

CONFIDENTIAL (FR)

CURRENT ECONOMIC COMMENT BY DISTRICT

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SUMMARY*

The economic picture presented by the Red Book reports is that the price freeze is working, but that uncertainties concerning Phase II are hampering business planning. Consumers are spending more freely, especially on durables, but demand for most producer goods remains very sluggish, and inventory investment policies are cautious. Employment in most districts does not appear to be improving significantly. Credit is generally available in all leading categories, and interest rates are lower. Two banks (Chicago and San Francisco) report recent evidence that the housing boom has lost momentum.

Most reports indicate that a gradual improvement in general activity is under way that will probably accelerate in 1972. But there are notable exceptions. Richmond reports a "substantial reduction in the pace of shipments and orders," reflecting, in part, the coal and dock strikes. Cleveland finds the coal strike a depressing influence. New York finds that "optimism (is) significantly more subdued." St. Louis states that "activity has tended to level off." A Boston academician warns of a "downward spiral." Cleveland, on the other hand, reports general improvement, and, uniquely, finds evidence of a substantial rise in capital outlays.

Lack of conviction as to prospects for future prosperity was characterized in a variety of cliches of limited descriptive power--e.g., "cautious optimism," "wait and see attitudes," and "waiting for the other shoe to drop." Business firms are cautious on inventories (Kansas City)

*Prepared by Federal Reserve Bank of Chicago.

hirings (Dallas and Philadelphia), and expansion of short-term debt (several banks).

Atlanta tells of cotton textiles producers not accepting orders because of higher cotton prices, and other specific problems are cited in connection with the freeze. Uncertainty over Phase II is not simply a matter of a desire for action by Congress and the new regulatory bodies. Businessmen worry that prices may be controlled more effectively than wages. Lenders are concerned that if interest rates decline further, increases in rates will not be allowed when loan demand strengthens.

Several banks found that purchasers of capital equipment do not view the investment tax credit as a significant stimulus to capital spending under current conditions. Requirements of utilities for new facilities remain large and will not be deterred by the factors affecting other sectors. Boston reports that some firms are reducing capital outlay budgets.

The surge in auto sales, apparently, is universal. Some banks, including Chicago, Minneapolis, and San Francisco, also emphasized strong demand for household durables, especially furniture. Increased consumer purchases, however, have not significantly reduced the rate of rise in liquid assets.

The trade balance may be improving because of pertinent aspects of the NEP. Boston sees evidence of a "Buy American" spirit. Atlanta reports foreign firms have "increased inquiries about plant sites and joint ventures."

Chicago, St. Louis, and San Francisco report large agricultural crops of good quality. Crop price declines, while resulting in reduced

income for crop farmers, are helping to boost meat production.

In the financial area, all banks report credit readily available, and generally at lower interest rates. At commercial banks, demands for consumer instalment loans and mortgage credit are strong, but demand for business loans is still slow.

FIRST DISTRICT - BOSTON

Our directors indicate that their consumer business is continuing to improve moderately, and in a few lines spectacularly, while their capital goods business is still quite sluggish. None of our directors experienced higher wholesale prices from their suppliers.

Judging from the sales experiences of our directors' firms consumer spending is moderately better, but there is no evidence of a buying spree. The one exception to this general experience is in boating, where dealers are expecting a tremendous boat year in 1972 and are ordering accordingly. These orders are, however, based on expectations, not actual sales experience.

Capital goods producers described business as sluggish in all lines except office and public construction. In some cases directors noted a recent deterioration in orders. One director said that he had just become aware that in the container machinery field, customers were cutting back their capital budgets. Another director felt that the recent downturn in capital goods orders was a result of uncertainties about investment tax credit.

Sales of intermediate products to the industrial sector were variously described as sluggish to poor, especially among suppliers to the aerospace and chemical industries. Only one director mentioned that one of his plants was continuing to decrease employment.

One director noted less foreign competition in the construction material market, in part due to the surcharge, in part to a new

buy-American feeling inspired by the President, and in part due to expectations of a tariff increase on these items. The director also felt that exchange revaluation had helped his export sales of machinery.

None of our directors had experienced any price increases during the freeze from their suppliers other than steel. Only one director expected to raise a product's price imminently, and that was in a line where the market has been so depressed that even with the price increase, the price will be below its May level. One director noted that his company's profits were hurt by the price freeze because new labor contracts and higher steel prices had gone into effect, but the company had been waiting until this autumn to raise prices. This director mentioned that he expected price guidelines of 3 percent, and he felt that he could get along with that.

On the wage front, one firm had a strike which was three to four days old. The issues were not completely clear, but among the demands was a 300 percent increase in pension benefits. Another director had signed new wage agreements in depressed markets which called for 5 to 7 percent increases, and in some cases even less, which were to go into effect if and when permitted. Another director noted that one of his non-union plants should have received a wage increase in October, but did not.

