

CONFIDENTIAL (FR)

CURRENT ECONOMIC CONDITIONS BY DISTRICT

Prepared for the
Federal Open Market Committee
by the Staff

November 12, 1980

TABLE OF CONTENTS

SUMMARY	i
First District - Boston	1
Second District - New York	4
Third District - Philadelphia	8
Fourth District - Cleveland	11
Fifth District - Richmond	16
Sixth District - Atlanta	19
Seventh District - Chicago	22
Eighth District - St. Louis	26
Ninth District - Minneapolis	29
Tenth District - Kansas City	31
Eleventh District - Dallas	34
Twelfth District - San Francisco	37

SUMMARY*

Overview. Reports from Reserve Banks this month indicate, on balance, some improvement in economic activity. Manufacturing bounced back in several areas as have retail sales and to a lesser extent capital investment, but conditions in the agricultural sector are mixed as the effects of the summer drought continue to be felt. Any optimism, however, is tempered by concern over the recent run-up in interest rates. Accordingly, many respondents are looking either for a pause in the present upturn or for a very sluggish recovery. Despite the weak outlook for the economy, inflation is expected to continue at high rates. While the demand for business loans varies among Districts, the decline in home mortgage activity appears rather pervasive.

Business Conditions and Outlook. The extent of the recent strengthening in production and sales activity varies from District to District. An upturn in manufacturing is reported in Boston and Atlanta but in Minneapolis, after three months of improvement, production is down. Economic conditions in Cleveland, Chicago and St. Louis were spurred by an increase in steel production, but this heightened demand is viewed as temporary--mainly the result of inventory replacement. Retail spending is generally stronger with the exception of San Francisco, where sales remain below last year's level. In New York and Chicago, the market for domestic automobiles is lackluster. While the majority of industrial respondents in a Philadelphia survey look forward to a pickup in business activity during the next six months, there is widespread concern among respondents that the recent surge in

* Prepared by the Federal Reserve Bank of New York.

interest rates will hurt the economic recovery. Philadelphia, Cleveland, Richmond, Atlanta, Chicago, St. Louis, Minneapolis, Kansas City, Dallas and San Francisco all cite some deterioration in local housing markets which they attribute to rising mortgage rates.

Prices. Purchasing agents in Kansas City report some slowing in the rate of increase in input prices, but this is expected to be shortlived. Sharply higher prices for both raw materials and finished goods are also anticipated in Philadelphia and Cleveland, and wage rates continue to accelerate in Chicago. Dallas also notes a further run-up in labor costs, particularly in energy-related industries, but lumber prices there are well below the levels of a year ago.

Financial Developments. Business loan demand remains sluggish in Boston and New York. In Dallas, however, commercial and industrial lending has been buoyed by heavy demand from energy-related industries. While declining mortgage activity is linked to sharply higher mortgage rates by Atlanta and Minneapolis, continuing economic uncertainty and falling real incomes are considered more significant factors by Cleveland respondents. A falloff in loan applications is reported by Philadelphia, and some San Francisco S&L's have completely dropped out of the mortgage market. Chicago and Atlanta note a growing trend towards renegotiable and variable rate mortgages. Mortgage demand remains high in Dallas, but few commitments are being made as loan defaults and FHA-VA foreclosures increase. Strong savings inflows are reported by Kansas City S&L's, while at San Francisco banks, large outflows have taken place.

Consumer Spending. New York, Philadelphia, Richmond, Chicago, Atlanta and Dallas all indicate retail sales gains spurred by heavy marketing and promotional activity. Advances are led by moderate to expensive apparel

items and other soft goods, but low priced soft goods and consumer durables still lag. Only a very modest improvement in sales is noted in reports from Cleveland, St. Louis, Minneapolis and Kansas City. In San Francisco, retail sales remain at recession levels. In Boston, however, stronger sales, even in constant dollars, are reported for the first time in months. Despite the short holiday selling period due to the late Thanksgiving holiday, merchants in New York, Philadelphia, Atlanta and Dallas are looking forward to a strong Christmas season. Automobile sales are being bolstered by the introduction of 1981 models in Kansas City and San Francisco. In Cleveland, only small cars are selling well. In New York, foreign car sales are brisk, but the demand for domestic models remains weak. With sales still sluggish, another wave of dealer closings in the New York area is anticipated. Automobile sales are described as disappointing in Chicago.

