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SUMMARY

Reports from the twelve Federal Reserve Districts suggest that economic activity continued to expand moderately from November through December. Conditions were said to be improving in the Boston, New York, Philadelphia, and Richmond Districts. Activity increased modestly to moderately in the Cleveland, Atlanta, Chicago, St. Louis, Kansas City, and Dallas Districts. The economy of the Minneapolis District “continued its moderate recovery,” while that of the San Francisco District “firmed further” in the reporting period leading up to the close of 2010. Conditions were generally said to be better in Districts’ manufacturing, retail, and nonfinancial services sectors than in financial services or real estate.

Contacts in the manufacturing sector in all Districts reported that activity continued to recover, with the Richmond and Chicago Districts citing especially solid gains in orders. However, the Boston, Atlanta, and Dallas Districts noted that business remained weak for manufacturers selling into the construction sector. Retailers in all Districts indicated that sales appeared to be higher in this holiday season than in 2009 and, in some cases, better than expectations. Nonfinancial service-sector contacts in the Boston, New York, Philadelphia, Richmond, Chicago, St. Louis, Minneapolis, Kansas City, Dallas, and San Francisco Districts cited demand increases ranging from slight to “relatively strong.” Transportation services were more mixed, with the Cleveland, Atlanta, and Kansas City Districts noting stable to slowing shipping volumes. Financial conditions were mixed across the Districts reporting on it, with overall loan demand slowly improving in Philadelphia and Richmond and weaker in St. Louis and Dallas. The Atlanta, Minneapolis, Kansas City, Dallas, and San Francisco Districts cited increased activity in the energy sector, while energy production in the Cleveland District was stable.

Residential real estate markets remained weak across all Districts. Commercial construction was described as subdued or slow, while commercial leasing activity reportedly increased in the Richmond, Chicago, Minneapolis, and Kansas City Districts.

1 Prepared at the Federal Reserve Bank of Boston and based on information collected on or before January 3, 2011. This document summarizes comments received from business and other contacts outside the Federal Reserve and is not a commentary on the views of Federal Reserve officials.
Most District reports cited comments by both retailers and manufacturers that costs were rising, but indicated that competitive pressures had led to only modest pass-through into final prices. Labor markets appeared to be firming somewhat in most Districts, as some modest hiring beyond replacement was said to have occurred and/or was planned in a variety of sectors. At the same time, however, upward pressure on wages was reportedly very limited.

Most Districts indicated that business contacts were positive about the outlook, although still generally cautious. The Dallas District noted modest increases in optimism and positive outlooks across a range of sectors, Chicago stated that contacts were cautiously optimistic about the 2011 outlook, and New York cited widespread optimism about the near-term outlook; The St. Louis, Minneapolis, Kansas City, and San Francisco Districts all pointed to planned increases in hiring by their contacts as evidence of expected strengthening in business activity in 2011. Contacts in the Philadelphia District foresaw “improving economic conditions in 2011, but … not strong growth.”

**Manufacturing**

The manufacturing sector continued to recover across all Districts. Contacts in the Richmond, Chicago, and St. Louis Districts identified a strong flow of new orders. Respondents in the Chicago District pointed to pent-up demand for both light and heavy motor vehicles, attributed to an aging fleet, as a key driver of activity in the manufacturing sector. The Cleveland District described orders as above expectations and respondents in the New York District noted that orders had picked up since the prior report. Overall, demand was generally characterized as stable and steady, and no District made mention of lingering fears of a double-dip recession, in contrast to the summer reporting periods. Capacity utilization continued to trend higher and is approaching normal rates for some contacts in the Cleveland and San Francisco Districts, while production in high-tech manufacturing was reportedly at high capacity in Dallas; some manufacturers in the St. Louis and Minneapolis Districts said they have or will soon expand capacity. Production levels increased in the Cleveland, Atlanta, Chicago, and Kansas City Districts. On the negative side, the Philadelphia District characterized the flow of new orders as "erratic,"
while the Boston, Atlanta, and Dallas Districts identified construction-related manufacturers as continuing to show considerable weakness, and makers of wood products in the St. Louis and San Francisco Districts reported very soft demand.

The Boston, Cleveland, and San Francisco Districts reported concerns about input prices, particularly of commodities; manufacturers in the Boston, Cleveland, and Richmond Districts indicated they had experienced lengthening lead times, shortages, or other difficulty obtaining supplies of some inputs. Only St. Louis mentioned firms with substantial investment plans for 2011. Boston, Cleveland, Chicago, St. Louis, and Kansas City reported that some factories had plans to increase employment, although these hiring plans were typically characterized as modest. The Philadelphia, Cleveland, Chicago, Kansas City, Dallas, and San Francisco Districts described the 2011 manufacturing outlook as optimistic.

**Consumer Spending and Tourism**

Retail spending showed improvement across all Districts, with most retailers reporting sales growth consistent with or ahead of plan for the recent 2010 holiday season. Boston, Richmond, Atlanta, Chicago, and Kansas City observed consumers positively reacting to promotions and discounting, although Philadelphia and San Francisco reported that retailers relied less heavily on discounting. Inclement weather, including the late December blizzard, had some impact on sales in the New York and Philadelphia Districts. New York, Cleveland, and Chicago cited increased consumer confidence.

Automobile sales were either steady or up in eight Districts during the reporting period, while New York stated that auto sales were “mixed but generally at favorable levels” and Kansas City noted limited auto sales but expected future improvement from additional incentives. Philadelphia, Cleveland, and Dallas indicated that vehicle inventories were at appropriate levels for the current sales rate. Cleveland reported an increase in leasing activity, while the effect of rising gasoline prices on sales of less fuel-efficient models was a concern cited by some dealers in Philadelphia.
Tourism was characterized as positive or improved in the Richmond, Atlanta, Minneapolis, Kansas City, and San Francisco Districts, while New York described tourist activity as brisk. Contacts from the Richmond, Kansas City, and Minneapolis Districts observed a strong start to the winter ski season, although unfavorable weather conditions at the end of December led to deteriorating conditions for winter activities in some areas of the Minneapolis District. New York City's Broadway theaters reported increased attendance and revenue compared with the 2009 holiday season. Occupancy rose in the Atlanta and San Francisco Districts’ major hotel markets. Room rates continued to run ahead of comparable 2009 levels in the New York and the Kansas City Districts, although rates have fallen in Kansas City since the last survey. Atlanta and San Francisco noted rising business travel.

Nonfinancial Services

Activity was said to be steady to increasing among Districts reporting on nonfinancial services. Providers of information technology services saw increases in sales in the Kansas City and San Francisco Districts. Advertising and consulting contacts in the Boston District reported significant growth in demand. In the Dallas District, legal firms noted an uptick in demand for services, while accounting firms reported seasonal slowness. Reports from the healthcare sector were mixed; St. Louis and Minneapolis reported ongoing increases in demand for healthcare workers, while San Francisco indicated a slight weakening in demand for healthcare services and Richmond reported little change. Demand for staffing services remained on an upward trend, with increases reported by New York, Philadelphia, Richmond, and Chicago. In addition, an employment-agency contact in the New York District observed increased demand for employees in the legal and financial services sectors, while the Dallas District noted strong, steady demand for workers in the professional, technical, healthcare, and finance fields. Reports from the transportation services sector were mixed, with increased demand reported by trucking firms and airports in the Richmond District, and slower overall activity in the Kansas City District. Freight companies in the Cleveland District noted stable volumes over the past six weeks, and contacts in the Atlanta District reported moderating freight volumes after significant increases in earlier 2010 reporting periods.
Real Estate and Construction

Activity in residential real estate and new home construction remained slow across all Districts. A majority of the Districts, including Boston, New York, Cleveland, Atlanta, Chicago, Minneapolis, Dallas, and San Francisco characterized local housing markets as weak and sluggish with little change from the previous reporting period. Kansas City noted further weakening, while Richmond received reports of both flat activity and further declines. The St. Louis District saw additional declines in existing home sales, but also cited increased new home construction permits. All Districts attributed slumping activity to concerns about the pace of economic recovery, especially in employment, while the Philadelphia, Atlanta, and Chicago Districts mentioned difficulty obtaining credit as another constraint on demand. High levels of existing home inventories continued to damp the pace of new home construction in most Districts reporting on construction, although Boston, Richmond, Dallas, and San Francisco mentioned pick-ups in multifamily construction within their Districts. Home prices generally declined or held steady in the New York, Philadelphia, Cleveland, Richmond, Atlanta, Chicago, Kansas City, Minneapolis, and San Francisco Districts; the New York, Atlanta, Chicago, and San Francisco Districts mentioned distressed properties placing downward pressure on prices. Boston reported rising median home prices across most states in the District, but contacts attributed those increases to relatively higher sales of more expensive properties rather than a general upward movement in home prices. Outlooks for residential real estate in the coming year were mixed, with contacts in most Districts described as expecting continued weak conditions.

Commercial real estate markets displayed mixed results across the Districts again this reporting period, as leasing markets exhibited increasing signs of recovery and nonresidential construction remained weak. Leasing activity increased modestly in the Richmond, Chicago, Minneapolis, and Kansas City Districts and showed tentative improvement in the Dallas District. Vacancy rates, while quite high across the country, fell marginally in the Kansas City District and in New York City’s office market. Leasing market fundamentals held roughly steady in the Boston, Philadelphia, and San Francisco
Districts. Commercial construction activity was described as very limited across most Districts, with the bulk of new activity coming from projects related to healthcare, public infrastructure, and multifamily housing. Contacts in most Districts expected modest improvements in commercial leasing in 2011, although the outlook for construction was mixed and some Districts noted rising costs as a concern.