All five of our academic respondents were available this month. Samuelson and Tobin pointed out that, since the NEP was announced, the economy, in general, seems to have weakened. Eckstein and Shapiro, however, both project 1972 GNP just under \$1,150 billion,

with a real growth rate just under 6 percent, but the unemployment rate well above 5 percent at the end of 1972. Wallich's expectation that long-term rates will be falling throughout most of 1972 is based upon a GNP gain of about \$90 billion.

Phase II wage policy is the biggest risk in the outlook at the moment according to Eckstein. To stop the previously negotiated increases would constitute a "sharp break with the previous pattern." Wallich felt some sacrifices, such as a partial cut or a stretching out in the deferred wage increases, will be necessary in order to avoid a spillover effect, which would upset a 5 percent wage standard.

The Federal Reserve System was explicitly excluded as a cause for the recent declines in interest rates. Eckstein and Tobin said monetary policy has not been all that easy. Monetary policy has been "less easy than was thought," Wallich stated, because the recent behavior of velocity has been overlooked. Wallich now considers a 6 to 7 percent monetary growth rate as "modest" and feels a 7 to 8 percent growth more appropriate for the present circumstances. He would scale this rate down only if it proved so high as to provoke a rise in long-term market interest rates, or if the rate of inflation continues to subside.

Tobin stressed that the economy is plagued by confusion and uncertainty and is in some danger of a downward spiral. Since fiscal stimulus has not yet been enacted and disagreement about Phase II persists, Tobin urges monetary authority to "get some expansion right now." Specifically, he advocated pushing the federal funds rate

down to 4 1/2 percent. Shapiro thinks short rates have fallen so sharply that there are going to be some rises; he feels a monetary growth rate of 4 to 5 percent in the next quarter or two and rising to attain a 6 percent rate in 1972 is appropriate.

Only Tobin questioned lowering the discount rate; his reservation was that the signal might be "misinterpreted," i.e., interpreted as evidence that the economic situation is a precarious one. Wallich would favor a reduction in the discount rate only if it were to be allowed to go up again in the future. If the lowest level reached is to become the ceiling level, Wallich thinks it unwise to reduce either the discount rate, the prime rate, or ceiling rates under Regulation Q.

SECOND DISTRICT - NEW YORK

On the basis of opinions expressed by the directors of the New York bank and of the Buffalo branch, the mood of rising optimism regarding the economy that appeared to be emerging last month has now been replaced by a significantly more subdued outlook. Much of the current assessment of the business situation is heavily conditioned by the uncertainties surrounding Phase II and, to a certain extent, by developments in the foreign exchange markets. Most felt that business activity would pick up in 1972, but, on balance, the sentiments expressed in this connection were cautious, and most looked for only a moderate increase.

Regarding consumer spending, the retailers that were contacted reported that business was better than last year but not very much so. They looked for a good Christmas season, but were only "conservatively optimistic" regarding sales over the coming months.

Virtually all the directors of the New York bank and of the Buffalo branch, moreover, saw no significant change in business capital spending plans. Among the New York bank directors, the chairman of the board of a large manufacturing concern felt that, at most, there might have been "some minor upward revisions."

Another director, a Rochester businessman, basing his comment on conversations with major manufacturers in the Rochester area, noted that the plans made in 1970 for 1972 had not been greatly changed. Similar sentiments were expressed by other directors. The chairman

of the board of a large New York City bank felt that the 9 percent increase in plant and equipment spending in 1972 indicated in the Edie survey was "optimistic," while most of the Buffalo directors felt that the 1972 increase would be closer to 6 or 7 percent than 9 percent. The Buffalo directors pointed to the uncertainties surrounding wage and price controls and the high rate of unutilized capacity as deterrents to capital spending. These directors felt, however, that the capital goods spending picture could be improved by congressional action on an investment tax credit and/or liberalized depreciation allowances, which would clear away some of the present uncertainties.

In general, most directors felt that, apart from some instances of stock piling, their own businesses had not been appreciably affected by developments in the foreign exchange markets, the 10 percent surcharge and the dock strikes.

Several of the Buffalo directors noted that domestic automobile sales had been "unusually brisk," a development they attributed at least in part to the import surcharge. The chairman of the board of a large New York City bank, however, was more pessimistic: he reported growing evidence, including a decline in foreign collections and in new import credits at his bank, that developments affecting foreign exchange and trade are having a detrimental effect on business and cited reports that some contracts have been held up pending the clarification of the international financial situation.

Much uncertainty was expressed about the effectiveness of Phase II (opinions expressed predate the Pay Board's 5.5 percent

decision). In general, the directors had a "wait and see" attitude. The president of an upstate bank characterized the situation as "confusion compounded by concern." The Buffalo branch directors expressed considerable uneasiness regarding labor union leadership's apparent tough stand against effective wage controls, and its potential impact on any future wage control program.