Residential Construction. Housing market conditions continue to deteriorate as rising mortgage rates further discourage demand. A decline in home sales is reported by Chicago, St. Louis and Minneapolis and housing starts are falling in Cleveland, Kansas City and Dallas. While new home prices are up slightly in Kansas City, prices are reported stable in Philadelphia and softening a bit for higher priced homes in Dallas.

Business Fixed Investment. The outlook for capital spending is mixed. Atlanta notes strong investment in many parts of its District as a result of both state and local tax incentive programs, but Boston reports a downturn in orders for heavy metalworking equipment and machinery for paper and pulp production. In New York, machine tool orders are stronger although industry spokesmen do not expect full recovery until late 1981. Construction of manufacturing facilities is up in parts of New England, particularly among defense-related industries. Military hardware production is also strong in

St. Louis, as is production of oil and natural gas equipment. Chicago respondents expect the demand for heavy trucks to rebound in 1981.

Agriculture. The outlook for agricultural production and farm income is mixed as many Districts continue to feel repercussions from the summer drought. Richmond reports farm loan demand is weaker than normal, while repayment rates are falling sharply. Renewals and extensions are higher and collateral requirements are stricter. Dallas also notes slower loan repayments, while Kansas City respondents expect a doubling in the number of farmers not expected to meet credit standards in 1981. Many of these farmers, however, will be eligible for low-cost emergency loans from the Farmers Home Administration. The outlook for crop yields is good in Minneapolis and San Francisco, but the Atlanta Reserve Bank reports that crop production estimates for the southeast have been lowered again.

Inventories. Retail and manufacturing inventories are generally lean. In Boston, stocks of home furnishings are so tight that any strengthening in demand is expected to translate into an immediate increase in production. Auto inventories, in particular, are being held down because of the high carrying costs according to respondents in New York. Other retail inventories are reported in line with sales with the exceptions of Kansas City and some areas of St. Louis where demand remains weak. These stocks, however, are expected to be worked down during the Christmas selling season.

Academic and Financial Consultants. All of this month's academic respondents agree that the recovery will be weak by historical standards as a result of tight monetary and fiscal policies. Professor Eckstein thinks that there will be a recession in 1981 as a result of the 15 1/2 percent prime rate. Eckstein believes that because of the essential inconsistency between the structure of the economy and the goal of price stability, only a

3 to 4 year recession will reduce the inflation rate significantly.

Professor Houthakker believes 1981 will be characterized by the slow real growth necessary to control inflation, which he expects to moderate slightly next year. Houthakker is not convinced further tightening is warranted and warns the Fed not to fine tune monetary policy. Professor Samuelson believes there is a 20-25 percent chance for a 1981 recession but 2 to 3 percent real growth is more likely. He feels that the inflation outlook is unfavorable and counsels the Fed to try to hit the money growth targets if the price is not exorbitant. Professor Tobin believes there is a good possibility that rising interest rates will cause a downturn next year, and he would not tighten monetary policy any further as a result.

The financial consultants continue to urge the Fed to persist in its determination to reduce the inflation rate. Mr. Kaufman expects a slowing in the pace of recovery in the early part of 1981. At about the same time, he anticipates a temporary decline in short-term interest rates along with a wave of new corporate bond offerings. Mr. O'Leary strongly urges the Fed to continue pursuing a policy designed to reduce the inflation rate and to defuse expectations of inflation. Mr. Stone feels that the Fed should soon achieve success in slowing the aggregates sufficiently to meet its longer term growth targets. He perceives a drop in short-term rates over the balance of the year, and while he does not foresee a double dip recession, a pause in the recovery within the next three months should be expected.

