness in lending is on the demand side,” one banker noted, and another said, “The news coverage has the public convinced the banks aren’t lending, but we’re looking for business.” However, other bankers said that an ongoing process of consolidation among large banks with branches in the
region continued to divert those institutions from major loan marketing efforts. Several contacts also noted that lending and investing by financial companies other than banks have been limited, especially in certain sectors, such as construction, real estate, and retail trade. Most of the banks contacted for this report said that credit quality continued to decline for all categories of credit. Looking ahead, bankers expect slow expansion in lending this year, and they are becoming increasingly concerned that a prolonged economic slowdown will result in further weakening in the creditworthiness of both business and individual borrowers.

**Real Estate and Construction**

Residential real estate activity in the Third District remained weak in February. Residential real estate agents and builders reported that sales have been nearly steady, but at a very slow pace. One builder said that “sales have been anemic,” and another said the rate has been “the lowest we have ever seen.” Inventories of both new and existing homes for sale have been practically unchanged since the beginning of the year. Builders continued to offer substantial incentives to purchasers, but real estate agents said an increasing number of sellers of existing homes have preferred to offer them for rent rather than accept low offers. Builders and agents expect sales to remain slow through most of this year, although some said that government programs to stimulate home buying could provide a lift to sales.

Commercial real estate firms indicated that construction, leasing, and purchase activity have remained on a downward trend since the last Beige Book. Contacts said a sharp reduction in financing for commercial real estate has put commercial properties of all types under downward price pressure, and that falling employment has reduced the demand for space, resulting in declining rents. Contacts expect commercial real estate investment and construction activity to remain weak through the year, and they expect vacancy rates to rise and rents to decline until overall economic conditions begin to improve.

**Services**

Service-sector firms generally reported a drop in activity since the last Beige Book. Business and professional services firms indicated that the reduction in activity has prompted layoffs and other cost-cutting measures. Firms providing services to the construction, real estate, and finance sectors reported particularly sharp pullbacks in demand. One such firm said that “we
are living hand to mouth” and trimming every possible budget item. Many of the region’s educational institutions have also been limiting expenditures. Endowment values have declined for most, and some have seen reductions in applications and enrollments. The outlook among area service firms remains negative, and several contacts say they have pushed out their expectations for a rebound to later in the year or into next year.

**Prices and Wages**

Reports on input costs and output prices largely reflect further declines since the last Beige Book. Manufacturing firms continued to note decreases in prices for most of the materials they use. Most also reported reducing their own prices, although food processors have raised prices recently. Retailers have reduced prices for some apparel and many large appliances and furniture, mainly in an effort to work down inventories in preparation for new spring merchandise. Prices of other goods were said to be mostly steady.

Firms in a wide range of industries reported they were implementing salary freezes or reductions and cutting back on fringe benefits, including 401-K matching contributions. A growing number of employers in the region have announced hiring freezes as well as immediate and prospective layoffs. Several firms that reported they intended to maintain staffing levels noted that they were reducing hours, imposing unpaid furloughs, or scheduling temporary plant shutdowns in order to reduce wage bills.
Economic activity in the Fourth District has weakened further since our last report. The downward trend in factory output and steel shipments that began late in the third quarter of 2008 continued. Residential construction remains very weak, with no improvement expected during 2009, while commercial builders reported a significant slowdown in construction activity. Sales by District retailers did show a slight improvement, but purchases of new motor vehicles remained at very low levels. Even though industrial demand has been falling, there was little change in energy production. Freight transport volume remains at low levels. Finally, regional bankers told us that commercial and industrial lending is flat to down, while community banks experienced some growth in C&I loans.

Employment dropped across all industry sectors except energy and healthcare. Staffing firms reported an overall decline in job openings as well. Given the weak labor market, wage pressures are contained. Capital spending has been trimmed back significantly from 2008 levels, and further cutbacks are contemplated. Almost all of our respondents affiliated with manufacturing, construction, and energy companies report that raw materials prices were stable or falling.

Manufacturing. Output by most District factories remained at low levels during the past six weeks. Any increased production was attributed to seasonal adjustments or the exit of market competitors. On a year-over-year basis, factory output fell by more than 25 percent on average. Respondents expect demand will remain very soft during the next few months. Almost all steel producers and service centers reported a worse-than-expected slump in shipping volume. The only end markets cited as showing some stability were energy and aerospace. Further, respondents believe that the demand for steel will remain at very low levels through at least the first half of 2009. District auto production declined precipitously during January on a month-over-month and year-over-year basis. The declines were felt by both domestic makers and foreign nameplates. A significant part of the downturn on the domestic side is attributable to an extended year-end shutdown of a small-car assembly plant and the permanent closing of a plant that produced SUVs.

Half of our contacts said that their companies have trimmed back or halted capital expenditures during the past couple of months. Further, most of them expect additional cutbacks or a freeze on spending during 2009. We heard only a few reports of customers falling behind in
payments on their accounts receivable. Suppliers to the residential construction industry cited difficulties obtaining credit. A majority of our contacts told us that raw materials prices, especially for metals, have fallen since our last report. Product pricing remains relatively stable, with some reductions noted. Manufacturers expect little inflationary pressure during 2009. Almost all of our survey respondents have laid off employees or increased the number of nonproduction days. Predictably, wage pressures are contained.

Real Estate. The residential construction industry remains very weak. Two contractors noted that January sales were slightly better than anticipated, and most of our contacts reported a rise in Internet and foot traffic. Nevertheless, builders are not expecting an industry turnaround through 2009, which they attributed to a lack of consumer confidence, tight credit, and excess inventory. There has been little change in the list prices of new homes, though builders are discounting. We continue to see some moderation in the prices of building materials and labor costs. General contractors and subcontractors reported minimal staff reductions.

Almost all the commercial builders we contacted told us there has been a significant slowing in construction activity during the past couple of months, and they expect this trend will continue through 2009. The only market segments cited as showing some stability were public works and energy. Contractors continue to pare down their backlogs, while inquiries have fallen off. Bidding on any new projects is very aggressive, as is subcontractor pricing. Construction materials prices have declined, especially for metal products. A majority of our contacts have laid off employees.

Consumer Spending. January sales for District retailers improved slightly on a month-over-month basis across nearly all industry segments. However, most survey respondents expect sales will flatten out or decline in the upcoming months. The exception is food sellers, who anticipate a small pickup in sales. On balance, there has been little change in vendor or retail pricing since our last report. Accounts from auto dealers show that purchases of new vehicles remain at very low levels, while used vehicles sales have improved. Dealers are not expecting an industry turnaround during the next few months. We heard numerous reports of retailers and auto dealers eliminating sales and front office positions and cutting back on store hours. Capital expenditures by retailers have been trimmed back significantly from 2008 levels.