Against this background, while most directors looked for some increase in economic activity, sentiments as to the extent of the recovery were mixed. Among the "bullish" minority, the vice president of Rochester's largest firm predicted a growth in GNP of 9 to 9 1/2 percent in current dollars over the next six months, citing the end of the inventory adjustment process and normal cyclical forces as the reasons for his optimism. The former chairman of the board of a large oil corporation also thought there would be a significant business upturn if the international financial situation is straightened out. The majority of the directors, however, were more cautious and, in general, linked their opinion regarding the potential advance to the extent of the success of Phase II.

THIRD DISTRICT - PHILADELPHIA

The general outlook for conditions in the Third District is one of cautious optimism. Manufacturing activity still seems somewhat sluggish although the prognosis for the next six months is an expanding regional economy. Consumer activity is on the upswing, and bankers see loan demand holding its own over the next few months. Most bankers are in favor of the floating prime in principle, but disagree on the mechanics of its implementation. The 4 percent guideline on dividends is generally well received.

District manufacturers seem optimistic about the level of general business activity but remain more cautious about trends for their own firms. For example, of the firms polled, nearly 50 percent report general business activity increasing in October and project continued expansion in November. But at the company level, although nearly 50 percent indicated increases in new orders and shipments for October, only 36 percent were willing to make such a forecast for November. In addition, a smaller percentage are planning to build inventories and add workers during November than reported such activity for October. The outlook for the longer term is more optimistic. Nearly 70 percent of the manufacturers foresee the regional economy expanding a half year ahead. As a result of this anticipated business expansion, close to 30 percent of the firms plan to add employees over that time span.

Consumer activity seems to be picking up steam. One banker noted that October had been one of their strongest auto loan months

ever. Another felt that the strength of the housing market would generate a strong demand for household durables in the next few months. Members of the bank's board of directors also see a somewhat sluggish industrial sector and an active consumer sector. They feel that the lack of optimism in the business community is overstated, and may be the result of yet uncertain Phase II guidelines.

Area bankers report a gradual trend upward in loan demand, with strength coming in the construction, textile, and retail sectors. They expect demand to remain stable during the coming months but consider that to be good, given the situation for the same period in 1970. Philadelphia banks lowered their prime rate in October, and some did again recently. One banker was concerned that bankers would get little credit for lowering prime now, but would be criticized later if demand pressures forced the rate back up. Most bankers were in favor of the floating prime in principle but questioned the timing and mechanics of the plans so far adopted. One bank president felt that the public would view the floating prime as an effort to avoid controls. Another thought it should be tied more closely to the cost of bank funds (fed funds or CDs) than to other open market rates.

The board of directors, in general, is pleased by the 4 percent guideline set for dividends since it recognizes the need for dividend flexibility. However, a few members wonder if the guideline might not cause dividends to move higher than they otherwise would. They argue that the 4 percent maximum may become an "expected" 4 percent so that corporations feel compelled to give their stockholders as much as possible under the guideline.

FOURTH DISTRICT - CLEVELAND

Output, employment, and unemployment in the district are all showing some improvement. Steel industry economists, however, say the recovery in their industry is proceeding more slowly than they expected a month earlier. Preliminary results of our survey of manufacturers' capital spending indicate that substantial increases are planned for 1972 in the Cleveland and Cincinnati metropolitan areas. Recently, some of our directors have also reported signs of strengthening in a number of areas, but signs of sluggishness in certain capital goods areas persist.

Our index of manufacturing activity turned up in September, following sharp declines in July and August. On the other hand, the nationwide coal strike that began on October 1, which involved 80,000 workers, is having a severe impact in mining activity in the district. (The Fourth District accounts for more than one-third of the nation's bituminous coal production.) Nonfarm payroll employment also rose in September, following three consecutive monthly declines. The district's insured unemployment rate rose noticeably from June to September, and then started to decline in October. However, unemployment is still high in some metropolitan areas, particularly steel centers.

Economists from four major steel companies in the district all reported an improvement in new orders last month, but they emphasized that the orders were well below normal October levels. Steel orders from the auto industry continue to be sparse. The auto

companies are talking about resumption of normal ordering in December for January delivery, but they will not say how much. ("Normal" depends on the schedule for auto production.) Apparently, the auto companies are being cautious because of uncertainty about the course of new car sales after the price freeze ends. The economists noted that steel consumption, in general, has been running below their earlier expectations, and that the economy has to show more improvement than it has recently exhibited to get the steel industry back to a reasonable level of operations. A heavier than expected volume of imported steel is retarding customer inventory liquidation and prolonging sluggishness in domestic orders. The consensus is that it will be February or March before we can expect to have "normal" steel output.

Preliminary results of our semi-annual capital spending survey show that in the Cleveland area, more manufacturing firms have reduced than raised their spending plans for 1971 since our spring survey, and manufacturing firms are planning a significant rise in the dollar volume of spending for 1972.