FIRST DISTRICT - BOSTON

Economic activity in the First District has picked up slightly. An important exception, however, is the capital goods sector where demand has begun to fall off. Retail sales in the region, which had been just keeping pace with inflation, appear to have made real gains over the past four or five weeks. In manufacturing, firms which make consumer products or industrial goods used in current production have seen increases in sales. On the other hand, orders for capital goods have fallen. Banking respondents report sluggish loan growth.

For most of this year retail sales in New England have risen with inflation, but there has been no volume increase. However, according to representatives of two large general merchandise chains, there has been a marked increase in sales during the past month. The demand for moderate to better goods is particularly strong; low priced items are faring less well.

Surveys of area manufacturers show sizeable increases in production and new orders. However, conversations with officers of individual firms are less encouraging. The demand for building materials, home furnishings, packaging and automotive products has picked up from lows reached earlier this year, but still remains depressed. In addition, orders for capital goods are weakening. Among the areas affected are heavy metalworking equipment; machinery for the pulp and paper, chemicals, rubber and plastics, and shoe industries; and commercial jet engines.

Despite this indication of declining investment nationally, several firms stated that they are proceeding as planned with their own

capital programs and construction of manufacturing facilities is up strongly in some parts of New England. The defense business is still strong, although one executive predicts some delay in orders until the new president takes office.

Manufacturing inventories appear to be tight. A representative of the home furnishings industry, which has been very adversely affected by the recession, says that despite weak sales inventories in the industry are at rock bottom and any increase in demand will translate into higher production.

Several manufacturers expressed considerable optimism about the prospects of a new administration and the change in the Senate. One senses that some will act in anticipation of future tax cuts. One chief executive says that the election results have encouraged him to launch a new sales campaign.

Banking respondents report that loan demand, both consumer and commercial, is sluggish.

Professors Eckstein, Houthakker, Samuelson, and Tobin were available for comment this month. All agree that the recovery will be weak by historical standards. They also agree that tight monetary and fiscal policies are responsible for this outlook.

Professor Eckstein thinks that with the prime rate at 15 1/2 percent there will be a recession in 1981. Noting that credit crunches now are coming six months apart, he argues that this is a period with the most extreme stop-go policies the U.S. has ever seen. Eckstein believes there is no way that monetary policy quickly can overcome the essential inconsistency between the structure of the economy and the goal of price stability. Accordingly, he thinks that only a prolonged recession (3-4

years) will reduce the inflation rate significantly.

Professor Houthakker expects the economy to continue to move sidewise through 1981. He believes this period of slow real growth is necessary to control inflation, which he expects to moderate slightly next year. Houthakker finds the recent rapid rate of money growth somewhat disturbing, but he is not convinced that further tightening is warranted. Since he views money growth as the result of a process of random fluctuation around a trend that is consistent with the targets, Houthakker warns the Fed not to try to fine tune monetary policy.

Professor Samuelson believes there is a background probability of 20-25 percent of a 1981 recession, but his best guess is for 2 to 3 percent real growth next year. He feels that the inflation outlook is unfavorable, so he expects housing once again to have to run the gauntlet of high nominal interest rates. Although Samuelson describes the money growth targets as nothing more than a shibboleth, he thinks that it will be taken quite amiss if they are violated this year. Thus, he counsils the Fed to try to hit the targets if the price is not exorbitant.

Professor Tobin believes there is a good possibility that rising interest rates will cause a downturn next year. He thinks that the crucial issue facing the country is whether to allow a normal recovery or not. It is Tobin's opinion that the Fed cannot decide this issue by itself. Tobin would not tighten policy further. He notes that the combination of rapid money growth near the end of the year and the special importance pinned to achieving calendar year money growth targets provides a good example of the hazards of the present monetary policy strategy. He believes that the Fed's credibility is important only if a program of announced monetary austerity is to be followed until inflation is wrung out of the economy.