**Banking and Financial Services**

Reports on credit activity were mixed across Federal Reserve Districts. Overall, loan demand was reported as stable in San Francisco, mixed in New York, steady to slightly softer in Kansas City, weaker in St. Louis and Dallas, and slowly improving in Philadelphia and Richmond. Demand for consumer loans declined in the New York, Cleveland, St. Louis, Kansas City, and San Francisco Districts. By contrast, consumer lending increased in the Dallas District, and exceeded expectations in the Chicago District. Bankers in Philadelphia, Cleveland, and Richmond anticipate consumer lending to expand in 2011. Demand for commercial and industrial loans was flat in New York, Kansas City, and San Francisco. Lenders in the New York, Cleveland, Minneapolis, Kansas City, and San Francisco Districts noted a drop in residential mortgage refinancing owing to the recent rise in interest rates, whereas Richmond reported strong demand for home refinancing. The Cleveland and Richmond Districts observed a pick-up in auto lending. Demand for residential real estate loans eased in New York and Kansas City, remained weak in Cleveland and Dallas, but increased in the Richmond District. Real estate lending declined in the St. Louis District. Lending in the commercial mortgage category increased in New York, was unchanged in Kansas City, and was weak in Dallas, with the exception of multifamily. Most Districts reporting on credit quality described it as improving, while bankers in the Cleveland District said that quality remained stable or edged up slightly. Reports on credit standards were mixed in New York, while standards were said to have eased somewhat in Atlanta, remained restrictive in San Francisco, and held steady in Kansas City. Delinquency rates were flat or trending down in Cleveland, while delinquency rates in the New York District rose for commercial mortgages, decreased in the
consumer lending category, and remained unchanged for all other loans. Total deposits rose in the Cleveland and St. Louis Districts and were stable in the Kansas City District.

**Agriculture and Natural Resources**

Unfavorable weather conditions damped agricultural production in some areas. The Dallas District reported that drought negatively affected range conditions by adding to costs of feeding livestock, while Atlanta cited the challenges prolonged drought presented to fruit growers. The Kansas City District indicated that dry weather could affect winter wheat development. Large snow falls hampered some ranchers in the Minneapolis District. However, agricultural demand generally improved among reporting Districts, and output prices rose, especially for corn, soybeans, wheat, cattle, and cotton.

The Kansas City, Dallas, and San Francisco Districts reported increased drilling activity. Cleveland cited fairly stable oil production, while the Atlanta District experienced the highest level of oil production in more than six years during the fourth quarter of 2010. Prices for crude oil and natural gas either stayed steady or slightly increased in the Cleveland, Minneapolis, Kansas City, and Dallas Districts. Cleveland reported steady coal production and prices, while the St. Louis District saw coal production increase.

**Prices and Labor Markets**

Most District reports mentioned increasing prevalence of cost pressures but only modest pass-through into final prices because of competitive pressures. Philadelphia and San Francisco noted somewhat reduced discounting in the retail sector during the holiday selling season, while New York, Minneapolis, and Dallas indicated retail prices were stable, Richmond said retail price increases had slowed, and Chicago and Kansas City cited discounting or depressed retail margins. For both retailers and manufacturers, increases in selling prices, if occurring, were said to be selective. Specific markets or products identified as experiencing high or rising prices included various food products, steel and other metals, building materials, textiles, chemicals, and petroleum-related products. Many Districts mentioned concerns among business contacts that petroleum-related prices, already above year-earlier levels, will
continue rising in 2011. The Philadelphia and Kansas City reports indicated that manufacturing firms planned to attempt more price increases in 2011, while some manufacturers in the Boston District were uncertain their price increases would stick and the Chicago report projected only “limited and gradual” pass-through.

Labor markets in most Districts appear to be firming somewhat, but with virtually no upward pressure on wages. All District reports indicated that employment levels are rising in at least some sectors, generally by modest amounts; however, some employers in the New York, St. Louis, and Minneapolis Districts also mentioned job cuts. Staffing firms in the New York, Philadelphia, Cleveland, Richmond, Chicago, and Dallas Districts gave positive reports; Cleveland, Richmond, and Atlanta said some firms were raising work hours instead of or in addition to hiring. The Boston, New York, Atlanta, Chicago, St. Louis, Minneapolis, Kansas City, and San Francisco Districts indicated that business contacts planned to continue or increase their pace of hiring in 2011. Some employers in the Boston, Atlanta, and San Francisco Districts expressed concern about added costs for healthcare; the Boston, Cleveland, and Chicago Districts noted selected skill shortages in some sectors. Overall wage pressures remained subdued; the Philadelphia District reported “mostly steady wages,” Cleveland said “wage pressures are contained,” Chicago indicated “wage pressures remained moderate,” Minneapolis and Kansas City stated wage increases or wage pressure “remained subdued,” and the Dallas and San Francisco reports described wage pressures as “minimal” or “largely absent.”
Economic conditions continue to improve in the First District in the waning months of 2010. Most contacted retailers report year-over-year sales increases, manufacturers generally continue to see expansion, and advertising and consulting firms cite relatively strong growth. Respondents in these three sectors indicate employment is stable to rising, with more of the same planned for 2011. Commercial real estate markets are said to be stable, while residential real estate continues in the doldrums. Selected commodities are causing some price pressures, but contacts report only modest pass-through into sales prices to date. The outlook for 2011 is generally positive, albeit moderate.

Retail

The majority of contacted First District retailers report positive sales results for the months of November and December. Year-over-year comparable same-store sales are mostly increases ranging from the low single digits to the low double digits, with the exception of one contact who reports a drop in same-store sales but notes a recent positive turn. Several retailers indicate that consumers continue to react positively to promotions. Sales of apparel, sporting goods, cameras, and other gift items were strong leading up to Christmas. Respondents generally are pleased with early holiday shopping results.

Contacts report mixed inventory levels in comparison to plan. As for prices, retailers note cost increases for commodities, including cotton, rubber, and nuts. Several respondents observe price pressure in the industry, but have yet to experience it themselves. Some contacts have worked to lock in pricing through vendor contracts; a couple say that vendors may be absorbing price increases or working to cover increases through product reengineering to keep their selling prices steady. Retailers say that price increases passed on to consumers, if any, will be selective. Headcounts continue to increase in line with new store openings, although a few firms are taking measures to reduce redundancy and consolidate headcount to gain other efficiencies. One respondent is concerned that uncertain potential employer costs associated with healthcare reform may affect hiring. Capital spending is mixed, with several retailers reducing capital spending now that one-time expansion projects have been completed. Outlooks are generally cautiously optimistic, with most contacts forecasting a slow and steady improvement in 2011.

Manufacturing and Related Services

The majority of manufacturing firms surveyed continue to report relatively positive business conditions. The exceptions include one firm with exposure to the residential construction sector, whose business has been sluggish for an extended period, and a few others whose business tends to be a-cyclical. On the positive side, a small diversified manufacturer reports sales growth in the high single digits and notes that its revenues have returned to pre-recession levels. A company in the electronics business says that its sales growth in the fourth quarter was slightly ahead of expectations, but is likely to be somewhat inconsistent going forward due to uncertainty about future large contracts. In addition, sales at a semiconductor firm remain strong relative to 2009 and are on par with their strong results in third quarter 2010; a food products manufacturer also reports strong sales.
A number of contacted firms continue to try to reduce or limit their inventories to maintain lean operations. By contrast, a few other firms report trying to increase their inventories somewhat either to meet higher demand or to try to offset continued supply constraints or disruptions. Plastics are one intermediate input that remains difficult to obtain, and a semi-conductor manufacturer reports that components necessary for its production process remain in short supply. These supply constraints have yet to translate into higher input or output prices for the affected firms. Increases in commodity prices are the main source of price pressure amongst responding firms; the prices of precious metals continue to rise as do the prices of grains and sugars. The manufacturers affected by these higher input prices have tried to pass along some or all of their increased costs to consumers in the fourth quarter or they plan price increases in early 2011, but they are not certain the increases will stick. Overall, selling prices remain relatively stable at the majority of contacted manufacturers.

Manufacturers continue to report stable to slightly increasing employment. The firms that are hiring tend to be increasing their headcount in skilled positions and/or in production workers to meet increased demand; none are planning substantial increases. Firms’ capital expenditures are little changed from previous reports. Most contacted companies anticipate their capital spending in 2011 will be roughly in line with 2010. Those firms who have increased capital expenditures or plan to do so are directing the spending toward IT upgrades or increased plant capacity.

Manufacturing respondents have mixed, but generally positive outlooks for 2011. One firm reports being “very optimistic” about next year, while most are “cautiously optimistic.” In comparison, the firm that has been struggling recently said the outlook for the next three to six months is “lackluster.” Many contacted firms remain concerned about their health care costs going forward, and a few expect that the macroeconomic uncertainty will continue to weigh on their sales growth.

**Selected Business Services**

Advertising and consulting contacts in the First District report significant growth in demand during the fourth quarter of 2010, with increases in revenue ranging from 5 percent to 30 percent. Most contacts attribute the rise to pent-up demand across many sectors and industries, as clients have been restrained by economic conditions since 2008. Responding firms held their prices steady or increased them slightly in the fourth quarter; some are planning to raise prices about 5 percent in 2011. Changes in business costs vary, with some firms citing stable wages, some raising compensation, and one firm cutting costs by hiring lower wage-rate replacements for selected employees. All contacts plan to increase employment next year to meet recent and expected increases in demand, with net hiring of 5 percent to 20 percent. Some of them expect salaries to stay stable through 2011, while some expect modest increases.

Most contacts are highly optimistic about their near-term performance and throughout 2011, mostly based on the increased volume of deals already secured and growing inquiries from clients. Expectations about general economic recovery in 2011 contribute to these projections as well. They expect annual growth in revenue ranging from 5 percent to 15 percent.
Commercial Real Estate

New England’s commercial real estate market was stable in recent weeks. In Boston, a steady volume of lease renewals generated significant revenue for brokers but resulted in little to no net absorption. For the year, office vacancy increased in greater Boston and, according to one contact, is currently in the high teens in the Financial District, while Back Bay and Cambridge enjoy much lower rates (below 10 percent). In Providence and Portland, modest positive absorption is cited in core downtown districts, as tenants are eager to sign deals to take advantage of low rental rates, which are not expected to persist much longer. In Hartford, the vacancy rate for downtown, class A office space was placed at 24 percent for the third quarter; there is some expectation that the city’s office absorption rate will turn modestly positive in 2011. Construction remains limited across the region, with the exception of the multifamily sector, which continues to attract strong investor interest and very attractive financing terms. Based on recent sales prices, one Boston lender to commercial real estate is concerned that the city’s multifamily market may be “overheating.”

The outlook ranges from quite cautious to solidly optimistic. Boston and Hartford contacts expect slow growth and only limited absorption in 2011. Prospects for absorption in 2011 were more robust in Providence and Portland, and a Boston banking contact expects very strong loan demand for commercial properties throughout 2011. No contacts are predicting a “double-dip” in the commercial real estate market (nor for the economy as a whole). Nonetheless, a few are concerned that commercial foreclosures could increase in 2011, putting downward pressure on property values.