Reports from some of our directors indicate some recent strengthening in business activity in a number of areas, while others involved with certain types of capital goods report continued sluggishness. One report of a strong increase in new orders in recent weeks came from a director associated with a large computer and business equipment manufacturer. The improvement was in a number of the firms' product lines and came from a wide variety of customers. There was some indication that some of the improvement

may have come at the expense of foreign competition. Another director from a highly-diversified manufacturing firm reported a recent widespread improvement in new orders for a number of the firms' divisions, but he also noted continued weakness in government-related business and aerospace activity. Another director reported that the situation in the machine tool industry remains extremely depressed and that there are no signs of an improvement over the near term. This same director noted a growing amount of skepticism among business associates about the likelihood of success in holding down wage increases under the administrative structure set up to direct Phase II of the President's new economic program. Persistent sluggishness was also reported by a director whose firm manufactures a number of specialty gear items; this director noted that a recent "stretch-out" in the production of rapid transit equipment had an adverse effect on the firm's sales.

FIFTH DISTRICT - RICHMOND

The moderate uptrend noted in district business activity over the last several months has apparently been slowed by the prolonged coal and dock strikes. Our latest survey of manufacturers suggests a substantial reduction in the pace of shipments and declines in new orders and backlogs. Other survey respondents continue to report strong retail sales, although the number reporting increases declined from the previous period. District bankers report some tapering in the recent strong surge of consumer and mortgage loans, and only moderate increases in business loan demand are indicated. District crops have suffered severe damage from Hurricane Ginger and heavy October rains.

The diffusion of responses from district manufacturers suggests a distinct slowing of activity, although most of the slowing appears to be centered in lines affected by the coal and dock strikes. Metals producers, especially in the Baltimore area, report substantial reductions in shipments, new orders, and backlogs. A number of manufacturers in other lines also commented that the strikes are adversely affecting their business. Furniture manufacturers continue to report a strong orders picture and are generally optimistic regarding the near-term future. Except for hosiery manufacturers, textile producers are also beginning to exhibit a cautious optimism about the future.

Our survey indicates that retail sales have been seriously affected, especially in West Virginia, by the coal strike. Sales of new cars are strong in all areas except those immediately affected by strikes. Retailers generally appear to be anticipating a record or near-record holiday season.

Manufacturing inventories reportedly have declined further, and while nearly one-third of our manufacturing respondents report inventory levels higher than desired, the overall inventory situation appears much improved over three months ago. Trade respondents indicate further increases in inventories, but all of this appears to be voluntary. Employment in the district has apparently declined somewhat in recent weeks, but this seems to be due mainly to strikes. More than one-third of our banker respondents reported employment declines in their areas. On the other hand, nearly one-third of manufacturing respondents reported an increase in the number of hours worked per week. No significant change in prices received were reported by manufacturing or trade respondents.

Responses from banks in the district suggest that both residential and nonresidential construction activity may have slackened some in recent weeks. Bankers report only moderate strength in business loan demand, and the number of banks reporting increases in demand for consumer and mortgage loans were down from the previous month. In strike-affected areas, bankers report a sizable increase in automobile repossessions and, in general, loan delinquencies.

Through November 4, the season's gross returns from flue-cured tobacco marketings were up 5 percent over last year, as 7 percent higher average prices offset a 2 percent decline in sales volume. Virginia and North Carolina crop losses resulting from Hurricane Ginger and heavy October rains have been estimated as \$83 million. Damage to the peanut crop alone is estimated to be \$49 million, or 48 percent of the total cash receipts from last year's record crop. Losses in corn, soybeans, and cotton account for the remaining \$34 million.

Looking ahead, most banking respondents believe that economic activity in their areas will either stabilize at present levels or increase. Most manufacturing respondents indicated that plant and equipment capacity relative to desired capacity is about right.

SIXTH DISTRICT - ATLANTA

Based on a recent Research Department survey of 21 business leaders and other contacts, support for the new economic program remains strong among businessmen and labor rank and file. However, there are doubts about the efficacy of Phase II because top labor officials may not cooperate. The surveyed businessmen believe that prices will increase moderately after November 13. They further indicated that the President's program has not yet resulted in any significant changes in capital spending plans and that consumer sentiment has improved only slightly since August. Evidently, no switching from foreign to domestic suppliers has yet occurred because of foreign exchange developments.

Survey respondents report nearly universal support among businessmen for the President's program. However, many businessmen feel that the program will be undermined by an inability of the Pay Board to control wage increases. Some businessmen expect price controls to be more effective than wage controls; many others are uncertain about how they will be affected by Phase II controls. The freeze has evidently caused considerable inequities that will be very difficult for Phase II controllers to rectify. A fear was expressed that a new bureaucracy may result from the program.

Price expectations differ considerably among businessmen, but, on average, price increases after November are expected to be more moderate than before the freeze. A few respondents expect

inflation to take up where it left off, mainly because they do not expect the Pay Board to be effective. More respondents expect scattered price increases and a definite reduction in inflation. A paper company executive reports that a scheduled \$8 a ton increase in newsprint prices has been postponed until at least January 1, and that the increase will then probably be less than \$8. A sales executive for a steel firm reports that some producers with a high percentage of flat rolled steel in their product mix will be in trouble if scheduled price increases on these products are not allowed to go into effect after the freeze. The cotton textile industry is reportedly not accepting new orders because increases in the price of cotton during the freeze have increased costs that, temporarily at least, cannot be passed along to buyers.