Banking. Regional bankers told us that commercial and industrial lending is flat to down, while community banks reported increased demand for C&I loans. A majority of banking
executives experienced some upward pressure on loan rates. On the consumer side, lending is stable to up, with several bankers commenting that home equity lines of credit remain the bright spot in their loan portfolios. Pricing for consumer loans showed little change. Refinancing applications for residential mortgages remain at high levels. Credit quality for consumer and business loan applicants has deteriorated, while the number of loan delinquencies increased across nearly all categories. Still, most contacts do not anticipate any further tightening of credit standards. Core deposits rose since our last report, with several bankers noting that deposit pricing is still very competitive. Major regional banks cut staff significantly, while community banks trimmed staff through controlled attrition. Several respondents’ institutions reduced or eliminated merit increases.

**Energy.** On balance, energy production has been stable during the past six weeks, with little change expected during the upcoming months. Nevertheless, nearly all of our contacts commented that industrial demand has been falling. Further, most oil and gas producers significantly reduced drilling activity. Prices received for oil and natural gas continued to drop, while coal prices were stable. For the most part, materials and equipment costs were stable or falling. Capital expenditures remained on plan; however, several producers told us that they intend to lower spending during the next few months. Access to credit was cited as an issue by an increasing number of our respondents. Employment levels were stable with little wage pressure.

**Transportation.** Shipping volumes for freight transport service companies remained at low levels, with little volume change over the past six weeks. On a year-over-year basis, January shipments were down 15 percent on average. The only market segment exhibiting some stability was energy, particularly coal. Expectations call for activity to remain at current levels or to decline further during 2009. Few problems in collecting on accounts receivable were reported, other than some slowdown in payments. Several trucking executives noted a small increase in the price of diesel fuel and significant increases in turnpike tolls, which they are unable to pass through to customers. Little change in capital spending was reported; though most companies have reduced expenditures to the replacement level. Several trucking executives are laying off drivers as part of their capacity reduction plans, while others did not replace drivers who have left voluntarily.
Overview. Economic activity in the Fifth District declined further in January and the first half of February. Business contacts across the service sector reported decreases in revenues and employment. Demand for manufactured goods also declined, with firms reporting idled or closed plants, excessively high levels of inventories, and falling product prices. Growth in residential lending was the one bright spot in the District, although the expansion was driven by refinancing activity. Meanwhile, commercial lenders observed deterioration in credit quality and commercial leasing activity fell in most areas of the District. Temporary employment agents also described reduced demand for workers, although they were somewhat optimistic about the next six months.

Retail. Retailers provided mixed reports on sales, although revenues were generally lower in recent weeks. A manager at a sporting goods store in western West Virginia said his total sales volume was down, despite a boost in apparel sales from severe winter weather. The owner of a chain hardware store in central Virginia noted that customer traffic had dropped, but that the size of the transactions remained steady. In contrast, managers at big box discount stores in Virginia Beach, Va., and central North Carolina told us the weak economy had raised both their customer traffic and their revenues. Contacts also reported a fall in big-ticket sales since our last report. Sales of new domestic automobiles continued to slump at District dealers, with sales of foreign nameplates also down, but to a lesser extent. On the other hand, a few car and light truck dealers observed strong performance in used vehicle sales and increased business in their service departments in recent weeks. Retailers continued to report cuts in jobs and hours. A spokesperson for a group of central Virginia retailers said many constituents were cutting hours and “the owners of smaller stores are more frequently on the floor” to cover the cutbacks. Retail prices grew at a somewhat slower pace. Fuel prices declined, according to contacts, and a grocery executive with store locations in Virginia and surrounding states noted that prices edged down for fresh produce and dairy products. Average retail wages contracted since our last report.

Services. Contacts at services firms saw generally slower demand in recent weeks. Several restaurant owners and managers reported a sharp decline in traffic and revenues. A contact at a national freight trucking firm in the District said freight volume was down and that his firm succumbed to downward rate pressures “to keep in line with competition,” while cutting wages for several classes of employees. A hospital administrator in central North Carolina noted
that demand for surgeries at that facility had fallen as local layoffs continued. Employment at services firms also declined across the District in recent weeks. A contact at a central North Carolina healthcare system told us that his organization had instituted a hiring freeze; an executive at an environmental services firm in Maryland reported that workers’ hours were reduced because of slow demand; and an executive at a commercial property management firm in central North Carolina observed a “constant drumbeat of small layoffs.” Average wage growth was little changed since our last report while price growth at services firms slowed.

**Manufacturing.** District manufacturers reported that production activity contracted further with broad weakness across shipments, new orders, and employment. A producer of automotive upholstery fabric in North Carolina said his company was facing deep declines in orders, while a machinery manufacturer in South Carolina noted that many of his suppliers were in dangerously poor financial health. A number of lumber companies also reported continued steep drops in sales, excessively high inventories, and continued price decreases. A contact at a lumber company in West Virginia that is eliminating one shift and disallowing overtime reported that, “This is the worst economic situation since our company began in 1972.” A primary metal manufacturer in South Carolina told us that the price for his product had dropped about 50 percent from last August and that without fast improvement, layoffs will deepen and wages and benefits will tighten. Meanwhile, a fabricated metal producer in West Virginia informed us that the company had shuttered a plant with about 700 employees due to the low aluminum price. Correspondingly, raw materials and finished goods prices were down significantly from our last report.

Activity at District ports weakened further since our last report. Imports declined amid continued concerns about consumer spending and inventory levels, while exports struggled across the board over the last two months. Contacts across the District reported seeing shipping lines scale back operations in recent weeks by delaying or consolidating services.

**Finance.** Residential lenders reported that activity picked up in January and February. The uptick was centered on firmer demand for refinance, which comprised 65 to 80 percent of applications since our last report. Some contacts noted, however, that refinancing was being constrained by appraisals “coming in at the lower end of the range.” Credit standards tightened slightly in recent weeks as lenders reported stricter verification of income and employment, required higher FICO scores, and applied more stringent appraisal standards. In contrast to
residential lending, demand for commercial loans remained sluggish. Bankers reported that businesses were increasingly cautious about making new deals, but noted some increase in refinancing activity for commercial properties. Credit standards remained tight with few changes in policy, although lenders reported scrutinizing applications more carefully “with a longer recession than initially thought in mind.” Contacts also noted a decline in credit quality since our last report. Bankers reported that year-end statements from their clients showed “continued stress” on balance sheets, especially for middle-market and consumer product-related firms.