SECOND DISTRICT--NEW YORK

Business activity in the Second District was mixed in October. Retail sales strengthened during the month, reflecting extensive promotional activity. Foreign car sales picked up, while the slump in domestic car sales deepened. No turnaround is expected on the domestic side until late spring. Outside the consumer sector, some signs of a weak pickup have been reported in chemicals, machine tools, and paper and packaging products. The respondents, for the most part, expect a slight upturn in the fourth quarter, but do not anticipate any major economic recovery until the second half of 1981. On the financial side, business loans at New York City banks have declined since mid-October. In the mortgage market, rates have stabilized recently after rising sharply in September and early October.

Consumer Spending

Retail sales in the Second District have generally strengthened during October. Sales for the month as a whole, both in the New York metropolitan area and upstate, were in line with or in a few cases even exceeded retailers' expectations, and inventories were considered satisfactory. Although the heavy promotional activity during this period was cited as the reason for much of the brisk sales, some underlying strength in consumer spending was perceived, especially for soft goods. Comparisons between the city and suburban stores were mixed in most instances. Similarly, the volume of cash and credit sales did not follow any pattern with the relative vigor of each varying from store to store. Retailers voiced some concern over November sales because of the late Thanksgiving but are planning for a strong Christmas.

Automobile sales in the Second District were mixed in October, with foreign car sales outperforming domestic. Foreign car sales were reported to be about as strong as in the comparable month last year with prospects for further improvement in November. In contrast, domestic car sales are below the volume a year ago, and the slump is expected to continue at least until late spring. Rising auto prices combined with shrinking discretionary income were cited as making consumer spending cautious so that only lower priced, leftover-1980 models appear to be selling. Consequently, the domestic dealers contacted expect more dealerships to close. Wherever possible, inventories at the dealer level have been kept intentionally lean. Auto makers voiced concern that any further downturn in sales might place some capital spending plans in jeopardy.

The Manufacturing Sector

Outside the consumer sector, there are slight signs of improvement. Some pickup in orders for chemicals has occurred, in part because improving conditions in the steel industry have increased demand for chemical products used as inputs in steel production. Orders for steel increased in August and September but remained flat during October. Further advances are expected during the coming months, principally for customers' inventory rebuilding. Some improvements were noted in paper and packaging products but this was felt to be largely due to advance buying to avoid expected price increases, rather than any strong recovery in underlying demand. Some machine tool makers are reporting strengthening sales, though for some companies shipments continue to outpace orders and full recovery in the industry is not anticipated before late 1981.

Economic Outlook

The outlook of most District respondents remains somewhat bearish. Although most expect some upturn in consumer spending in the fourth quarter, they still expect relatively weak growth through the first half of 1981. Several respondents suggested that this is going to be a W-shaped recession because the economic fundamentals do not warrant a sustained recovery. The second downturn is expected to be seen first in the housing sector where permits began to weaken in October. Higher interest rates were cited as the principal cause of a weakening housing market, but the decline is not expected to be as sharp as earlier in the year. Respondents also observed that capital spending has shown no definite signs of recovery.

Financial Developments

Business loans at New York City banks have been weak since mid-October, in contrast to a large increase in loans at banks outside the Second District. In the mortgage market, rates seemed to have stabilized at about 14 percent. The Federal override of the mortgage usury ceiling has resulted in the first sale of pass-through securities by a New York mutual savings bank-- a \$10 million private placement with three life insurance companies.

Financial Panel

This month we have comments from Henry Kaufman (Salomon Bros)., James O'Leary (U.S. Trust), and Robert Stone (Irving Trust).*

Kaufman: While real GNP will probably increase at an annual rate of at least 3 percent in this quarter, a slowing in the pace of the recovery is likely in the 1st quarter of 1981, reflecting the impact of higher interest

* Their views of course are personal, not institutional.

rates and increases in the Social Security tax. In the credit market, another wave of new corporate bond offerings is likely to hit the market in the early part of next year when short-term interest rates are likely to decline for a short period of time.