Apparently, the President's program has as yet had little effect on capital spending plans. Most respondents report no change in investment plans since the beginning of Phase I. However, a telephone company has increased its estimates of business activity in 1972 and 1973, and increased its capital spending plans accordingly. An electric utility stepped up its purchases of needed autos and trucks just to take advantage of the freeze. An auto dealer reports that he is going ahead with a previously postponed facility, evidently because of the surge in auto sales.

A majority of those surveyed report little change in consumer attitudes since the freeze. However, production of consumer appliances has reportedly been increased in anticipation of

improved sales, and consumer demand for textile products has increased. Textile inventories have been reduced substantially at mills and at the wholesale and retail levels, and a good expansion of sales is anticipated "after uncertainties are removed."

Foreign exchange developments apparently have not as yet caused much switching from foreign to domestic suppliers. The price spread between foreign and domestic steel has decreased, but no actual switching has occurred yet. Cotton exports have been encouraged by foreign exchange developments, and this has added to upward pressure on the price domestically. A port official reports that the floating exchange rates have caused only moderate difficulties. A jewelry store executive reports that diamond importers are temporarily holding current stocks off the market in anticipation of price increases later. An importer has reportedly shelved plans for a major expansion of facilities because of the 10 percent import surcharge. The director of a state board of industry and trade reports that foreign firms have increased inquiries about plant sites and joint ventures, as a result of foreign exchange developments and the import surcharge.

SEVENTH DISTRICT - CHICAGO

The economic picture in the Seventh District continues to be characterized by strength in consumer durable goods and in residential construction; contrasted by weakness in producer goods, nonresidential construction, and inventory investment. Uncertainty over Phase II may be dampening and delaying a restoration of business confidence, and, therefore, of expansionary business policies. District labor markets are soft and, overall, do not appear to be improving. Credit is readily available in all categories, but, except for consumer auto loans, demand for credit is not vigorous, and, in the case of residential mortgages, has weakened recently.

Manufacturers of appliances, color television sets, and furniture have increased output in response to larger retail sales. In part, these developments reflect the rise in newly completed residences, and the continued high level of output of mobile homes, which are shipped furnished. But retailers, generally, express optimism on prospects for sales in the oncoming Christmas season. Auto output schedules are being raised modestly, indicating that producers do not view the surge of auto sales merely as a temporary phenomenon associated with the price freeze and the import surcharge.

Although businessmen typically offer public endorsements for the optimistic general forecasts made by professional forecasters, there is widespread skepticism. Current trends in investment policy-- both for inventories and for fixed capital--and in hirings and other decisions requiring cash outlays, suggest lack of confidence in the

general forecasts. (This may, of course, make the upsurge all the more vigorous once momentum is gained.)

Uncertainty over Phase II will not be resolved simply by promulgation of broad guidelines. Questions relate to the relationship of price increases and wage increases which, in large degree, will determine profits; to the methods of enforcement and the machinery for adjudication of disputes. The poor performance of the stock market is cited as evidence of this uneasiness. In addition, some influential bankers and businessmen are listening to, and repeating, forecasts of a general decline in activity offered by consultants and commentators.

Part of the current uncertainty could be relieved by favorable action by Congress on pending NEP legislation. But the effect of the tax credit and depreciation reform is emphasized by sellers rather than buyers of equipment.

Steel orders are said to be slow, unsteady, and disappointing, but, nevertheless, basically on the uptrend. Total orders for producer goods (finished goods and components) are, at best, holding steady. Sales of trucks, in contrast, have been excellent, reflecting some of the same factors encouraging auto sales. Producers of both farm and construction machinery report a sharp decline in sales abroad in recent months--a trend that predated August 15. (A large part of these sales are from European factories.) Softness in markets for producer equipment is cited as evidence that prices would not have been raised even if it were not for the freeze.

From the buying side, planned investments of many manufacturing firms are well below peaks of past years. Work in hand by plant design firms is at a very low ebb. Utilities are moving ahead with expansion programs that are far from complete.

Reports from real estate brokers, mortgage lenders, and title insurance firms indicate a more-than-seasonal slowing in demand for residential mortgage loans, starting in late September. Sales of housing units, especially existing units, have weakened, and some builders have reduced plans for starts in 1972. Credit is said to be readily available at stable rates, so the situation reflects some easing in demand for housing. Increased vacancies had been noted earlier in luxury apartments, but the recent development includes all types of housing.

In the farm sector, income of livestock feeders is up because of higher prices for animals coupled with reduced feed costs. But crop income is down sharply because of plummeting corn prices. Harvesting is well-advanced in most areas, and crops are excellent. Meat packers find the freeze burdensome because of varying seasonals and other complications associated with joint products. The ceiling price on hides is causing shortages because of increased foreign demand.