**Real Estate.** Reports from Fifth District residential real estate agencies remained dismal. Most Realtors continued to report very slow house sales in January although there were spotty reports of some pickup in February. A Washington, D.C., agent told us that January and February sales were “extra slow” – prices were down 17 percent from a year ago and the number of units sold was down 40 percent. Business remained “very slow” in Greenville, S.C., and in Richmond, Va., with the Richmond contact reporting rising inventory levels. An agent in Fairfax, Va., told us that he was expecting strong spring sales and that his open houses had been flooded with customer traffic. In contrast, a Greensboro, N.C., Realtor reported low consumer confidence, bankruptcies, and closings among some major builders. However, he was optimistic for a turnaround in the next few months due, in part, to several prominent companies locating in his area by the end of 2009 and early 2010. House prices dropped across much of the District.

District commercial real estate markets remained stagnant from January to mid-February. Leasing activity declined in most areas, although contacts reported some interest in office space in northern Virginia, Norfolk, Va., and Charlotte N.C. While posted rental rates were unchanged in most markets, negotiation was more common and landlord concessions were on the rise. A Baltimore, Md., agent reported that there was “no point asking what the face rent is – it’s all about what tenants can afford.” Concessions grew in Columbia, S.C., as landlords “scrambled” to renew leases, while tenants in Norfolk and Charlotte sought rent relief to avoid defaulting on contracts. Vacancy rates rose in Baltimore, Washington, D.C., Raleigh, N.C., and Charleston, S.C., – especially from a glut of big box retail space coming on to those markets – but held steady in Richmond, Va., and Charleston, W.Va. Commercial sales activity was at a standstill in Baltimore, Richmond, Columbia and Charleston, S.C., although bargain hunters with cash were active in the northern Virginia and Norfolk markets. Property prices held steady or decreased slightly as limited financing and soft demand reduced the number of sales transactions.
Tourism. Although contacts on the Outer Banks of North Carolina and in Virginia Beach, Va., told us that bookings for Valentines’ Day weekend were somewhat stronger than a year ago, overall tourist activity along the coast was a bit weaker when compared to our last report and to a year ago. An analyst from Myrtle Beach attributed the weakness to ongoing concerns about the national economy. He also indicated that the reduced bookings had pushed hotels to roll out discounts earlier. In contrast, a manager at a ski resort in Virginia reported that time share sales were running “neck-and-neck” with last year, total bookings were up, and tourist spending was steady. Similarly, a contact at a West Virginia ski resort told us that bookings were somewhat stronger than a year ago, which he attributed to patrons taking advantage of cheaper room rates during the week.

Temporary Employment. Fifth District temporary employment agents reported generally weaker demand for workers since our last report. Contacts cited the difficult economic conditions as reasons for the drop in demand. One agent reported that although business was slower than last year, the past two years were particularly strong, and hiring had continued in the life sciences, pharmaceutical, professional services, and IT industries. A contact from Raleigh, N.C., was optimistic that demand would be stronger over the next six months with new business in the area, recent company acquisitions, and lifted freezes on hiring. In addition, when business improves, the contact expects many companies to hire workers on a contractual rather than a payroll basis, thus increasing demand at staffing companies.

Agriculture. Colder-than-normal temperatures, combined with relatively low precipitation, hindered crop development in some parts of the District. For example, a contact in Virginia reported that colder temperatures and below-average precipitation had slowed small grain growth. At the same time, other farmers benefited from the moderately dry weather, such as farmers in southern areas of the District who were able to get an early start on land preparation.
SIXTH DISTRICT – ATLANTA

Summary. Sixth District economic activity weakened further in January and early February compared with late 2008. Most retail contacts reported that consumer spending declined more than expected. Residential real estate contacts noted that sales continued to slide, although at a more modest pace than last reported. Residential construction levels remained at very low levels. The outlook among commercial real estate contacts worsened as vacancy rates continued to rise. Manufacturing contacts noted further reductions in orders and production. By most accounts, business and consumer access to credit remained tight and loan demand was generally weak. Labor market conditions worsened as more businesses reported cutbacks in hours and layoffs. Price pressures remained subdued throughout the District.

Consumer Spending and Tourism. Retail activity remained weak. District contacts reported that sales and store traffic for January and February were disappointing and expectations were lowered for the coming months. Several retail chains reported closing underperforming stores. Auto dealers reported dismal January sales for both domestic and foreign makes. Inventories of District assembled vehicles continued to climb.

Tourism activity slowed in most parts of the District. Despite increased price discounting and promotional activity at various attractions, the overall number of tourists visiting Florida fell early in the year compared with late 2008 levels. Reports from New Orleans indicated that hotel occupancy rates for Mardi Gras were on par with 2008 levels.

Real Estate and Construction. Reports from homebuilders and Realtors indicated that new and existing home sales remained weak during January and early February. However, sales declines measured year-over-year moderated slightly. Some contacts noted a pickup in traffic, with potential buyers mostly interested in finding deeply discounted homes. Existing home inventories generally rose above year-earlier levels, while new home inventories were slightly below year-earlier levels. Housing starts remained very weak, and the outlook among builders continued to be pessimistic. However, the uptick in traffic led most Realtors to be cautiously optimistic that sales were approaching a bottom.
Commercial real estate reports were decidedly more negative than previously reported. Vacancy rates continued to rise in many parts of the District and this was putting downward pressure on rents, most notably in the retail sector. Most District commercial contractors reported declines in activity, with more projects postponed or cancelled. Going forward, commercial real estate contacts anticipate that more space will become vacant in coming months and that construction will slow significantly.

**Manufacturing and Transportation.** A majority of District manufacturing contacts noted further declines in production levels and new orders compared with a year earlier. The number of export orders continued to fall, and most contacts reported that inventory levels decreased as well. Contacts remained generally pessimistic about near-term production, employment, and price levels amid severe contractions in demand.

District transportation contacts reported that January and early February were very weak. Several trucking contacts servicing retail and building product industries reported a considerable drop in tonnage and lower revenues. Regional rail activity was also down compared with a year earlier, with continued declines in shipments of autos, chemicals, and construction-related items.

**Banking and Finance.** Most District banking contacts reported that access to credit remained tight for both consumers and small businesses for the first two months of 2009, although money was available to customers who met stricter credit standards. Some contacts reported that job insecurity was having a negative effect on loan demand, with potential borrowers feeling uneasy about taking on additional debt.

**Employment and Prices.** Labor market conditions remained bleak for the District in January and February. Business contacts continued to note reduced hours and layoffs across most industries.

Most District contacts reported a continuation of lower input costs. Manufacturers and construction firms reported that prices paid for both raw materials and finished goods declined further over the past two months and are expected to remain soft in the near term. Several manufacturing contacts noted that final goods prices were relatively stable in January following cuts to prices made late last year.
Natural Resources and Agriculture. Energy industry contracts confirmed that regional fuel stocks were well above their typical winter levels, even as refineries scaled back operations and underwent seasonal retooling.