Residential Real Estate

Home and condo sales in the First District continued to show significant year-over-year declines in November, as many contacts had expected. Respondents say the large year-over-year declines throughout New England partially stem from the extra boost in activity observed in November 2009 when the first-time homebuyer tax credit was originally set to expire. Nonetheless, home and condo sales activity remains sluggish by any measure throughout the region, with all contacts anticipating that total 2010 sales will fall short of 2009. Meanwhile, the median price of homes continues to edge up in the New England states, with the exception of New Hampshire, which observed another month of year-over-year price declines. Contacts attribute increasing median home prices to relatively higher sales of more expensive properties rather than a general upward movement in home prices. Second-home purchases continue to fare well relative to other segments of the market, as higher income buyers take advantage of low mortgage rates and a large inventory of discounted homes. Most contacts report that inventory levels are rising; they do not see this as a source of concern except for a contact in New Hampshire, where the November months of supply exceeded other states in the region.

Contacts anticipate a continuation of current sluggish activity levels into 2011, with fewer swings than in 2010. Some respondents express concern about possible tax reforms restricting the mortgage interest deduction.
The Second District’s economy has shown further signs of improvement since the last report. Hiring has continued to pick up outside of the manufacturing sector. Business contacts in most sectors report improved conditions and express widespread optimism about the near-term outlook. Cost pressures have risen but consumer prices have remained generally stable. Retail sales over the holiday season were generally strong and ahead of expectations, though post-holiday sales were adversely affected by the late-December blizzard. Tourism activity has remained brisk and consumer confidence has improved moderately since the last report. Commercial real estate has been mixed: there have been scattered signs of improvement in the office market, but the market for industrial space has weakened. Housing markets have also been mixed but generally weak. Finally, bankers report mixed loan demand overall and tightening credit standards on commercial loans and mortgages.

**Consumer Spending**

Virtually all non-auto retail contacts report that holiday season sales were strong and on or ahead of plan, while prices were generally stable. Two major retail chains note that sales in the region were substantially ahead of plan in the weeks leading up to Christmas. A New York State retail association notes that holiday-season sales were stronger than a year ago and stronger than most retailers had expected. While stores in the New York City area generally report brisk sales, a late-December blizzard reportedly curtailed business substantially in the days after Christmas. Two large malls in upstate New York report broad-based strength in sales, despite snowstorms on Black Friday and again in early December; traffic was brisk for most of the holiday season, helped by a steady flow of Canadian shoppers. Most retail contacts report that they hired somewhat more holiday season workers in 2010 than in 2009.

Automobile sales were mixed but generally at favorable levels, as both retail and wholesale credit conditions continued to improve. Rochester-area dealers report that sales of new autos surged 24 percent
from a year ago in November and appear to be running about 10 percent ahead in December, helped by incentives. On the other hand, dealers in the Buffalo area report that sales were down slightly from a year earlier in November and remained fairly sluggish in December; the inclement weather was seen to be a factor.

Tourism activity in New York City has remained fairly brisk since the last report. Manhattan hotels report that occupancy rates remained close to 90 percent in November and December, while room rates continued to run nearly 10 percent ahead of comparable 2009 levels. The late-December snowstorm appears to have had little net effect on occupancy: while many visitors had to cancel their reservations, others who were unable to leave extended their stays. Broadway theaters report that both attendance and total revenues were running about 10 percent ahead of a year earlier in late November and most of December, despite the recent closing of a number of shows. Theaters remained open during and after the post-Christmas blizzard, though attendance is expected to be down noticeably. The Buffalo area saw a modest pickup in tourism during the final week of December, buoyed by a worldwide junior hockey tournament. Finally, the Conference Board reports that consumer confidence among residents of the Middle Atlantic states (NY, NJ, PA) climbed in both November and December, ending the year at the highest level since May.

Construction and Real Estate

Housing markets across the District have been sluggish but generally stable since the last report, while new construction activity has remained exceptionally weak. The housing market in western New York State was described as “dead” in November and December. A contact in New Jersey’s housing industry reports that market conditions have stabilized but have yet to improve, weighed down by a large inventory of unsold existing homes. Single-family home construction has picked up slightly but remains at a very low level, while multi-family construction has fallen. Transaction prices in northern New Jersey are reported to be flat to declining modestly, though the underlying market is hard to gauge because a
disproportionate number of recent transactions are distress sales. New York City’s co-op and condo market was relatively stable in the fourth quarter, while the rental market has shown signs of picking up.

Commercial real estate markets have been mixed, with scattered signs of improvement in the office market, but some softening evident in the industrial market. In New York City, office leasing activity rose to a four-year high, though much of the new leasing reportedly involved companies moving around (often to smaller quarters). Still, there was some net absorption of office space, and vacancy rates declined moderately. Asking rents were generally stable but rose in some prime areas of Manhattan. There were also signs of modest improvement in the Buffalo and Rochester areas, where vacancy rates edged down and rents were up 4 to 5 percent from a year earlier. On the other hand, office vacancy rates climbed and rents edged down in Long Island, while markets in northern New Jersey, Westchester and Fairfield County (CT) were stable. Industrial vacancy rates were little changed, but rents declined across most of the District—particularly in the Albany and Rochester areas, and in New York City. Both residential and commercial construction activity remain at exceptionally low levels throughout the District. A commercial developer in western New York State notes that many small sub-contractors have exited the business and medium-sized firms are struggling.

Other Business Activity

A major New York City employment agency that specializes in office jobs, reports that business was relatively good in December—typically a slow time of year. Legal sector hiring has rebounded a bit from exceptionally weak levels, while financial sector hiring has continued to improve gradually. Fewer job seekers are coming in than a few months ago. More generally, non-manufacturing firms report that they are adding jobs, on balance, and many plan to increase staffing levels in the first half of 2011. Manufacturing contacts, however, indicate some recent tapering off in employment levels, based on our December survey. Nevertheless, contacts in both manufacturing and other sectors generally indicate that
business picked up in December and express widespread optimism about the outlook for the first half of 2011. Contacts also report widening cost pressures but only a modest pickup in their selling prices.

**Financial Developments**

Small- to medium-sized banks in the District report mixed results for loan demand: they note increased demand for commercial mortgages, on balance, and steady demand for commercial and industrial loans; however, weakening demand is reported for consumer loans and residential mortgages. Bankers indicate steady demand for refinancing, though two large lenders in western New York note a drop in home mortgage refinancing. Respondents report some tightening of credit standards for commercial mortgages and commercial and industrial loans but little or no change in credit standards for consumer loans and residential mortgages. Bankers note continued narrowing in spreads of loan rates over costs of funds for all loan categories—particularly in the commercial and industrial loan category, where slightly over half of bankers indicate a decrease in spreads and only one in ten reports an increase. Respondents also indicate an ongoing decline in the average deposit rate. Finally, bankers report that delinquency rates increased for commercial mortgages, decreased for consumer loans, and were little changed for residential mortgages and commercial and industrial loans.
Business conditions in the Third District have improved somewhat since the last Beige Book. Manufacturers, on balance, reported increases in shipments and new orders in December. Retailers achieved moderate year-over-year increases in sales during the holiday shopping period. Motor vehicle dealers also posted year-to-year sales increases as 2010 came to a close. Third District banks reported slight increases in loan volume outstanding since the last Beige Book, mainly in personal loans. Residential real estate agents and homebuilders indicated that sales have been seasonally slow. Contacts in the commercial real estate sector said leasing and construction activity have remained at low levels since the last Beige Book. Service-sector firms reported that activity has been moving up slowly. Business contacts reported more instances of price increases for inputs recently than they did in the previous Beige Book, and several said they expect output price increases to become more common in 2011 than they were in 2010.

Most Third District business contacts foresee improving economic conditions in 2011, but they do not expect strong growth. Manufacturers forecast a rise in shipments and orders during the next six months. Retailers expect sales to continue to move up on a year-over-year basis. Bankers expect modest growth in lending. Contacts in residential real estate expect activity to increase slightly. Contacts in commercial real estate expect only marginal strengthening in market conditions. Service-sector companies expect continued slow growth in the early months of 2011.

Manufacturing
Third District manufacturers reported increases in shipments and new orders from November to December, on balance. However, gains were not spread among all of the region’s major manufacturing industries. Increases in demand for their products were common among producers of furniture, chemicals, testing and measuring instruments, and food products. In contrast, producers of metals, other industrial materials, lumber products, electrical equipment, and machinery generally had month-to-month declines in orders, and other manufacturing sectors reported no change. Overall, the region’s manufacturers continued to report that the flow
of new orders has been erratic. Several used the words “hand to mouth” and “choppy” to describe the recent trend in orders.

Third District manufacturers expect business conditions to improve during the next six months, on balance. Among the firms surveyed in December, slightly more than half expect increases in new orders and shipments, and less than one-tenth expect decreases. Capital spending plans among area manufacturers have been increasing since mid-year, and in December one-third of the manufacturers polled said they planned higher capital outlays in the next six months, and less than one-tenth planned cutbacks.

Retail

Third District retailers generally reported year-over-year increases in line with plans for the year-end holiday shopping period. On balance, stores posted moderate increases in sales without significant unscheduled price reductions. Sales of winter outerwear and jewelry rose fairly well from year-ago levels, but sales of big-ticket electronic items were not strong. A snowstorm on the day after Christmas deterred some shoppers and forced some store closings, but merchants said sales picked up in subsequent days. “The shoppers came. We still did well,” one merchant said. Looking ahead, most of the retailers surveyed for this report said they expect continued year-over-year increases in sales, although they also noted that consumer confidence remains fragile.

Third District auto dealers reported rising sales as 2010 came to a close. Dealers said that inventories were increasing as they took delivery of new models, but dealers generally considered their stocks of new and used vehicles appropriate for the current sales rate. Dealers expect sales to be somewhat higher in 2011 than in 2010, although several expressed concern that rising gasoline prices could restrain sales of less fuel-efficient models.

Finance

At most of the Third District banks contacted for this report, total outstanding loan volume has increased slightly since the last Beige Book. In general, banks reported increases in lending on home equity lines and credit cards but indicated that other types of lending were practically flat. Some bank lending officers noted that usage of credit lines by business firms continued to be low. Commercial bank officers generally indicated that credit quality measures
have been slowly improving. The outlook among Third District bankers surveyed for this report is that lending to both consumers and businesses will move up slowly in 2011. Bankers foresee gradual increases in consumer lending if employment moves up, little or no gain in real estate lending, and a slight increase in commercial and industrial lending.