EIGHTH DISTRICT - ST. LOUIS

Following a moderate expansion throughout most of the year, business activity has tended to level off in recent weeks according to a survey of some leading businessmen. Confusion and greater caution tend to dominate the thinking of business leaders as plans relative to Phase II of the Administration's new economic program are discussed. Construction has apparently stabilized at a relatively high level and, as a result, sales of the construction supply industries and new home furnishings have likewise stabilized. Retail sales of the larger department stores have remained unchanged in recent weeks, but store managers remain optimistic. Output of major manufacturers in the district continues to expand moderately, and some new investment plans were mentioned. Both savings flows into financial firms and loan commitments continue up.

Most of the businessmen interviewed expressed confusion and doubt as Phase II plans of the Administration's new economic program unfold. Typical of the expressions was the view of an official of a major manufacturing firm who stated "I am somewhat negative at the moment. We would have been better off without the freeze." Several expressed the view that the proposed investment tax credit will help, but at the same time expressed doubts that wages will be maintained at levels consistent with high investment incentive. Those interviewed are especially concerned with the

confusion relative to existing labor union contracts and current labor-management negotiations.

Construction continues to provide the major stimulus to the Eighth District economy. However, after rising sharply during the first part of the year, it has tended to level off recently. Demand growth for building supplies has also slowed. The trend is similar for new home furnishings, such as built-in appliances and synthetic fibers for carpets.

Major manufacturing firms report a continuing moderate uptrend in output and sales. Plastics and fibers for the transportation and home building industries are well above year-ago levels. Factory sales of soft goods are likewise higher. Steel is in a slump as a result of excessive inventories, accumulated in preparation for an expected strike. Leather goods factory sales are also low as a result of rising imports, and the turnaround for such goods is expected to be slow, despite the surtax on imports.

Most officials interviewed would like to see more definite economic policies before making major changes in their investment plans. Some reawakening, however, was noted. Two major manufacturing firms reported expansion projects, and one large retailer, whose outlets are concentrated in the inner city, reported plans for major expansion in the outlying area.

The uptrend of savings flows into financial firms and loan demand continues. Despite the announced decline in the prime rate, mortgage rates generally remain firm at 7 to 7 3/4 percent. Other

credit terms, such as downpayment requirements, however, are apparently easing.

The Eighth District agricultural situation is generally favorable. Weather conditions were good throughout the production and harvesting season. Large crops have been produced and harvested, but storage facilities are reported to be short in some areas. This larger volume of farm products has already been reflected in a sizable decline of wholesale prices of farm products, and in a slight decline in the wholesale price of all commodities.

NINTH DISTRICT - MINNEAPOLIS

The consensus response to our monthly phone survey of Federal Reserve bank directors is that district consumers have not yet reduced their savings rate or begun to spend accumulated savings. The district's strong increase in housing construction has stimulated sales of furniture, home furnishings, and appliances, and these retailers are quite optimistic about the future. Directors are unaware of any pressure for large pay increases after November 12, but generally feel that previously negotiated pay hikes will have to be granted. District manufacturers foresee their sales improving in the fourth quarter and during the first half of 1972.

Although one director detected some decline, the consensus was that the savings rate of district consumers has not yet been reduced. Most directors reported that savings deposits have continued to rise, and one director disclosed that his bank had just concluded its most successful promotion to attract new savings accounts. Skepticism was also expressed as to whether or not district consumers would start to spend accumulated savings. However, one director did indicate that he expected the savings rate would come down and that consumers would start liquidating accrued savings.

District housing unit authorizations in the four-month period ending in September were 29 percent above a year ago, and bank directors report that this has stimulated district sales of furniture, home furnishings, and appliances. One director revealed that furniture dealers in his area have a backlog of deliveries, and

that furniture manufacturers are having some difficulty filling orders. Several directors also indicated that retailers expect furniture and home furnishing sales to continue to improve.

Bank directors detected no pressure in their areas for large pay increases after November 12. One stated that workers in his area were just anxious to retain their present jobs and maintain their current incomes. Two directors felt that union members would be willing to settle for smaller pay increases than labor leaders are demanding, while another indicated that a union he deals with is not too concerned about pay board guidelines as it feels it has the political clout to eventually surpass them.

Directors generally believed that after November 12 workers would be reluctant to sacrifice any previously negotiated wage increases which were foregone during the freeze. According to one, workers in his area might be willing to give up retroactively-paid increases but would expect to receive the higher wages after the freeze. Another stated that differences between pay board guidelines and negotiated wage increases would eventually have to be given to workers. Previously negotiated wage increases were considered to be legal commitments which have to be honored by another director.

According to the preliminary results of our fourth-quarter industrial expectations survey, district manufacturers continue to expect that their sales growth will improve in the fourth quarter and during the first half of 1972. After surpassing year-earlier

levels by 5.2 percent during the third quarter, district manufacturing sales are expected to be up 9.7 percent from a year ago in the current quarter before advancing 8.2 percent during the first half of 1972. The current sales predictions are very close to those made for their respective quarters in the third-quarter survey.