Most of the District received much needed rainfall in January. However some areas in Alabama and Florida continued to report poor soil moisture conditions. The Districts’ poultry and cotton producing industries continued to be affected by lower global demand. The recent salmonella outbreak had a significantly negative effect on the local peanut industry, and the severe drop in consumption and uncertain outlook threatens the economies of several rural communities where major production facilities are located.
SEVENTH DISTRICT—CHICAGO

Summary. Economic activity in the Seventh District remained weak in January and February. The expectation of most contacts was for economic activity to remain weak into late 2009 before slowly beginning to recover in 2010. Consumer spending, construction, and manufacturing activity continued to decline, and labor market conditions deteriorated further. Credit conditions remained tight. Price and wage pressures tilted toward the downside. Most key agricultural prices decreased during the reporting period.

Consumer spending. Consumer spending continued to soften. Retailers reported that sales were slow, with apparel, big-ticket, and luxury items experiencing the largest declines. Discount stores and fast-food restaurants fared better than their higher-priced counterparts. A contact noted that inventory reductions were likely to be substantial for the first quarter. Auto dealers reported slight increases in showroom traffic and sales, particularly for used vehicles. Nonetheless, their expectations for overall vehicle sales moved lower. Auto dealers also noted that service center activity continued to be strong, while vehicle inventory levels remained elevated and new orders were down substantially.

Business spending. The pace of business spending continued to weaken. Contacts reported that they were trying to control costs by closely monitoring expenditures and by reducing inventories. Furthermore, contacts in several industries cited cuts in annual capital expenditure budgets as well as delays in the timing of capital spending. Labor market conditions in the District deteriorated. A contact noted that the longer the duration of the current downturn, the more plant closings and permanent layoffs will replace the temporary measures of rotating shifts and reducing hours now being employed to lower output but still retain labor. Additional layoffs were reported across a wide variety of industries. Hiring activity remained low, outside of lower-end retail companies, healthcare, environmental related businesses and highly skilled professionals in financial services and information technology. In addition, a staffing firm reported a sizeable reduction in billable hours from the previous reporting period.

Construction/real estate. Construction activity in the District weakened further from the previous reporting period. Residential construction continued its steady decline, with housing demand remaining low, particularly for higher priced homes. Few mortgage originations reflected new purchases, and even the recent boom in refinancing activity began to ebb with the rise in mortgage rates in recent weeks. A contact also noted that tighter secondary markets for mortgages
and credit standards along with lower home values have resulted in a much higher rejection rate of applications during the recent refi boom relative to a year ago. Downward pressure on prices and rents continued. One contact expressed the belief that the processing period for new foreclosures will likely run its course by year’s end, potentially easing that influence on inventories and prices. Nonresidential development and construction also weakened, with the exception of the healthcare sector. Contacts expected a very limited impact on construction from the recent fiscal stimulus bill for 2009, with a small boost to activity more likely in 2010 or 2011. Several contacts reported that commercial property values were declining along with rents as vacancy rates continued to rise, particularly in the retail sector. The availability and cost of financing remained a concern for residential and commercial developers, with additional cancellations and project delays reported.

**Manufacturing.** Manufacturing activity in the District continued to decline from the previous reporting period. Production and new orders were reported to have weakened further, and several manufacturers reported aggressively liquidating inventories purchased during last year's surge in material prices. Activity in the domestic steel industry improved slightly from a very weak December. A contact noted that service center inventories remain low, suggesting a quick turnaround for the industry when demand improves. Other metals-related industries noted weakening conditions. Mining activity was reported to have declined substantially, with a subsequent drop in the demand for heavy mining equipment also reported. The demand for heavy trucks and construction machinery, construction materials, and housing-related items such as appliances declined further. A contact noted that more overseas customers were not accepting delivery on shipments of heavy machinery, as financing in other countries for purchases was falling through. Several contacts expressed concern over a further weakened state of the auto industry. Inventories of light vehicles remained elevated, and sales in February were likely to be much lower than even January’s depressed pace. In contrast, contacts reported strength in demand for large agriculture equipment and pharmaceutical products.

**Banking/finance.** Credit conditions remained tight. Bank lending decreased from the previous reporting period and loan performance deteriorated as business bankruptcies in the District increased. Contacts in the banking industry reported increases in the fees and pricing for credit to riskier applicants, but stressed that credit remains available for well-qualified borrowers. The auto and commercial real estate sectors were noted to be of particular risk. Several contacts in the financial sector reported that high volatility and illiquidity in some asset markets continued to limit investment activity by banks, hedge funds and private equity firms. Strains on bank balance sheets
continued to be seen by contacts as limiting credit availability. The demand for liquidity remained high, but borrowing spreads decreased as elevated counterparty risk concerns eased some from the previous reporting period. Conditions in the commercial paper and corporate bond markets were noted to have improved significantly. In contrast, illiquidity in the auction-rate securities market and the secondary market for jumbo residential mortgages were raised as concerns.

**Prices/costs.** Contacts reported closely monitoring margins given ongoing declines in the demand for their goods and services. In general, material prices declined in January and February. There were a few reports of firms continuing to try to pass on last year's higher material prices; but, for the most part, the input price declines that were showing through leaned toward price reductions. Contacts in the construction industry cited expected increases in the price of cement as a concern. Gasoline prices also increased from the previous reporting period, but contacts noted that pass-through had been minimal and that fuel surcharges from the previous year had disappeared in recent weeks. The low cost of fuel was also reported to be showing through to other energy prices, including electricity. Heavy discounting continued in retail trade, where margins remained tight. Wage pressures also continued to tilt toward the downside, with several contacts alternatively noting pay freezes or reductions in non-wage compensation.

**Agriculture.** Most agricultural commodity prices fell since the previous reporting period. Crop prices moved down and were substantially lower than a year ago. Farmers continued to store more corn and soybeans than last year given the current lower prices. Farmland cash rents and input costs for crop production have not decreased as much as crop prices, so farmers faced added pressures in making plans for 2009. Some farms may incur significant losses, even at cash prices above the triggers of the government safety net. Spring planting intentions remained somewhat uncertain, though shifts toward soybeans and away from corn are likely to occur. Hog prices increased, but dairy and cattle prices declined from the previous reporting period. Even with recent below normal precipitation in some areas, almost the entire District had plentiful levels of ground water heading into the spring.
Summary

The economy of the Eighth District weakened further since our previous report. Retail and auto sales were lower in January and early February compared with a year ago. Manufacturing activity continued to decrease and activity in the services sector declined in most District areas. Residential real estate markets continue to be weak. Reports from commercial and industrial real estate market contacts were mixed. Overall lending at a sample of large District banks decreased moderately.