**Real Estate and Construction**

Third District residential real estate activity has slowed seasonally since the last Beige Book. Both homebuilders and residential real estate agents generally indicated that the usual winter lull in construction and sales had taken hold. In contrast, some real estate agents reported an increase in rental activity of single-family homes. Real estate agents attribute the rise in home rentals to several factors: relocated owners unable to sell their houses at their asking prices, buyers unable to obtain mortgages, and tightening of credit qualifications for renters of apartments. Sales of higher-priced homes have continued to be slower than sales of lower-priced homes in most parts of the region. Home prices have been flat to down in most markets. Residential real estate contacts expect sales to remain sluggish until economic conditions, especially employment, improve. However, several contacts noted that sellers have recently become more willing to reduce asking prices, and this appears to be giving some lift to the sales trend. As one agent remarked, “When sellers get realistic, buyers respond.”

Nonresidential real estate firms indicated that there has been little change in commercial and industrial markets since the last Beige Book, although some noted a few signs of improvement. Contacts said that vacancy rates and rents have been nearly steady, but more tenants have signed long-term leases recently compared with most of 2010, during which short-term leases were more common. Several contacts in commercial construction reported that building owners have recently shown more interest in renovation and new construction, although the contemplated projects are not large. Commercial real estate contacts expect market conditions to improve gradually in 2011. One contact said, “The outlook is considerably less bearish, although it’s not bullish,” and another noted that “the lack of new construction underway will support the beginning of a recovery in leasing.”
Services

Service-sector firms generally reported slightly rising activity since the previous Beige Book. Contacts said that the health care sector continued to have relatively better gains than other sectors and that service-sector activity related to construction continued to be weak. The outlook for the services sector as a whole is modestly positive. One contact said, “We see some slight improvement in the near term, but it will be well into 2011 before there is stronger growth.”

Prices and Wages

Reports from manufacturers since the last Beige Book indicated spreading increases in input costs, but mostly steady output prices. Goods mentioned as rising in price were food products, chemicals, petroleum products, metals, and electrical equipment. Several manufacturers noted evidence of upward price pressure developing in their industries and said they expect more widespread price increases for finished products during 2011. Retailers generally noted more signs of rising costs since the last Beige Book. They cited increases for food products, textile products, shipping charges, and energy. However, many said that competition among stores was limiting increases in retail prices.

Business firms in the region reported mostly steady wages since the last Beige Book. Staffing firms and employment agencies said they have recently seen some growth in demand for temporary workers and slight increases in permanent hiring, but no significant changes in wages or salaries.
FOURTH DISTRICT – CLEVELAND

On balance, economic activity in the Fourth District expanded at a modest pace since our last report. Manufacturers reported some improvement in demand. Information received from retailers and auto dealers on the holiday shopping season was generally positive. Energy production and freight transport volume were stable. Residential and nonresidential construction remained sluggish. And while demand for business loans showed some signs of a pickup, consumer borrowing was weak.

Reports of rising payrolls were limited to the manufacturing sector. Staffing-firm representatives noted an increase in the number of new job openings, with vacancies concentrated in professional business services. Wage pressures continue to be contained. Apart from elevated commodity and steel prices, raw materials and product pricing were fairly steady.

Manufacturing. Reports from District factories indicate that demand was stable or rising during the past six weeks. Compared to year-ago levels, production was higher, with many contacts experiencing low double-digit increases. Several manufacturers noted that while their production levels declined recently—following seasonal trends—orders were above expectations. In general, manufacturers are fairly optimistic and expect at least modest growth during 2011. A few noted that lead times for the delivery of raw materials were getting longer, which they attributed to rising demand across industry sectors. Steel producers and service centers all reported that shipping volume had increased since our last survey, with shipments being driven by energy-related, transportation, and heavy equipment industries. Steel executives we spoke with have heightened expectations for business growth during 2011. District auto production showed a slight decline during November on a month-over-month basis. Compared to a year ago, domestic auto makers showed a substantial rise in production, while foreign nameplates posted a modest decline.

Capacity utilization continues to trend higher, approaching what many of our respondents consider to be more normal rates. Inventories are close to targeted levels. Capital spending plans are conservative, with only a few of our contacts expecting to increase capital budgets for 2011. Outlays are aimed primarily at maintenance, equipment upgrades, and increasing production efficiencies. Prices for agricultural and metal commodities, steel, and scrap remain elevated, while the prices of most other raw materials have been stable. Several producers announced selective product price increases to reflect a rise in the cost of steel and agricultural commodities. Most contacts told us that they have expanded their permanent, full-time payrolls slightly since our last survey, and they will continue hiring at the same pace during 2011. Permanent new hires were largely salaried. To meet rising demand, employers are extending production hours or bringing in temporary hourly workers. Wage pressures are contained. Companies are continuing to restore merit increases and payments to 401K plans.
Real Estate. New home construction was generally flat at a low level during the past six weeks and on a year-over-year basis, with most sales occurring in the move-up buyer categories. Contractors expect construction to remain sluggish through the winter months. List prices of new homes and discounting have shown little change, while some upward pressure on the cost of building materials was reported. Land purchases and construction of spec homes are constrained by the availability of credit. Subcontractor pricing remains very competitive. General contractors continue to work with lean crews, and no hiring is expected in the near term.

Discussions with nonresidential builders drew mixed responses, with a small majority of our contacts reporting stronger activity than a year ago. There is growing concern over the continuing slowdown in inquiries and tightening margins. However, most builders said they had a sufficient backlog to keep them busy in the upcoming months. New projects generally fall into the health-care category, with some industrial and infrastructure work. Our contacts are uncertain about business conditions through 2011. A few builders mentioned that their customers have the ability to fund projects, but they are hesitant to commit. Builders expect construction material suppliers to begin raising prices early in 2011, but they are uncertain as to the amount or whether the increases will stick. General contractors reported no change in employment levels and wages. Subcontractors continue to cope with very difficult industry conditions.

Consumer Spending. Reports from retailers on the holiday shopping season were generally positive. General merchandise stores had the strongest results, while activity at small specialty outlets was mixed. Almost all of our contacts said that sales increased in the low to mid-single digits when compared to year-ago levels. Some retailers noted that consumers are becoming more confident, and it is beginning to show in their buying patterns. Nonetheless, we still heard mixed reports on purchases of discretionary items. Looking forward to the first quarter of 2011, retailers generally expect transactions to rise in the low to mid-single digits on a year-over-year basis, and they believe that rising sales will include more discretionary items. Vendor pricing was generally stable. Most retailers plan a modest increase in capital spending during 2011 for remodeling, expansion, and e-business. Hiring was limited to temporary holiday workers and no pickup is expected in the new year.

Auto dealers reported new vehicle sales during November were steady to up slightly on a month-over-month basis. When compared to year-ago levels, sales were generally higher. A few of our contacts also noted an increase in leasing activity. Looking forward, dealers expect sales to follow seasonal trends through the winter months. However, they anticipate that sales will be slightly higher than the prior year’s level. New car inventories are in line with demand. Reports on used vehicle purchases were mixed. Little change was seen in credit availability. Buyers with high credit scores can readily obtain financing. Dealers’ spending on showroom
upgrades to comply with factory mandates remains modest. More aggressive capital outlays are dependent on sustainable demand.

**Banking.** In general, bankers reported that commercial loan demand was stable or showed modest growth since our last survey. A few bankers commented that although loan originations are up, outstanding balances have declined. We also heard reports from some large banks that lending to small businesses is increasing. On the consumer side, conventional loan demand remains soft, although several of our contacts told us that they are beginning to see early signs of growth. Direct and indirect auto lending continues to show strength, while some weakening was observed in the use of home equity lines of credit. Interest rates for business and consumer credit were stable. Many of our contacts said that demand for residential mortgage refinancing has slowed due to the rise in interest rates. New-purchase mortgage originations remain weak. Core deposits continue to grow, with most of the growth occurring in nonmaturing products. Credit quality was characterized as either stable or showing a slight improvement, especially for business applicants. Delinquency rates are stable or trending down. Staffing levels have shown little change during the past few weeks; however, several bankers reported that they are considering hiring during 2011.

**Energy.** Reports indicate that oil and gas output from conventional wells was fairly steady during the past six weeks. A small increase in gas production is expected if very cold weather persists. Production from Marcellus shale was somewhat higher and is expected to continue to increase. Spot prices for natural gas have increased slightly with the onset of winter, while wellhead prices paid to independent oil producers were fairly stable. Coal production has been steady since our last report, with little change anticipated in the near term. Spot and contract prices for coal were generally stable; however, the price of metallurgical coal increased slightly. Other than a rise in diesel fuel prices, equipment and material costs have been flat. Staffing has not changed, and it is expected to remain at current levels for the near term.

**Transportation.** Freight transport executives reported that shipping volume was stable during the past six weeks. Looking ahead to 2011, most carriers expect growth to be somewhat stronger than they experienced in 2010. They also expect that activity will be more in line with normal seasonal patterns. Almost all of our contacts reported rising prices for diesel fuel, some of which are being passed through to customers via a surcharge. Capital outlays remain at relatively low levels. Spending in 2011 is expected to rise modestly as freight carriers are forced to replace aging equipment. However, some carriers are considering leasing new equipment versus buying, as rising prices for new tractors constrain purchases. Hiring is for replacement only. Two of our contacts noted that they would like to begin hiring additional drivers, but it is difficult to find qualified applicants. Wage pressures are beginning to emerge due to a growing problem with driver turnover and a tightening of the driver pool.
**Overview.** Economic activity improved in the District over the last four to six weeks. The manufacturing sector posted solid gains in December, with many firms citing strength in both orders and shipments. Retailers in the District reported a spike in December sales, along with a marked increase in foot traffic. Modest revenue growth continued at most services firms. Tourism in the District benefited from an early start to the skiing season. The banking sector reported moderate improvements in business loan demand, particularly for industrial equipment. Contacts at temporary employment agencies stated that demand was flat to up slightly. While residential real estate activity was mixed, several commercial Realtors cited a pickup in sales activity, but commercial construction continued to be weak.

**Manufacturing.** Manufacturing activity posted solid gains in December, building on a pickup in October and November. A chemical producer indicated that shipments continued to improve and he expected his operating rate to be at 95 percent of capacity over the next year. He also expected exports, a major part of his recent business gains, to improve further in 2011. An auto-parts supplier said that demand from auto manufacturers continued to exceed initial forecasts, resulting in material shortages and higher supplier costs. A machinery manufacturer noted that his automotive business remained very strong and he anticipated additional strengthening in 2011. He pointed out that other industrial businesses were also picking up nicely. A building materials manufacturer reported that orders were surprisingly strong compared to three months ago, which he attributed at least in part to inventory restocking. Survey contacts reported that prices of raw materials grew at a somewhat quicker rate than in our last report, while prices of finished goods were little changed.