The optimistic outlook for district manufacturing sales can be attributed to a rejuvenation in durable goods sales. In the third quarter, district durable goods sales surpassed year-earlier levels for the first time in a year and are expected to strengthen during the forecast period. Much of this expected improvement can be traced to the district's lumber and wood products, electric and nonelectric machinery, and scientific instrument industries. No significant increase in the rate of sales gain is foreseen by district nondurable goods manufacturers.

TENTH DISTRICT - KANSAS CITY

Economic activity seems to be picking up a bit in the Tenth District, although most firms are being conservative in expanding employment and inventory levels. Capital spending intentions in various types of businesses across the district suggest a slight increase, on balance, over last year. Investment plans are said to be virtually unaffected by the promise of a tax credit. Business loan demand remains generally soft, and deposits are reported as steady. Interviewed bankers and other businessmen are guardedly optimistic about the economy in 1972, but few really expect a boom year. Many executives are apprehensive about Phase II and the wage increases that may be allowed.

Judging from the businesses contacted, economic conditions are improving somewhat. Construction contractors report increased activity and have been doing some hiring. A manufacturer of small aircraft has recalled some employees. Other firms, however--including a manufacturer who has recently suffered a strike by his steelworkers, a major airline, and oil companies--are doing increased business with fewer workers. With only one exception, reported plans for expansion held little promise for adding jobs once capital additions are put in place. And while production activity is increasing, inventories still are being held down.

A survey of major utility companies shows continuing expansion in this industry. Plans for capital outlays vary from maintaining last year's pace to substantial increases over recent

rates of growth. Prospects for tax relief are said to make no difference in investment intentions. As in the past, employment is expected to grow less rapidly than total services.

Firms in other industries also are expecting to make new capital outlays. A large manufacturer of rubber products plans a multimillion dollar plant expansion next year. A major agricultural supplier reports new plant and equipment expenditures for next year will be below those in the recent past because of project completions, but still will total several millions. Two large sugar corporations, two big oil refineries, and three steel-using companies all are planning modest additions to plant and equipment at about last year's pace. None of the reporting executives of these firms feel that the investment tax credit has influenced their plans in more than a very small way. Businessmen feel that Phase I has been a success, and they expect 1972 to be better than 1971. Uncertainty about Phase II--"waiting for the other shoe to drop"--is complicating decision-making right now. For example, one manufacturer, who normally sets standards for production costs a full year in advance, is finding it difficult to do so because suppliers are unwilling to quote full-year prices.

Loan demand at district commercial banks varies considerably from area to area, but generally continues to follow the pattern of recent months. Real estate and consumer instalment (especially auto) loans remain the stronger categories. Several bankers, moreover, noted an improvement in the quality of consumer credit--delinquencies

in some cases are at record lows. Construction loans and a few calls on national account lines are the only bright spots in an otherwise bleak business loan picture. Some bankers look for a seasonal upswing in business loans over the next two months. One respondent mentioned the possibility of an increase in transportation business loans in response to the proposed investment tax credit.

District bankers report steady deposit figures in the past month. Rates offered for CD money have, in several cases, been set above money center levels by one-eighth to one-fourth point, but response has been only moderate. One banker observed that consumers seem to be financing purchases out of savings rather than by borrowing.

The "floating" of the prime rate was widely applauded as a further step toward deemphasizing that rate. Most district banks are quoting a 5 1/2 percent prime rate, but they will charge their national prime borrowers whatever those firms are paying to money center banks. The district's largest bank has just introduced a new policy of not announcing its prime rate. The bank's policy is ". . . to be very competitive and in fine tune with money market rates." Judging from responses, the rate structure for local non-prime borrowers has probably not declined in line with national prime rate reductions.

ELEVENTH DISTRICT - DALLAS

The announcement of Phase II of President Nixon's new economic program apparently had little effect upon the thinking of the directors of this bank in terms of leading them to make substantial alterations in their outlook for economic activity in the region and nation. Of the 26 head office and branch directors surveyed, an overwhelming majority now expect economic activity in the nation to increase moderately over the next nine months. This was essentially the opinion of these businessmen, bankers, and educators prior to the President's outline of the control apparatus to be established under Phase II. The directors believe that these improving economic conditions in the nation will produce a moderate decline in the unemployment rate and be accompanied by moderately rising prices. Banking directors are now expecting a moderate fall in interest rates, while industrial directors anticipate no real growth in employment, plant and equipment expenditures, or inventory investment for their firms over the near term.

With respect to the national economy, almost three-fourths of the directors currently foresee a moderate gain in activity. Prior to the disclosure of Phase II, this view was held by slightly more than two-thirds of the directors. The announcement of the Phase II outline also produced little change in the directors' assessment of the unemployment rate. Nearly 60 percent of the directors are still of the opinion that the unemployment rate will

fall moderately. As for the present outlook for prices, about two-thirds of the directors expect that moderate increases will occur, and the balance anticipate that prices will remain essentially unchanged. Until the Phase II program was made public, about one-fourth of the directors were expecting substantial increases in prices, half were anticipating moderate increases, and the rest were looking for little change. Thus, the consensus of directors, by a small majority, is that the creation of the Pay and Price Boards enhances the prospect for greater price stability.