Consumer Spending

Contacts reported that retail sales in January and early February were down, on average, over year-earlier levels. About 63 percent of the retailers saw decreases in sales, while 33 percent saw increases. About 47 percent of the respondents noted that sales levels met their expectations, 37 percent reported that sales were below what they had anticipated, and 16 percent reported sales above expectations. Apparel items were strong sellers, while furniture moved more slowly. About 58 percent of the contacts noted that inventories were at desired levels, while 29 percent reported that inventories were too high, and 13 percent reported that inventories were too low. The sales outlook among the retailers for March and April is pessimistic. About 72 percent of the retailers expect sales to decrease over 2008 levels, while 28 percent expect sales to increase.

Car dealers reported that, compared with last year, sales in January and early February were down, on average. About 74 percent of the car dealers surveyed reported a decrease in sales, while 9 percent reported the opposite. About 35 percent of the car dealers noted that used car sales had increased relative to new car sales. About 48 percent reported more rejections of finance applications. About 42 percent of the car dealers surveyed reported that their inventories were too high (mostly for new cars), while 17 percent reported that their inventories were too low (mostly for used or low-end cars). About 62 percent of the car dealers expect decreased sales over 2008 levels for March and April, but 24 percent expect sales to increase. The remaining contacts expect sales to be similar to last year.
Manufacturing and Other Business Activity

Manufacturing activity continued to decline since our previous survey. Several manufacturers reported plans to reduce operations and lay off workers, while a smaller number of contacts reported plans to open plants and expand operations. Firms in the auto parts, rubber products, machinery products, household appliance products, electrical equipment, and wood product manufacturing industries reported plans to lay off workers because of weak product demand. Firms in steel product, primary metal, and heavy metal manufacturing also reported job losses and temporary plant shutdowns. Several auto parts and auto manufacturers offered early retirement buyouts to reduce their labor forces. In contrast, firms in the heavy machinery and household appliance manufacturing industries reported plans to open new facilities, and contacts in the plastics/rubber products and airplane manufacturing industries reported plans to expand existing facilities and operations.

The District's services sector continued to decline in most areas since our previous report. Firms in the leisure/hospitality, business support, education, and transportation services industries cut jobs. In addition, firms in medical services, transportation services, business support services, and information services reduced payroll expenses through pay cuts, required time off without pay, or demotions. In contrast, two contacts in the financial services industry reported plans to expand operations and hire additional workers. A firm in business support services also hired new workers to handle increased demand.

Real Estate and Construction

Home sales remained weak throughout the Eighth District. Compared with the same period in 2008, January 2009 home sales were down 14 percent in St. Louis, 23 percent in Little Rock, 34 percent in Louisville, and 39 percent in Memphis. Residential construction also remained weak throughout the District. December 2008 year-to-date single-family housing permits fell in nearly all District metro areas compared with the same period in 2007. Permits declined 35 percent in Little Rock, 42 percent in Louisville, 43 percent in St. Louis, and 59 percent in Memphis.
Commercial real estate market conditions were mixed throughout the District while commercial construction markets were generally slow. Compared with third-quarter 2008, fourth-quarter 2008 industrial vacancy rates decreased in Little Rock and Louisville but increased in Memphis and St. Louis. During the same period, suburban office vacancy rates decreased in Louisville and Memphis but increased in Little Rock and St. Louis. Downtown office vacancy rates decreased in Memphis but increased in St. Louis, Louisville, and Little Rock. A contact in northeast Arkansas reported that overall commercial construction is at a standstill. A commercial construction contact in Louisville reported fewer requests for new project bids as business owners are holding back in the uncertain environment.

**Banking and Finance**

A survey of senior loan officers at a sample of large District banks showed a moderate decrease in overall lending activity during the fourth quarter of 2008. During this period, credit standards for commercial and industrial loans tightened somewhat, while demand for these loans was moderately weaker. Credit standards for commercial real estate loans were tightened somewhat, while demand for these loans was moderately weaker. Meanwhile, credit standards for consumer loans ranged from unchanged to tightened somewhat, while demand ranged from moderately weaker to moderately stronger. Credit standards for residential mortgage loans ranged from unchanged to tightened somewhat, while demand for these loans ranged from about the same to moderately weaker.

**Agriculture and Natural Resources**

Total production of corn, sorghum, and cotton decreased from 2007 to 2008, while total production of soybeans, winter wheat, and tobacco increased, and total production of rice did not change. The prices of winter wheat, rice, and tobacco increased from 2007 to 2008 in all District states that produced them, while the prices of corn, sorghum, and cotton were mixed among states, and the price of soybeans was down in most states. The total value of field crops in District states fell by 1 percent from 2007 to 2008.
The broad-based economic downturn continued in the Ninth District. Activity weakened since the last report in consumer spending, tourism, services, construction and real estate, manufacturing, energy, mining and agriculture. Labor markets continued to deteriorate as a number of companies announced layoffs. Overall wage increases remained modest. Prices remained relatively stable since the last report; many prices were lower compared with a year ago.

**Consumer Spending and Tourism**

Overall retail sales were lower than a year ago. A major Minneapolis-based retailer reported that same-store sales in January were down 3.3 percent compared with a year earlier. A Minnesota-based furniture retailer reported that recent sales continued to lag year-earlier levels. An outdoor goods retailer in Minnesota reported that recent sales were flat compared with last year. Preliminary January sales reports at a Montana mall improved from December levels, according to the manager. A representative of an auto dealers association in North Dakota reported slower activity than last year. Auto dealers in southwestern Montana reported some improvements in sales during January after fairly dismal sales during the last part of 2008. On a positive note, a new anchor department store and a fitness center have helped traffic increase 20 percent in January at a Minneapolis area mall.

Tourism activity was slower than last winter. A ski resort in Montana noted that lodging revenue was down 15 percent compared with a year earlier. A Minnesota ski resort reported that sales were down 15 percent through mid-February, but pre-sales for March and early April have recently picked up. In contrast, good snow conditions have helped buoy tourism activity in western South Dakota.

**Services**

Services sector activity decreased overall since the last report. Contacts from the legal sector noted a downturn in business. Architects reported continued weak demand. Several media services companies cut back on content. Hospitals reported weakening demand for elective services, but an uptick in emergency services, as consumers are shifting from clinics. However, some information technology firms noted solid demand from companies investing in cost-reduction projects. Several appraisers and mortgage companies noted a big increase in refinance activity.
Construction and Real Estate

Commercial construction activity decreased. January commercial permits decreased in Sioux Falls, S.D. A commercial developer in Fargo, N.D., said activity there had decreased, but the area was faring better than in many others. A Minneapolis commercial real estate firm forecast flat office and industrial construction in 2009 from the previous year. However, developers were optimistic about the impact of the federal fiscal stimulus package. Residential construction decreased slightly. The number of permitted units in Minneapolis-St. Paul was down 7 percent in January from the previous year. The number of January residential permits declined in Sioux Falls.