Port-related activity in the final months of the year was somewhat mixed, but remained generally above year-ago levels. A port contact reported that imports from Asia provided most of December’s year-over-year increase in volume traffic, while exports held steady. Another port official stated that exports of both bulk and container goods remained strong and noted that the weak dollar helped support commodity exports to Europe. Overall, however, both imports and exports of commodities and finished goods slowed a bit over the last month. Some of the slowdown on the import side was attributed to weakness in the local economies, with retail goods from China accounting for much of the slowing but apparel goods from South America still holding up well. However, a container shipper described the volume of his goods both into and out of ports as “firm and solid, but not booming.” And a railroad official stated that his port-
related freight volumes were running a little stronger than a year ago, but noted that he did not see the usual growth in traffic during November over the previous month.

**Retail.** District retailers reported a surge in December sales, particularly for groceries, toys and apparel, according to our recent survey. Several managers at chain discount stores reported solid sales leading up to Christmas. In addition, retailers indicated that Black Friday sales were brisk at big-box stores, as media attention helped pull in customers, but Cyber–Monday also brought a big jump in online sales. One exception was big-ticket sales, which continued to languish particularly for items driven by home sales, such as furniture, according to our latest survey. A central Virginia retailer told us that Black Friday left the local cluster of small shops “looking like a ghost town.” However, a new promotion, "Small Business Saturday," bolstered sales that weekend. Retail merchants reported that customer buying patterns have changed; a furniture store owner commented that three out of four of her in-store customers had first browsed the store’s website or called for product information. Although snow fell in many areas across the District in mid-December, most roads were clear on the Saturday before Christmas and, thus, the weather did not hinder shoppers. Retail price growth slowed compared to a month ago, according to our latest survey, while average retail wages grew more quickly.

**Services.** The District’s non-retail services firms generally improved in December from a month earlier. Revenues rose at most services firms, according to recently polled contacts. Demand picked up at trucking firms, and Virginia airports reported increased passenger travel. Telecommunications firms also noted stronger revenue growth. However, demand for healthcare services was little changed since our last report. Several contacts cited difficulty getting business loans. According to participants in our latest survey, price growth eased slightly at services firms, and average wages also moderated somewhat.

**Finance.** Loan demand in the District continued to improve at a slow pace across most market segments over the last six weeks. One banker noted an uptick in demand for industrial equipment loans, particularly from auto suppliers in the District. Loan demand for autos (notably from fleet purchasers) also picked up. However, the banker also added that consumer demand—excluding auto loans—was flat at his bank, with most new applications being primarily for home improvement projects. Another banker, who reported an increase in consumer loan demand over third-quarter levels, did not expect demand to fade after the holidays. In Richmond, a loan officer stated that consumers were more confident about submitting loan applications, particularly for renovation loans. A regional commercial banker reported improvement in small business
lending, especially for equipment leases; she also noted that her bank experienced an increase in SBA loans. While most lending officials reported strong demand for home refinancing, a Richmond banker also cited an improvement in home purchase applications. Only in West Virginia, which lagged in entering the recession, did a banker report that loan demand around the state was still “awfully soft” across most market segments over the last six weeks, and added that there was very little in the pipeline.

**Real Estate.** Residential real estate activity around the District was mixed over the last six weeks. A Maryland contact reported that sales were down compared to a year ago, but also noted an increase in permits (mostly multi-family). However, a contact in the Charlotte, North Carolina area stated that real estate was flat across the board. Several contacts said that problems getting appraisals approved on a timely basis had reduced sales by discouraging potential buyers and had also increased transaction costs. Several real estate agents in other areas reported that housing had started to move, although at deeply reduced prices. Sales activity varied by price range around the District, with most contacts indicating that sales were concentrated at the low end of the price range. Contacts generally reported that prices were either stable or still declining, although one contact stated that prices in his area were rising moderately.

While commercial real estate activity remained weak throughout the District, reports of modest improvement increased since our last report. For example, a Realtor in the Research Triangle area of North Carolina reported that property sales were moving briskly, although partly because prices were low. Contacts indicated that leasing activity in the area also improved, particularly at locations that already had relatively high occupancy rates. Apartment construction edged up, according to District reports, particularly in the Washington, DC area. A survey of construction contractors showed an even split among increasing, decreasing and no change in activity over the past six weeks. Most respondents noted little change in credit availability, with many still having difficulty obtaining credit. Moreover, price pressures remained intense, with most indicating that not only were materials prices increasing but also that intense competition, even for small projects, was squeezing profit margins.

**Labor Markets.** Employment activity in the District was generally stable to somewhat stronger in recent weeks. Several firms reported cautiously hiring back employees as the economy improved. Several small retailers in the Richmond area reported that holiday hiring was limited this year; some hired fewer seasonal employees and extended hours for permanent personnel. However, several contacts noted that fewer staff often meant increased theft. Several
employment agencies stated that demand for temporary workers was at least stable or stronger than six weeks ago. A temporary employment agency in the Charlotte area reported an uptick in requests from small- and medium-sized firms, whereas previously only large firms were hiring. In contrast, an executive search firm stated that employment activity had stalled in October and had not yet picked up.

Tourism. Assessments of tourist activity remained mostly positive since our last report. Managers at ski resorts in Virginia and West Virginia characterized demand as somewhat stronger than at this time a year ago, as unusually cold weather got the ski season off to an early start. A market analyst reported that the Baltimore area was experiencing its best tourist activity in at least three years. A contact in Myrtle Beach reported a modest increase in resort bookings and noted that tourists were spending more at local shops than a year ago. A contact from the Outer Banks of North Carolina, however, described tourist demand as somewhat weaker than a year ago and characterized holiday spending by tourists on gifts and food as flat to down from a year ago.
SIXTH DISTRICT – ATLANTA

Summary. Reports from Sixth District business contacts indicated that economic activity rose moderately in late November and December. Holiday sales were described as generally positive and above expectations. Tourism contacts noted increases for both business and leisure travel. Weakness continued to be reported in the real estate sector as both builders and brokers noted very low levels of activity. Most manufacturers noted a slight increase in new orders and production levels, although those producing construction-related goods continued to experience lower activity. Transportation companies reported moderating freight volumes after significant increases earlier this year. Business contacts continued to report that obtaining loans at acceptable terms has remained difficult, especially for small businesses and start-ups. Bankers repeated that they experienced a lack of loan demand from qualified borrowers. Employment indicators continued to recover, albeit slowly. Most business contacts said that they remain hesitant to add to their permanent workforce until they experienced a sustained increase in sales. A majority of business contacts indicated that current cost pressures remained high, citing increasing material prices and rising labor and benefits outlays. However, most firms remained reluctant to pass input cost increases through to consumers given intense competitive pressures.

Consumer Spending and Tourism. Many District retail stores noted that holiday sales were above their expectations. Most indicated that traffic and sales increased compared with a year ago; however, smaller retailers reported less of an increase in business than larger stores. The majority of businesses contacted noted that sales were driven by a mixture of discounting and stronger demand. The outlook among merchants remained optimistic. District automobile dealers indicated that vehicle sales improved recently and were ahead of year-ago levels. Sales of commercial trucks were also up modestly.

Tourism activity increased slightly relative to a year ago for both business and leisure travel and the outlook remained modestly positive going into 2011. Hotel occupancy rates rose in several of the District's major markets compared with last year. Cruise lines reported an increase in both bookings and pricing power.
**Real Estate and Construction.** Reports from most District homebuilders indicated that the pace of new home sales growth through December remained weak compared with a year ago. Many contacts continued to report that buyers were having a difficult time securing loans. Builders also noted construction activity held steady at very low levels. The outlook was mixed with Florida and Georgia builders expecting weaker activity over the next several months, while elsewhere in the District modest improvements were expected.

Residential broker reports indicated that the pace of existing home sales growth remained weak compared with a year ago, but declines were more modest than in recent reports. Contacts also indicated that home sales at the low-end of the market weakened notably. Throughout the region, short-sales, REOs, and pending foreclosures continued to put downward pressure on home prices which remained below year-earlier levels in most areas. Realtor outlooks for sales growth over the next several months improved somewhat from previous reports.

Nonresidential construction activity remained at low levels through the end of the year. Commercial contractors said that the pace of development and backlogs remained below the year-earlier level. Contacts indicated that access to funding remained challenging and competition for projects had become more intense. Many indicated that they expected the commercial market to remain constrained in 2011.

**Manufacturing and Transportation.** Sixth District manufacturers reported a modest increase in new orders and production levels, while finished inventories contracted only slightly. Several respondents expressed plans to increase production in the short-term. Goods producers tied to the construction sector continued to report very low levels of activity. Manufacturing-related transportation companies reported moderating freight volumes after significant increases earlier this year. Regional rail shipments of farm products increased since the last report, nearly reaching double their year-ago level, while shipments of motor vehicles and equipment declined. The outlook among transportation firms remains optimistic for 2011 as moderate growth in shipments is expected for the first half of the year.

**Banking and Finance.** Some surveys indicated that credit standards have eased somewhat in recent months, but remained tight compared with pre-recession levels.
Business contacts continued to report that obtaining loans on acceptable terms has remained difficult, especially for new and small businesses. Small businesses whose balance sheets were damaged by the recession reported difficulty qualifying for loans even though their financial situation had improved. Meanwhile, bankers continued to report a lack of loan demand from qualified borrowers.

**Employment and Prices.** District labor markets continued to recover, albeit slowly. Business contacts reported that their hiring plans for 2011 have not changed with most remaining hesitant to add to their permanent labor force until they experienced a sustained increase in sales. District firms continued to note a preference for increasing existing staff hours and using part-time or temporary staff. Nevertheless, some contacts noted that they plan to expand their workforce in 2011 at a conservative pace in response to increased output, store openings, or replacing employees lost to attrition or retirement.

A majority of business contacts indicated that current cost pressures were higher, citing increasing material prices and rising labor and benefit costs. Many firms also noted that they were setting aside funds for expected future increases in employment taxes and healthcare costs. However, firms remained reluctant to pass input cost increases through to consumers given intense competitive pressures. Nearly all contacts noted that markups were either near or below what they considered to be normal, reporting that increased productivity has placed some downward pressure on product prices.