The outlook for the regional economy was also largely unchanged by announcement of the Phase II outline. Eighteen of the directors currently foresee a moderate increase in activity in their local areas, as compared with 14 earlier. The announcement caused no alteration in the directors' assessment of the prospects for the unemployment rate in their local areas. Just over half were (and still are) anticipating a moderate decline in the unemployment rate. The directors believe that prices will edge upward slightly in the district. Earlier, directors were somewhat less optimistic about prices.

Commercial banking directors were also surveyed on their outlook for money and capital market rates and the commercial bank prime lending rate. Nine of the 14 commercial bankers now believe that short-term rates will decline moderately. Prior to the announcement of Phase II, ten of the respondents thought rates would remain essentially unchanged or increase moderately. Their evaluation of the prospects for long-term interest rates has also im-

proved slightly. A clear majority now anticipate that capital market rates will either remain unchanged or decline moderately over the next nine months. Over the same period, half of the banking directors believe the prime lending rate at their banks will decrease moderately, 43 percent forecast no change, and 7 percent think that a moderate increase is in the offing.

Directors associated with nonbanking businesses were surveyed with respect to the outlook for their firms and industries. The announcement of Phase II caused virtually no change in the assessments of eight businessmen-directors as to their outlook for employment, prices, plant and equipment expenditures, and inventories over the next nine months. A majority believe that employment, plant and equipment expenditures, and inventories for their firms will remain unchanged, and that the prices of output of their firms will increase moderately. Three believe that Phase II will have no impact on their profits, four are of the opinion that profits will decline moderately, and only one anticipates that profits will be improved.

Other directors were asked to assess the reception of Phase II in their respective areas. Three out of the four directors in this category indicated that the program was very well received. With respect to the relative impact of the stabilization programs, two of the directors feel that Phase II favors labor, one director believes that the program benefits consumers, and one is of the opinion that business is favored.

TWELFTH DISTRICT - SAN FRANCISCO

According to our directors' reports, economic activity in the Twelfth District is continuing to grow at a steady pace. Most of the strength continues to come from the consumer sector and construction, particularly residential building. The end of the West Coast dock strike is another favorable factor for many businesses' prospects. On the other hand, there is no sign of any vigorous upswing in business capital expenditures beyond recent levels.

Significant increases in consumer spending occurred in October. In some cases, retailers reported increases 15 percent over the previous year's sales, including consumer durables, whose sales had been slow. Auto sales are also stronger. Much of the increase reported occurred in September, and sales seem to be somewhat slower in October. Domestic car dealers expect a good year, and their principal concern seems to be slowness in deliveries from the factory. Foreign car dealers, in contrast, are less optimistic because of the effects of the import surcharge and the disruption caused by the dock strike in delaying shipments of new cars.

Construction activity is the other important source of strength. Activity is centered on single-family building, while construction of multifamily units is slowing because of higher vacancy rates. The continued inflow of funds, particularly into savings institutions, has insured a steady flow of finance to builders at somewhat lower interest rates. One director in southern

California reported that this ready availability of funds is encouraging further building of multifamily units, despite a local surplus.

Unemployment rates continued near 12 percent in the Seattle-Tacoma area. According to some of our Seattle directors there is no evidence that unemployment will be reduced in the immediate future, and it is expected to increase seasonally during the coming winter months. The area has a considerable surplus of warehouse and office space. Although some businesses, particularly those which are medium-sized and serving national rather than regional markets, are doing well, they are not able by themselves to bring about any major reduction in local unemployment.

Our directors were asked to assess the prospects for increased capital expenditures in the light of recent changes in economic policy. The general consensus was that there would be no immediate increase; current projects were being carried through, but few revisions of plans have occurred. The explanation was that uncertainty about the policies to be followed in the so-called Phase II has led businesses to be cautious until the direction of policy is known. Once the wage and price guidelines are established, they should be more willing to undertake increased investment. Only one director reported actual examples of increases, but both of these projects were contingent upon the passage of the tax benefits proposed by the President, and in any event both projects are scheduled for a 12-month completion date.

District agriculture has been experiencing a good year in terms of market prices and yields. The exclusion of agricultural prices from the price freeze has not resulted in any jump in market prices. In practice, the inability of buyers of farm products to pass along price increases has limited the prices they are willing to pay. One director reports that livestock prices have been held to 3 to 5 percent below the ceilings for dressed meat.

Banks' deposits have been gradually rising. On the loan side, the greatest demand has been for consumer instalment credit and real estate mortgages. Commercial loans have not been showing any strength in most parts of the district. With the exception of minor reductions in interest rates, the lending and investment policies of the district banks have been basically unchanged during the past month.