The commercial real estate market weakened. A Minneapolis-St. Paul commercial real estate firm noted that vacancy has increased for the office, industrial and retail segments; it forecast a decline in lease rates, as it expects newly completed projects to outpace absorption. In Sioux Falls, a commercial real estate agent said the market has softened. Residential real estate remained slow, with possible signs of nearing bottom. January closed sales in Minneapolis-St. Paul increased 2 percent over the previous year; prices were down more than 24 percent, as more than half of sales were due to lender-mediated foreclosure or short-sale activity. A real estate agent in Fargo described the market there as slower than in recent years, but still brisk overall. A bank director in western Montana said mid-priced homes were still selling well, but luxury homes were taking longer to sell or were pulled from the market.

Manufacturing

Manufacturing activity decreased since the last report. A January survey of purchasing managers by Creighton University (Omaha, Neb.) indicated that activity significantly decreased in Minnesota and South Dakota, and slightly decreased in North Dakota. Several manufacturers decreased production since the last report. A Minnesota window maker announced production cuts, a fiberglass producer plans to close a plant and a metal cab maker reduced production. In South Dakota, a respirator plant temporarily shut down and a computer component producer plans to shut down.

Energy and Mining

Activity in the energy and mining sectors fell since the last report. Mid-February oil and gas exploration declined significantly from early January. Several ethanol plants went up
for auction. A Montana metals mine recently reduced production. A large cooperative energy utility noted decreased demand after adjusting for weather patterns.

**Agriculture**

Agricultural conditions deteriorated since the last report. Results of the Minneapolis Fed’s fourth-quarter (January 2009) survey of agricultural credit conditions indicated that lenders expect overall agricultural income and spending to decrease significantly in the first quarter of 2009. “The agriculture economy is looking a little tough due to lower prices in both the livestock and grain markets,” commented a Montana respondent to the survey. Meanwhile, milk prices dropped significantly since last December.

**Employment, Wages and Prices**

Labor markets continued to deteriorate, with a number of companies announcing layoffs. After cutting 2,400 jobs companywide in the fourth quarter, a Minnesota-based manufacturer indicated that more cuts are likely in 2009. Similarly, a Minnesota-based telecommunications firm that laid off 350 employees in October said more layoffs were to come. Also in Minnesota, a window maker plans to eliminate 50 positions and temporarily lay off about 400 workers, a cleaning and sanitizing products maker is cutting 200 jobs and a financial services company is cutting 100 jobs. In addition, a snowmobile and utility vehicle manufacturer announced plans to lay off more than 110 employees, while a nearby competitor will lay off 100 employees. Falling oil prices led to about 150 layoffs in western North Dakota. A company that makes processing equipment for the semiconductor industry recently announced plans to lay off 200 employees in Montana after cutting 100 workers in November. A job service center in Montana reported seeing many more people per day in January than in the past, and job seekers were less selective about job openings.

Overall wage increases remained modest, and examples of pay cuts or freezes were noted. Some companies that announced layoffs reported that executives and, in some cases, other employees received cuts in their compensation packages. State workers in South Dakota recently accepted a freeze in pay levels.

Prices remained relatively stable since the last report; many prices were lower compared with a year ago. Minnesota gasoline prices in mid-February were about 35 cents higher than at the end of December, but were about $1 lower than a year ago. Metal prices remained much lower than a year ago after decreasing sharply last fall.
Economic conditions in the Tenth District continued to deteriorate in January and early February. Consumers retrenched further, shying away from durable goods and curtailing restaurant dining and travel. Manufacturing activity and capital spending weakened further, and the decline in real estate activity intensified as construction weakened further and home prices maintained their downward trend. Energy activity dampened significantly as drilling waned and rig counts hit five-year lows. Farm incomes declined with crop and livestock prices. Lack of demand and wide availability put downward pressure on prices of raw materials and finished goods, but wages and salaries remained steady.

**Consumer Spending.** Retail sales were lower in January and early February, and a plurality of retailers reported lower sales than expected. Sales declines were broad-based, but sales of durables such as home furnishings, lawn and garden equipment, and appliances were especially weak. Expectations were for continued sluggishness in retail sales in the near term. Mall traffic was down, as were sales in most stores. Most auto dealers reported sales declines and expected sales to retrench further over the next few months. Used cars were selling well, while sales of new cars and large vehicles were down significantly. Auto dealers continued to note tight credit conditions. Hotels unanimously reported lower occupancy rates over the previous month and airline traffic was slower in many cities; however, some recreational venues such as zoos and botanical gardens saw modest improvement, suggesting that consumers may be keeping their entertainment dollars local. Restaurant sales were down across the board.

**Manufacturing and Other Business Activity.** Manufacturing and other business activity contracted further in January and February with some reports of businesses closing or consolidating. Finished goods inventories shrank significantly as factories cut production.
Shipments and new orders slowed since the last survey period, but a few firms reported stable or improved sales. Export orders eased slightly and were expected to slow further. Many firms have put capital spending on hold due to weak demand and difficulty obtaining financing. Both the number of workers and weekly hours were lower in most manufacturing enterprises. High-technology services was a bright spot in the District economy in January and early February. About half of contacts reported increased activity. The transportation sector continued to weaken. Most of the sustained activity was in the transport of staple products, especially food, and goods targeted to discount retailers.

**Real Estate and Construction.** All surveyed Realtors reported declines in home prices in January and early February, and most noted declines in sales, especially for higher-end homes. Modest improvements in sales were expected in the next three months, but Realtors expected prices to continue on their downward spiral. Although bargain prices and lower interest rates spurred some buyers to the real estate market, other potential homebuyers were waiting on the sidelines, hoping for additional government incentives. Mortgage lending was up, due largely to refinancing. Commercial construction continued to weaken significantly in January and early February, and industry professionals were pessimistic about the future. Vacancy rates were higher and absorption rates and rents were lower. Credit to commercial construction enterprises remained tight.

**Banking.** Bankers reported a decline in loan demand, an increase in deposits, and a modestly improved outlook for loan quality since the last survey. Demand fell for commercial and industrial loans, commercial real estate loans, and consumer installment loans. Banks continued to report tighter credit standards on commercial and industrial loans, commercial real estate loans, and consumer installment loans. Standards on residential real estate loans were
generally unchanged. Assessments of current loan quality were similar to the last survey, but expectations for future loan quality improved modestly. Most respondents reported increases in deposits.

**Energy.** Drilling activity continued its downward trend in January and early February in the face of declining prices. All contacts expected drilling activity to fall further in the future, despite expectations of higher prices for crude oil. Contacts were split on expectations of future natural gas prices. The District rig count was down dramatically, reaching its lowest level since late 2003.