**Natural Resources and Agriculture.** Regional oil production reached its highest level in over six years in the fourth quarter of 2010 as increased output from offshore platforms boosted production. Although drilling activity remained well below pre-oil spill levels, the number of rigs operating in the Gulf of Mexico has crept up since hurricane season ended. Contacts continued to note that the lower pace of drilling permit issuance and additional rig inspections could weigh on future energy output in the Gulf.

Most of the Southeast continued to experience varying degrees of prolonged drought. Reports also indicated that both the lack of rain and colder-than-average temperatures have presented challenges to Florida citrus growers. The drought has reduced the physical size of the fruit slightly, and the recent cold snaps have affected young new plantings. Supplies of both cotton and soybeans continue to be tight with strong global demand keeping prices high.
Summary. Economic activity in the Seventh District increased further in December, and contacts were cautiously optimistic about the outlook for 2011. Consumer spending rose more than expected, and business spending continued to increase at a steady pace. Manufacturing production also increased, while private construction remained weak. Credit conditions continued to improve. Cost pressures rose, but there was limited pass-through to downstream prices. Higher prices for agricultural commodities boosted farm revenues.

Consumer spending. Consumer spending increased in December, as holiday retail sales exceeded those of a year ago. Retailers pointed to sales and promotions, rising consumer confidence, and some pent-up demand as potential reasons for better than expected holiday retail sales. Discretionary spending was up this holiday season—apparel, jewelry, and electronics accessories were particularly strong, while big-ticket electronics and furniture performed slightly better than a year ago. In contrast, auto dealers reported that sales held steady in December despite an increase in showroom traffic. Retailers, in general, expressed a positive outlook for 2011, expecting stable, moderate growth in sales in the first half of the year with the potential for spending to accelerate later in the year.

Business spending. Business spending continued to increase at a steady pace in December. Farmers bought equipment before the end of the year to minimize their 2010 taxes. Several retail and manufacturing contacts reported plans to increase outlays for equipment and structures in 2011. Inventory rebuilding leveled off with both manufacturers and retailers indicating that inventory levels were in a comfortable range given the current pace of sales. Hiring of permanent employees remained limited, although a number of manufacturing contacts reported plans to increase their workforces in the coming year. Several continued to note, however, that finding workers with the right skills remained a problem. Temporary hiring continued at a steady pace, with a large staffing firm reporting stable growth in billable hours. In addition, temporary-to-permanent job transitions were noted to be inching up for professional workers.

Construction/real estate. Construction activity was weak in December. Although it edged somewhat lower, the elevated inventory of unsold homes continued to constrain new residential construction. Builders reported a decline in signed contracts and a slight increase in contract cancellations. Contacts also noted that credit was difficult to obtain for refinancing or new construction in neighborhoods where foreclosures and short sales are putting downward pressure on
transaction prices and appraisal values. Private nonresidential construction was little changed in December. However, several construction contacts reported negotiations with automakers that are planning to renovate or expand a number of assembly plants in 2011. Although vacancy rates remained elevated, there were some reports of improvement in commercial real estate conditions. In particular, commercial subleasing activity was noted to have increased as pricing continued to be attractive. Public construction, driven by highway and bridge work, was again strong.

**Manufacturing.** Manufacturing production improved again in December. New orders were solid and order backlogs increased substantially. In general, contacts expressed a positive outlook for growth in manufacturing next year. Several manufacturers of tubes, hydraulics, and other fluid power products noted that activity had returned to its previous peak levels of 2008, and was expected to increase further in the coming year. The fabricated metals, automotive, and heavy equipment sectors were also expected to remain strong sources of growth. A contact reported that global steel consumption was likely to reach an all-time high in 2011. In addition, contacts noted that pent-up demand remains in the motor vehicles sector, with the average age of both light and heavy vehicles still rising. Demand for heavy trucks, in particular, was expected to be even stronger than previously anticipated. In contrast, a contact in the appliance industry noted that shipments were weaker than expected in the fourth quarter, but were still higher than the prior year.

**Banking/finance.** Credit conditions continued to improve in December. Corporate credit spreads for a number of large firms in the District were slightly improved even as market interest rates were increasing. Although demand for liquid assets remained elevated, several contacts noted a substantial increase in risk appetite, which, in particular, benefitted equity markets. The profitability of financial firms increased despite tighter interest rate margins, as loan quality continued to improve. Core loan demand from middle market firms remained limited, as these businesses continue to hold large amounts of cash on their balance sheets. However, contacts noted more inquiries for loans to finance merger and acquisitions as well as an end-of-year increase in demand for small business loans. Consumer credit demand was stronger than expected. Financial market participants were cautiously optimistic in their outlook for financial and economic conditions in 2011, although a few questioned the sustainability of recent improvements, as they expected business and household deleveraging to continue for some time.

**Prices/costs.** Cost pressures increased in December, but limited pricing power again constrained pass-through to downstream prices. Retailers reported that, on balance, wholesale prices edged up further, although there were some large increases in wholesale apparel prices. Most
retailers were accepting lower profit margins with pass-through limited to increases in delivery and other small surcharges. Commodity prices, notably for oil, steel, rubber, and lead, increased. However, contacts thought that only a limited and gradual pass-through of higher materials prices would take place. Wage pressures remained moderate.

**Agriculture.** Net farm income was higher than a year earlier. Crop insurance helped stabilize revenues in areas where there had been disappointing yields. There were, however, reports that some farmers were taking losses because they earlier had oversold their crop production on futures markets at lower prices. Agricultural land values and farmland cash rental rates for the next growing season increased sharply. Demand for crops remained strong in December, with a notable boost from increased exports to Asia. Crop inventories remained low compared with the high level of demand. Prices for corn, soybeans, and wheat rose during the reporting period. Input costs for crop farms were steady so that margins continued to improve. Hog and cattle prices also increased; while milk prices were generally lower, pressuring the margins of dairy producers.
Summary

Economic activity in the Eighth District has increased modestly since our previous report. Manufacturing activity has continued to increase, and the services sector has improved slightly. Early reports from general retailers indicate that holiday sales increased over a year ago. Home sales have continued to decline across the District, and commercial real estate and construction activity was sluggish. Overall lending activity at a sample of small and mid-sized District banks declined in the three-month period from mid-September to mid-December.

Manufacturing and Other Business Activity

Manufacturing activity has continued to increase since our previous report. Several manufacturers reported plans to open plants and expand operations in the near future, while a smaller number of contacts reported plans to close plants or reduce operations. Firms in the automobile and automobile parts, plastics product, glass, furniture, sanitary paper products, and food manufacturing industries reported plans to expand existing operations and hire new employees. Contacts in the household appliance and paper manufacturing industries reported plans to open new facilities in the District and hire new employees. In contrast, firms in container manufacturing and wood products manufacturing announced plans to close plants and lay off workers.

Activity in the District’s services sector has increased since our previous report. Contacts in the storage, business support services, restaurant, and health care industries reported plans to open new facilities in the District and hire new workers. In contrast, contacts in the hazardous waste disposal industry announced plans to decrease operations and lay off workers. General retail contacts noted that holiday sales increased compared with the same period last year. Sales
of new automobiles have grown modestly in recent months, while used car sales have been mixed across the District.

Real Estate and Construction

Home sales continued to decline throughout the Eighth District. Compared with the same period in 2009, November 2010 year-to-date home sales were down 14 percent in St. Louis, 8 percent in Little Rock, 17 percent in Memphis, and 1 percent in Louisville. Residential construction, however, continued to increase throughout most of the District. November 2010 year-to-date single-family housing permits increased in the majority of the District metro areas compared with the same period in 2009. Permits increased 4 percent in Little Rock and 6 percent in St. Louis and Memphis but decreased 5 percent in Louisville.

Commercial real estate and construction conditions were sluggish throughout most of the District, but contacts anticipate improvements in some areas. A contact in Louisville noted that commercial real estate markets continue to struggle, although contacts expect improvements in the suburban office market in 2011. A contact in northwest Arkansas reported that commercial real estate markets are soft. Contacts in St. Louis noted that commercial construction activity was slow. Contacts in south-central Kentucky noted that commercial construction activity has been very limited, but they anticipate some recovery in the next few months. Contacts in northeast Arkansas reported a few new commercial construction projects in retail centers. Industrial construction activity remains slow throughout most of the District. A contact in St. Louis reported low levels of construction activity. Contacts in south-central Kentucky noted some manufacturing and healthcare-related projects. Contacts in Louisville and St. Louis reported more build-to-suit than speculative industrial construction.
Banking and Finance

Total loans outstanding at a sample of small and mid-sized District banks decreased 2.5 percent in the three-month period from mid-September to mid-December. Real estate lending, which accounts for 73.3 percent of total loans, decreased 2.4 percent. Commercial and industrial loans, accounting for 16.3 percent of total loans, decreased 0.9 percent. Loans to individuals, accounting for 4.9 percent of loans, decreased 6.1 percent. All other loans, accounting for 5.5 percent of total loans, decreased 5.3 percent. Over this period, total deposits increased 0.7 percent.

Agriculture and Natural Resources

Cotton production was strong in the District. The number of bales of cotton ginned (separated from the seed) increased by 75 percent from 2009 by early December and by 6 percent from the average 2007-2009 levels. The District’s mid-December year-to-date coal production increased by 2 percent from 2009, while total coal production from mid-November to mid-December was 5 percent higher compared with the same period in 2009.
NINTH DISTRICT--MINNEAPOLIS

The Ninth District economy continued its moderate recovery since the last report. Consumer spending, tourism, services, manufacturing, energy, mining and agriculture saw increases. Commercial real estate showed a slight but surprising increase in activity; commercial construction was flat, and residential construction and real estate decreased. Labor markets continued to strengthen modestly, and wage increases remained generally subdued. Overall price increases were modest, but some exceptions were noted among inputs.

**Consumer Spending and Tourism**

Consumer spending during the holiday season increased from a year ago. Sales activity was favorable during December compared with the prior year at a Minneapolis area mall. A North Dakota mall manager reported that traffic was up about 3 percent to 5 percent in December from the previous year. In South Dakota, a mall manager noted strong retail activity during the last week before Christmas; some stores reported lean inventory levels following unanticipated strong holiday sales volumes. Also in South Dakota, a toy retailer reported strong holiday sales compared with a year ago. A chamber of commerce representative in northern Wisconsin reported that area retailers were pleased with the holiday shopping season. A Minnesota bank director noted that holiday shopping began earlier this season.