**Agriculture.** Agricultural conditions varied with precipitation levels in late January and February. The winter wheat crop was reported in good condition throughout Nebraska and Kansas due to adequate moisture while crop conditions deteriorated in dry areas of Oklahoma. Lack of moisture also eroded pasture conditions and limited winter forage for livestock. Farm incomes declined with lower crop and livestock prices. Loan renewals and extensions increased as some farmers decided to wait for crop prices to rebound before marketing remaining inventories. District contacts reported softer loan demand for real estate and capital purchases but expected an increase in operating loans as input costs remained elevated. Farmland values declined amid weaker farm incomes and softer demand from off-farm investors.

**Wages and Prices.** Hiring retrenched in January and early February as businesses struggled to contain costs and respond to faltering demand in the slowing economy. Nevertheless, wages and salaries held steady. Prices continued to ease. Raw materials were widely available for construction and manufacturing enterprises, which put downward pressure on input prices, especially for lumber. Manufacturers reported reduced prices for finished goods, and retailers largely reported lower prices as well.
The Eleventh District economy weakened further in January and the first half of February. Falling demand was reported across a broad range of industries, with manufacturers and energy respondents noting the largest declines. Outlooks remain pessimistic, and many contacts expect little improvement through year-end.

**Prices** Contacts in most industries said selling prices were down. One major exception was the retail sector where prices were recently holding steady following the winter clearance season. Respondents in the oil services industry said prices were falling rapidly. Within manufacturing there were scattered reports of “as-needed” orders, as customers were wary of holding inventory that was declining in value. Petrochemical prices experienced significant price declines in January and February as demand and energy feedstock prices fell. Fabricated metals producers said prices are “falling like a rock.” Across industries, input costs had come down and lower commodity prices appeared to be flowing through to longer term supply contracts. Fuel surcharges continue to be reduced but have not completely disappeared.

From January through mid February, the price of West Texas Intermediate crude oil fluctuated between $48 and $34 per barrel. An inventory improvement put the price near $40 as the survey period ended in the third week of February. While retail diesel prices fell by about 11 cents per gallon, gasoline prices are up about 25 cents since early this year as demand has strengthened to year-ago levels. Natural gas prices fell to a six-year low of near $4.00.

**Labor Market** Labor markets remained weak, and payroll reductions were prevalent across industries, with the most significant layoffs noted for manufacturers and energy services firms. Several respondents were trying to avoid cutting staff by trimming hours and salaries instead. There were some reports that firms were considering pay freezes for top management. Staffing firms noted pressure from clients to lower pay rates.

**Manufacturing** Most manufacturers reported declines in orders and production since the last survey, and outlooks remain pessimistic.

Producers of construction-related manufacturing products said orders continued to fall over the past six weeks. More than one respondent expressed concern about whether their firm would make it through the current downturn, and several noted competitors or customers had gone out of business or filed for Chapter 11. Bookings for residential building materials were down sharply and contacts reported layoffs and plant closings. Metals producers that supply to the nonresidential construction sector said orders were unexpectedly low as commercial activity weakened, the only exception being demand tied to institutional/public works construction. Outlooks were grim among construction-related respondents, with most not expecting any improvement this year.

Eleventh District respondents in high-tech manufacturing reported continued declines in production and orders. Reductions in demand were widespread across most products and areas of the world. Layoffs and temporary plant shutdowns have increased since the last survey. Most contacts said they were aggressively cutting inventories to very lean levels. One semiconductor respondent expects demand to fall through the first quarter as industries that use
semiconductors in production reduce inventories. While most contacts noted the outlook remains particularly uncertain, most expect some improvement by year-end.

Demand for paper products was mixed. After falling late last year, orders of corrugated boxes held mostly steady over the past six weeks, although demand is below year-ago levels. Manufacturers of printing paper said demand softened further during the survey period, after accounting for a normal seasonal slowdown. Inventories were reportedly bloated, and some contacts were reducing payrolls.

Weak orders for autos and aircraft continue to hamper the transportation manufacturing sector, yet sales of some specialized products rose. Contacts in the food processing industry said sales growth of food products has flattened out, but contacts are satisfied with current levels and expect growth to remain steady in coming months. Most respondents noted stable prices.

Refiners’ margins slowly improved from very low levels in December. Contacts said the last couple of weeks have been quite good, although operating rates were relatively weak and fell through the survey period. Although petrochemical prices continue to fall significantly, demand improved slightly in January as customers who had worked down their inventories began to re-order. Still, contacts said orders were on an “as-needed” basis only. February has not shown signs of continued demand improvement.

Retail Sales  Retail activity picked up slightly since the last survey. Contacts were mixed in their explanations for the uptick, but most suggested that discounts and clearance prices in January lured consumers. Consumer discretionary spending remained weak overall, but there were some reports of gains in department store revenues and home products sales. Contacts said Texas sales were just slightly outperforming the national average.

Auto sales held steady at low levels in recent weeks and contacts are hopeful this signals the bottom. With many incentives already in place prices are not expected to go any lower. Respondents expect the next 15 months to be tough and expect several franchise dealers to go out of business in 2009.

Services  Staffing firms said business was worse than anticipated with orders down sharply for both direct placements and contract work. Demand was dismal for workers across a broad range of occupations, the only notable exceptions being sales professionals and workers trained in mortgage refinancing or collections. Pricing remains competitive and some firms let go of market share to maintain margins. Accounting firms reported steady demand—mostly concentrated in tax and audit-related services. Legal activity weakened since the last survey. The majority of business continues to be concentrated in litigation and bankruptcy, while corporate, real estate, and transactional demand remain weak. Bankruptcy-related business has increased, but not to the levels legal contacts had expected. The general outlook among service contacts was more pessimistic than reported in the last survey.

Eleventh District-based airlines report demand continues to fall and fares are following suit. International passenger traffic is down substantially. Most airlines were re-assessing business strategies. Respondents in intermodal transportation said cargo volume continued to fall since the last survey, a result of the decline in demand for imports and the decrease in exports. Large parcel express air and ground cargos continued to be negatively impacted by poor U.S. retail sales. On a brighter note, railroad shipments rebounded slightly in recent weeks, although contacts still expect a difficult year ahead.
Financial Services  Most Eleventh District financial institutions characterized loan demand as “disappointing.” Several respondents said that while capital is more readily available for lending, loan demand has fallen and borrowers that are coming forward are less credit worthy or unwilling to meet more stringent terms. Lenders continued to set interest rate floors on the prime rate or price off LIBOR on some loans. Commercial real estate lending has “dropped off a cliff” over the past few months, and large loans that are maturing cannot get renewed with the same financial terms. Contacts said the “hyper-focus” on the value of commercial properties is creating underwriting problems for even healthy institutions. Lenders said overall credit standards remain tight and noted somewhat tighter scrutiny for consumer loans recently. Deposits were stable.

Construction and Real Estate  Housing conditions in the Eleventh District remain weak, but there were scattered signs of improvement since the last survey. After a “horrible” fourth quarter wrought with cancellations and a lack of sales, homebuilders reported buyer traffic picked up in January and has been sustained in February. Low interest rates are helping pull potential buyers off the sidelines say contacts. New home sales picked up since the last survey, although they are “nowhere near” the level seen in prior years. Several contacts noted that despite encouraging signs, several smaller builders are expected to exit the market in the coming months. Margins are squeezed, cash flow is extremely tight, and financing is difficult—even for legitimate contracts. Existing home sales continued to decline and median prices edged lower, although contacts say the level of inventory is low and should continue to keep price declines minimal compared with the national average. Several respondents expressed hope that the housing stimulus package would give the market more time to heal, but some noted parts of the plan were not enough to spur sales.

Commercial real estate transactions remain minimal, yet some contacts noted that “price rediscovery” of real estate assets was starting to happen. Still, most contacts said uncertainty about the size of the write-downs was keeping lenders and sellers on the sidelines. Office leasing activity remained slow but “ok,” according to contacts. The outlook for commercial real estate remains uncertain given that many loans are coming due amid the difficult financing environment. Contacts expect nonresidential construction to decline in 2009.

Energy  Demand for oil services and equipment is shrinking rapidly as the U.S. rig count follows energy prices down. The domestic rig count has lost an unprecedented 697 rigs since the September peak and 382 since year-end. Texas accounted for 57 percent of the decline this year. Initially, domestic drilling cuts were concentrated in conventional, vertical drilling, but more recently the decline is spreading to horizontal, unconventional natural gas drilling. Respondents said demand for some durable equipment, such as pumps, drill pipe and bits, is down by 90 percent or more—as these parts can be cannibalized from rigs taken out of service.

Agriculture  The dry spell continues to grip much of the District. Wheat and oat crops are suffering from lack of moisture. Grazing conditions are poor as well, and most ranchers reported the supplemental feeding of livestock. Hay stocks are low and feed costs remain high, forcing some ranchers to cull their herds. District dairy producers report weak conditions. A stronger dollar and weak export demand led to declines in milk prices.
TWELFTH DISTRICT–SAN FRANCISCO

Summary

Economic activity in the Twelfth District slowed further during the survey period of January through late February. Upward price pressures continued to ease in general along with the prices of energy and other commodities, and upward wage pressures were virtually nonexistent. Retail sales remained very sluggish with the exception of necessities such as basic groceries, and demand weakened further for service providers. District manufacturing activity continued to decline on net. Demand weakened for agricultural producers and fell further for oil extractors. District housing markets remained moribund, and demand for commercial real estate continued to fall. Contacts from financial institutions reported further weakening in loan demand and continued tight credit conditions.

Wages and Prices

Upward pressures on prices eased further during the survey period. Declining demand reduced sellers’ pricing power in many sectors, and price discounts deepened for assorted retail items. Prices declined further for energy and many commodities, including various construction materials and food products. Gasoline prices rose but remained well below the highs reached last year.

Upward wage pressures remained modest to nonexistent on net. Hiring freezes and restricted work schedules have become commonplace, and unemployment rose significantly throughout the District. Compensation increases were very limited in general: many employers have frozen or cut wages, eliminated incentive pay, or reduced benefit costs, for example through the elimination of 401(k) matching programs. Reports indicate that some companies that have not yet reduced workforces or cut compensation costs plan to do so soon.
Retail Trade and Services

Retail sales remained anemic. Consumers continued to shift away from discretionary spending and focus on necessities, reducing their overall spending and causing somewhat better performance for discount chains compared with traditional department stores. Many retailers saw double-digit sales declines relative to 12 months earlier, although contacts in the grocery industry reported that sales have grown in recent months. Demand remained especially weak for furniture, appliances, and electronic items. New automobile sales, both domestic and foreign, remained feeble, but sales and prices stayed relatively firm for used vehicles.

Demand for services continued to decline since the last survey period. Contacts in the restaurant and food services industry noted sharp sales declines accompanied by growing layoffs and closures. Providers of health-care services saw further drops in patient volumes, attributed largely to postponement of elective procedures and cutbacks in government-funded medical programs. Demand weakened significantly for providers of professional services such as accounting, business consulting, and legal services, with ongoing layoffs noted. Travel activity in the District fell further, and airlines responded by reducing passenger capacity. In Hawaii, sharp ongoing declines in visitor arrivals caused further layoffs at hotels and resorts, and contacts in Southern California reported growing cancellations of corporate travel commitments.

Manufacturing

District manufacturing activity languished during the survey period. Producers of wood products, transportation equipment, and construction equipment saw further declines in demand. New orders and sales of semiconductors and other information technology products continued to fall, causing layoffs and further reductions in capacity utilization for many firms. Contacts in the metal fabrication industry reported very weak demand and capacity utilization rates in the range
of 25 to 50 percent. Aerospace manufacturers continued to produce commercial aircraft at a brisk clip, but reductions in airline capacity have weakened the outlook for new orders going forward, and orders for small corporate jets have dropped significantly of late. Food manufacturers remained a bright spot, seeing strong demand overall as growing sales to grocery stores more than offset declining sales to restaurants. Several contacts noted that an inability to raise sufficient financial capital has been hampering current operations.

**Agriculture and Resource-related Industries**

Demand slipped somewhat for agricultural producers and weakened further for oil extractors. The pace of sales slowed for an assortment of agricultural products, notably livestock, dairy, and wheat. Agricultural input costs, particularly for fuel, transportation services, and fertilizer, reportedly have stabilized at levels well below the highs established last year. However, California farmers faced supply constraints and higher prices for water, and they expect supply to tighten further as the growing season proceeds. For oil extractors, ongoing declines in global demand caused further reductions in sales and rising inventories.

**Real Estate and Construction**

Activity in the District’s housing markets remained mired at very low levels, and considerable demand declines were reported for commercial real estate. The pace of home sales stayed very slow in most areas, despite some pickup in recent months as price declines have increased affordability, and construction of new homes was limited. Conditions in the commercial office market deteriorated noticeably, as leasing activity slowed further and vacancy rates continued to rise. Contacts reported that restricted credit availability has held down construction activity in both sectors of late. Construction projects funded by state and local governments fell further during the survey period as a result of budgetary constraints.
Financial Institutions

District banking contacts reported that loan demand continued to weaken and credit conditions remained tight. Many businesses have scaled back their capital investment plans, causing demand for commercial and industrial loans to fall further, and the market for commercial and residential real estate loans continued to wane. Declining asset values and rising loan losses caused banks and other financial institutions, such as money management firms, to scale back activity and lay off significant numbers of employees. Credit quality continued to deteriorate, as weakness in corporate and household borrowers’ balance sheets and income statements deepened, and bank lending standards remained stringent on net.