According to an auto dealers association in Minnesota, new vehicle sales through November were up slightly from a year ago; light trucks gained market share relative to cars. A Minnesota domestic auto dealer reported strong December sales.

Winter tourism activity was up from a year ago. Sales of snowmobiles increased at two dealerships in central Minnesota compared with the previous year, as early snowfall blanketed the region. A representative of a Minnesota ski resort reported that winter sports activity in the area was well ahead of last season due to good snow conditions and a better outlook for the economy. However, rain and warm temperatures at the end of December led to deteriorating snow conditions for cross country skiing and snowmobiling in northwestern Wisconsin.

**Construction and Real Estate**

On balance, commercial construction was flat at low levels. Commercial construction activity has trended downward in Fargo, N.D., and Great Falls, Mont., according to sources there. Commercial builders in the Minneapolis-St. Paul area described activity as
mostly stable, though some noted signs of slight increases. November commercial and office permits increased in Sioux Falls, S.D., from a year earlier. Overall residential construction decreased. The value of November residential permits fell 7 percent in Minneapolis-St. Paul from a year earlier, though the number of permitted units increased. Home building permits in November fell in value in Sioux Falls, but increased slightly in Fargo from the previous year.

Commercial real estate showed a slight but surprising increase in activity. In Minneapolis-St. Paul, several large leasing deals were announced and a large suburban office tower was recently sold. A November survey by the University of St. Thomas found increased optimism among Minnesota commercial real estate market participants. A commercial broker and developer in Fargo said activity there has picked up as well, with a reduction in the amount of empty retail space. Residential real estate markets slowed. A November survey of Ninth District real estate agents showed decreases in sales prices and transactions and increases in inventory and time on market. November closed sales in Minneapolis-St. Paul fell 39 percent from a year earlier, and median sales prices declined more than 2 percent. In contrast, a real estate agent in Bismarck, N.D., described the market there as healthy.

Services
Professional business services firms reported increased activity. A contact that supports business travel services noted an unexpected increase in activity since the last report. A large technology company is increasing the number of its contract programmers to support software upgrades. An architectural firm noted an increase in projects up for bid as well as a greater number of bidders. Firms that support the mortgage refinance market noted a sharp decline in activity due to higher long-term interest rates.

Manufacturing
Manufacturing output was up since the last report. A December survey of purchasing managers by Creighton University (Omaha, Neb.) showed increases in manufacturing activity in Minnesota, South Dakota and North Dakota. A South Dakota maker of video display systems noted increased new orders since the last report. A Minnesota equipment component producer noted strong sales and was increasing production capacity. A bank director reported that regional manufacturers were busier than a year ago.
**Energy and Mining**
Activity in the energy and mining sectors increased since the last report. Late-December oil exploration activity increased since mid-November. New wind-energy investments were announced since the last report. Continued strong prices were noted for District mining commodities, and District mines were operating at near capacity. A Montana mine recently signed an agreement that will again supply palladium to a large domestic automaker. In Minnesota, November iron ore production increased from October and a mine plans to upgrade its facility to supply Mexican steel plants.

**Agriculture**
Since the last report, agricultural output prices strengthened, but large snowfalls hampered some ranchers. Prices for most District agricultural commodities increased since the last report, including corn, soybeans, wheat, steers and hogs. Snow cover was relatively modest in Montana and South Dakota, but deep snow impeded ranchers in North Dakota and Minnesota.

**Employment, Wages and Prices**
Labor markets continued to strengthen modestly. According to an ad hoc poll of 104 contacts conducted in early January, 39 percent expect to increase hiring and 11 percent expect to decrease hiring over the next six to 12 months. A representative of a Minnesota-based health care system noted that the pace of hiring health care workers was picking up. A Montana job service office reported a relatively sizable number of job openings posted, but demand for nonskilled workers declined somewhat. A Minnesota iron ore pellet producer recently hired 50 workers and plans to hire 24 more to increase production levels. However, a recreational vehicle manufacturer will lay off 500 workers this spring at a plant in northwestern Wisconsin. In Minnesota, a trucking company recently closed, laying off 210 drivers.

Wage increases remained generally subdued. However, a Minnesota all-terrain vehicle powertrain manufacturer gave out bonuses for the first time in several years following the company’s relatively strong performance during 2010.

Overall price increases were modest, but some exceptions were noted among inputs. Bank directors noted generally stable retail prices, but mentioned some input price increases, such as copper and some steel products. Minnesota gasoline prices at the end of December were about 20 cents per gallon higher than a month earlier.
The District economy continued to expand in late November and December, despite slower construction activity. Strong consumer spending over the holidays lifted retail sales and expectations for future spending. Manufacturing activity improved amid a rise in new orders and stronger durable goods production, and some plant managers planned to increase capital spending and hire more workers. Residential and commercial construction remained weak, though commercial real estate sales edged up and vacancy rates dipped slightly. District bankers reported stable banking conditions with some improvements in loan quality. Energy activity expanded further, and incomes improved for the agricultural sector. Even though several district contacts expected to increase employment, wage pressures remained subdued. With raw materials prices continuing to climb, more manufacturers expected to pass through higher input costs to finished goods prices; however, most retailers did not plan to raise selling prices in the coming months.

**Consumer Spending.** Consumer spending improved in late November and December, and many retailers expected further gains in the coming months. Brisk holiday shopping boosted retail sales with some reports of price discounting. Store managers reported that major appliances and household items sold well. Retail sales were expected to edge up further in the next three months. After improving slightly in the last survey, auto dealers reported limited sales, which contributed to larger vehicle inventories. Dealers were optimistic, however, that auto sales would pick up with additional financing incentives and discounts. Restaurant operators reported stronger overall sales despite a continued decline in the average check amount. Tourism activity improved, and Colorado resorts reported a strong start to the winter ski season. District hoteliers reported average occupancy and room rates fell since the last survey but were above year-ago levels.

**Manufacturing and Other Business Activity.** District manufacturing activity strengthened further since the last survey, and plant managers were increasingly optimistic about future activity. Plant managers reported that production, shipments, and new orders increased in December, led by durable goods manufacturers. During the first half of 2011, manufacturers expected new orders, shipments and production to rise, and finished goods inventories to remain
Some factory managers planned to increase employment levels as well as capital spending in the coming months. Stronger demand for computer software and IT consulting contributed to a rise in sales at high-tech firms. Activity in the transportation sector slowed since the last survey period but remained above year-ago levels.

**Real Estate and Construction.** Residential and commercial construction slowed in late November and December, while commercial real estate sales and vacancy rates improved slightly. There was little new home building activity since the last survey period, and construction supply sales were down. Homebuilders and real estate agents noted reduced buyer traffic and a decline in home sales, especially compared to last year when buyers were motivated by the federal tax credit program. With limited sales activity, home inventory levels were expected to grow over the next three months, accompanied by further reductions in home prices. After rising in the last survey period, mortgage loan activity eased with fewer home purchases and less demand for refinancing. Commercial construction activity slowed and was expected to remain weak over the next three months. District commercial real estate contacts, however, reported an uptick in sales and noted prices generally held steady despite further rent reductions. Vacancy rates dipped and were expected to move lower as absorption rates gradually improved.

**Banking.** In the recent survey period, bankers reported generally stable deposits and loan demand with an improved outlook for loan quality over the next few months. Overall loan demand was stable to slightly weaker. Demand for commercial and industrial loans and commercial real estate loans were little changed while demand for residential real estate loans and consumer installment loans decreased. For the third straight survey, credit standards remained unchanged in all major loan categories. Compared to a year ago, loan quality edged up slightly, and bankers expected loan quality to improve further over the next six months. After rising in the previous survey, bankers reported that deposits held steady.

**Agriculture.** Agricultural growing conditions deteriorated since the last survey period, but rising crop prices supported farm income gains. Continued dry weather across the Southern Plains intensified drought concerns and could affect winter wheat development, especially in Oklahoma and Kansas. Crop prices rose further at year-end, boosting farm incomes. Strong export demand
for beef supported an uptick in cattle prices, but hog prices fell with bigger supplies and softer demand for pork. With rising incomes, farm loan repayment rates improved, farm loan renewals and extensions fell, and farm capital spending remained robust. Even with a modest increase in the number of farms for sale, strong demand pushed farmland values higher.

**Energy.** District energy activity expanded further in early November and December. District contacts reported increased drilling activity, driven by additional oil rigs in Oklahoma. While energy producers expected drilling activity to rise in the coming months, some indicated that a lack of qualified labor and limited availability of equipment and services would constrain future drilling activity. Natural gas prices held steady, with ample supplies offsetting higher demand as the winter heating season began. Crude oil prices rose in late November and December, and contacts expected further price gains with stronger global demand and a weaker value of the dollar. Ethanol prices rose with tighter supplies and a one-year extension of the ethanol blenders’ credit and tariff. Higher ethanol prices preserved producer profits despite elevated corn prices.

**Wages and Prices.** Wages generally held steady even as some firms reported an uptick in hiring, and prices paid for raw materials rose further. Several contacts across a variety of sectors expected to increase employment over the next six to twelve months, including manufacturing, transportation, high-tech, energy, and retail. However, few employers planned to offer higher salaries, and wage pressures were expected to remain low. Firms that were maintaining or reducing staff levels often cited low sales growth and uncertainty over regulatory costs as reasons for not hiring. District manufacturers reported another jump in raw materials prices and expected more increases would follow. Transportation companies, builders, and construction supply firms also expected input prices to rise, especially for fuel and petroleum-based products such as roofing shingles. More plant managers planned to pass higher input costs to finished goods prices, and several transportation and high-tech firms anticipated raising prices in the next three months. In contrast, District contacts in the retail sector noted some price discounting during the holiday sales season, in addition to reduced hotel rates and more incentives offered by auto dealers. Most retailers expected selling prices to hold steady in coming months. Menu prices remained flat at restaurants despite a steep rise in food costs.
The Eleventh District economy expanded moderately over the past six weeks. The energy sector continued to be a source of strength, and staffing firms reported demand held steady at high levels. Retailers said holiday sales were on track to exceed those of last year. Reports from the manufacturing sector were mostly positive. Construction activity in the district remained subdued and loan demand was weak, however.

**Prices**  Price pressures increased slightly since the last report. Many responding firms noted higher input prices, and a few had increased selling prices including firms in the food, paper, staffing, airline, shipping, and primary and fabricated metals industries. Retailers said prices held steady, but were expected to increase in the second half of 2011.

The price of crude oil increased about $10 per barrel during the reporting period based on continued strength from Asia, better demand in the US, and a weaker dollar. Retail prices for both gasoline and diesel rose with the price of crude. The price of natural gas edged up seasonally, early in the reporting period, but fell back to near $4 per McF by late December due to weak demand and large inventories. Prices for most petrochemical products continued to rise since the last report, according to respondents.

**Labor**  Employment levels held steady at most responding firms, although there were some reports of hiring. Staffing firms were hiring for their own needs and in anticipation of continued strong demand going forward. Primary metals and high-tech manufacturing firms reported increasing payrolls, and airlines were hiring in call centers and at airports. A few contacts in the energy industry said they were looking for workers to fill very skilled positions. Wage pressures were minimal.

**Manufacturing**  Most construction-related manufacturers reported steady demand at low levels, although there were reports of stronger demand related to apartment construction and business remodeling. Outlooks were generally more optimistic than in the last report, with contacts expecting some improvement this year.

Respondents in high-tech manufacturing said demand continued to grow at a moderate, sustainable pace since the last report. Contacts noted that production was at high capacity and inventories had increased from very lean to desired levels. Several firms said they had added slightly to payrolls. Areas of strength included smart phones and gaming consoles, while demand for computers was reported as "bouncing along the bottom." Most respondents expect growth to continue at a moderate pace for the next three to six months.

Responses from paper producers were mixed, but overall demand remains at low levels. Most expect conditions to remain stable as the economy slowly recovers. Food manufacturers noted improved
sales during the reporting period. Transportation manufacturers also noted an increase in demand, and outlooks are for modest growth in 2011.

Petrochemical producers noted strong domestic and export demand, except for construction-related materials. North American producers of natural-gas based resins and plastics continue to enjoy significant advantages in export markets.

Demand for oil products continued to improve against normal seasonal trends. Refinery utilization rates moved up to the highest December levels since 2007. Margins held steady, despite the surge in the price of crude oil. Suppliers reported that refiners’ confidence has improved.

**Retail** Contacts expect to finish 2010 on a positive note with holiday sales exceeding year-ago levels and outlooks improving modestly. Inventories are at desired levels and in-line with seasonal norms. Two large retailers noted that their sales in the District outperformed those nationwide during the reporting period, but the gap is expected to narrow. The outlook for 2011 remains muted and contacts expect demand to remain flat or grow modestly at best.

Automobile sales held steady over the reporting period, and 2010 sales should show a solid increase over 2009 levels. Contacts expected sales to be strong the final week of December. Inventories rose modestly but are in the desired range. The outlook for 2011 is for continued gradual improvement.

**Services** Staffing firms reported demand held steady at high levels. Strength remains broad-based, with particularly strong demand for workers with expertise in the professional, technical, healthcare and finance fields. Contacts noted that call centers were becoming a new source of strength. As in the last report, contacts said direct-hire activity was picking up. All contacts had positive outlooks and expect continued strength in 2011.

Accounting firms noted seasonal slowness, with demand about even with the year-ago level. Contacts expect a reasonably good year in 2011 but noted demand is unlikely to pick up substantially until clarity is reached on some public and fiscal policy issues. Legal contacts noted an uptick in demand for services—primarily corporate merger and acquisitions and real-estate services. Demand overall was characterized as soft, but improving.

Reports from transportation services contacts were mixed, but mostly positive. Railroad contacts noted business is much better than this time last year and were optimistic in their outlooks. Shipping and intermodal contacts said volumes were up from year-ago levels. Airlines reported continued steady demand. Most contacts in the transportation services industry expect modest to moderate growth this year. However, one intermodal shipping contact said higher input costs had dampened his outlook.

**Real Estate and Construction** The housing market remained weak since the last report. Sales were sluggish at low levels, according to contacts. Homebuilding activity continues to bounce along the
bottom. Contacts are cautious in their outlooks but are hopeful that job growth will translate into increased sales this year.

Office and industrial leasing activity is spotty but appears to be moving in a positive direction, according to respondents. Commercial construction activity overall remained weak, despite increases in multifamily and hospital construction activity.

**Financial Services**  Financial firms reported soft loan demand overall. National institutions noted some pickup in consumer and industrial loan demand, but regional banks reported no change. Commercial real estate lending was weak, with the exception of multifamily. The residential mortgage market was reported as “spotty” across the state, but unchanged overall. Contacts said loan pricing is increasingly competitive. Outlooks remain cautious though more optimistic, and contacts expect to see an uptick in mergers and acquisitions of small banks this year due to the increased cost of regulatory compliance.

**Energy**  Drilling activity remains high. Crude pricing is strong, and margins are good. Growth in the rig count has slowed due to the continued shift away from dry gas toward more oil-directed drilling, natural gas formations rich in associated oil or natural-gas liquids. The liquid-rich Permian basin and Eagle Ford shale areas in South Texas are booming.

**Agriculture**  Drought conditions became prevalent in the District in December, with more than 85 percent of Texas classified as abnormally dry or worse. Ranchers felt the immediate impact of the drought, as poor pasture and range conditions necessitated costly supplemental feeding for livestock. Dry land winter wheat was in need of rainfall, and 2011 crops could be adversely affected if soil moisture levels remain low going into spring planting. Demand for agricultural commodities remained above average, and export activity continued to rise for cotton, beef and grains. Prices were strong for most crops, with cotton, wheat and corn prices increasing further. The overall outlook for demand and prices for agricultural commodities is very optimistic.
TWELFTH DISTRICT–SAN FRANCISCO

Summary

The Twelfth District economy firmed further during the reporting period of late November through the end of December. Price pressures for final goods and services remained limited despite increases for selected raw materials, and upward wage pressures were largely absent. Holiday retail sales were up notably compared with a year earlier, and demand continued to expand for consumer and business services. District manufacturing activity grew further on net, with sustained improvement noted for metal fabricators. Production activity remained solid for agricultural producers, and demand grew on balance for providers of energy resources. Home sales and construction stayed sluggish, and conditions continued to be weak overall in commercial real estate markets. Reports from District banking contacts indicated that loan demand was little changed from existing low levels.

Wages and Prices

Upward price pressures remained subdued on balance. Price increases were noted for assorted raw materials, such as cotton, copper, aluminum, and especially oil. However, final prices for most retail items and services continued to be held down by tepid demand and vigorous competition.

Contacts in most sectors characterized wages as essentially flat, although some continued to point to substantial increases in the costs of health insurance and other employee benefits. The most significant wage pressures were reported for workers with advanced skills in high-tech fields, for whom demand has been growing at a brisk clip in some parts of the District. Contacts in most sectors expect hiring activity to pick up over the next six months, but to a very modest degree, suggesting that wage pressures overall will remain quite limited during the first half of 2011.

Retail Trade and Services

Retail sales increased notably compared with the prior holiday season. Both traditional department stores and smaller specialty retailers reported that holiday sales exceeded their expectations, which were for modest growth. Moreover, tightly controlled inventories enabled many retailers to rely less heavily on price discounts and promotional activity than in the recent past. The pace of sales
improved modestly for grocers compared with the prior reporting period, while it remained largely unchanged at a slow pace for retailers of furniture and major appliances. Demand for new automobiles continued to strengthen, particularly for light trucks. Demand for used vehicles was strong as well, and the resulting high trade-in values reportedly helped spur sales of new vehicles.

Demand increased further for business and consumer services on balance. Sales continued to expand for providers of technology services, including biomedical products, but they remained largely flat for providers of professional and media services. Restaurants and other food-service providers noted further modest improvements in demand, and suppliers of energy services reported increased deliveries to end-use customers. By contrast, providers of health-care services reported that demand weakened slightly in recent months. Conditions continued to improve for businesses in the travel and tourism industry. Contacts from several major markets in the District noted increases in visitor volumes and hotel occupancies, which resulted from rising business travel as well as tourism.

Manufacturing

Manufacturing activity in the District continued to expand during the reporting period of late November through the end of December. Demand grew further for manufacturers of semiconductors and other technology products, with contacts noting balanced inventories and high levels of capacity utilization. Production rates remained at or near capacity for makers of commercial aircraft and parts, as an existing order backlog for larger aircraft was reinforced by rising orders for smaller commercial jets. Metal fabricators saw further increases in demand; sustained improvement has brought capacity utilization back near normal and prompted some firms to rehire employees laid-off over the past two years. Petroleum refiners continued to reduce their output and work down inventories, which have been at elevated levels in recent months. Conditions remained depressed for manufacturers of wood products.

Agriculture and Resource-related Industries

Demand was solid for agricultural products, and activity was stable to up slightly for extractors of natural resources used for energy production. Orders and sales remained robust for a variety of crop and livestock products, especially cotton and cattle. Outside of price increases for livestock feed, reports
indicated that input costs were generally stable. Demand for crude oil grew further, spurred by robust demand from emerging economies combined with modest growth in domestic demand. For natural gas, ample inventories kept extraction activity largely flat.

**Real Estate and Construction**

Demand in District residential and commercial real estate markets was largely unchanged at very low levels. The pace of home sales remained quite slow throughout the District. In addition, an abundance of foreclosed properties and short sales kept inventories of available homes elevated in most areas, which put downward pressure on prices and the pace of new home construction. Demand for rental space grew in some areas, however, with a Seattle contact noting a modest increase in construction of apartment buildings there. Conditions continued to be weak on balance in commercial real estate markets, as vacancy rates stayed high in many parts of the District; rent reductions and other concessions by landlords remained common. In a positive sign, however, investor demand for well-leased office buildings continued to boost market values in some of the District’s major commercial markets, such as San Francisco.

**Financial Institutions**

Reports from District banking contacts indicated that loan demand was largely stable compared with the prior reporting period. Businesses continued to be cautious regarding capital spending, which held the volume of new commercial and industrial loans at low levels. However, contacts noted a slight uptick in utilization of existing lines of credit for businesses. Consumer loan demand remained weak overall, and contacts reported a significant decline in mortgage refinancing, which they largely attributed to the recent rise in long-term interest rates. Lending standards remained relatively restrictive for most types of consumer and business loans, although reports suggested modest ongoing improvements in overall credit quality. Venture capital financing was a bright spot, with contacts noting increased investor interest and funding for early-stage technology companies during the reporting period.