Mr. O'Leary: We are in the midst of a broad revolutionary change in the long-term capital markets--a sharp reduction in the availability of funds for investment in straight, long-term fixed-rate bonds and mortgages. Since most investors are convinced that the upward trend of inflation and of interest rates will continue, there will continue to be a very high-risk premium in the yields on these instruments and the long-term, fixed-rate markets will continue to be subject to great volatility. The need for the Federal Reserve to persist in its determination to pursue a policy designed to reduce the inflation rate and to defuse the expectation of inflation is thus most urgent. It is imperative that the new Republican Administration aid the monetary authorities with real fiscal restraint and other long-term policies.

Mr. Stone: Member bank borrowings have now reached levels that should enable the Fed to achieve success in its effort to slow the aggregates sufficiently to meet its longer term growth target. Success could probably be assured by holding borrowings at or slightly above current levels for another three to four weeks. As markets begin to perceive such success, short rates will drop very rapidly--probably by 100 to 150 basis points, which I judge to be the amount of expectational fluff now in the market. Rates would then work lower over the balance of the year, closing well below present levels. I do not believe that the economy will experience a double dip. We are, however, likely to see a pause some time within the next months, and this will reinforce the decline in interest rates.

THIRD DISTRICT - PHILADELPHIA

Indications from the Third District in November are that business remains mixed. Manufacturers indicate no change in industrial activity in November from last month, but expect a significant upswing six months from now. Employment may be given a boost from this brightened outlook, but inflation is expected to continue with no foreseeable relief. Retail sales are moderately strong this month, owing mostly to retailers' marketing efforts, however, and not underlying strength in the economy. As for the future, local merchants are slightly edgy about the first half of 1981 and, therefore, are planning no changes for inventories. In the financial sector, local bankers report mixed loan activity in November as C&I loan volume is up but consumer loans are down. In the housing sector, sales have dropped off sharply in the last few months as mortgage money has gotten tight. New starts have slowed as contractors and developers are waiting for sales to pick up.

INDUSTRIAL ACTIVITY

Area manufacturers responding to the November Business Outlook Survey report no change from October in overall business activity. This could mean that the expansion that appeared to be starting in September and October has been choked off, although it is still a little early to draw any hard conclusions. In terms of specific indicators, both new orders and shipments have dropped marginally in November, while inventories appear to be growing slightly. On the employment front, local manufacturers continue to make small cuts in payrolls and working hours.

Nevertheless, the six-month-ahead outlook is still good according to the survey participants. Over 60 percent of the respondents expect general business activity to pick up between now and May. Both new orders and shipments are expected to

increase substantially over the period, and inventory building is planned at more firms than ever before in the survey's history. Labor stands to gain as well from this brightened outlook, as survey respondents plan to lengthen the average workweek and hire new employees by next May. Increased capital outlays are also expected.

Prices are up again in November in the industrial sector. Input costs are higher for about 65 percent of the survey participants and 27 percent report charging more for the goods they sell. Looking ahead, inflation is expected to continue, as 96 percent of the managers surveyed project raw materials costs to increase by May, and nearly 70 percent plan price hikes for their finished goods.

RETAIL ACTIVITY

Area retailers report sales to be moderately strong in November compared to year-ago levels, which is pretty much in-line with their expectations. District merchants attribute these gains to marketing efforts on their part, however, and not to underlying strength in the economy. Sales of soft goods, particularly apparel and sporting goods, are doing well while big ticket items remain sluggish.

As for the future, local merchants are uncertain about November sales because Thanksgiving falls late, allowing only three post-holiday Christmas shopping days in the month. A strong Christmas season is expected, though. As a Director of this Bank in the retail business notes, Christmas sales are projected to be good, particularly in the days just before Christmas.

Retail inventories are "in-line" to "a little tight" at this point. Area retailers remain slightly edgy about the first half of 1981, though, and plan no changes for stock levels, hoping to keep inventory-sales ratios healthy.

FINANCIAL ACTIVITY

Third District bankers report mixed loan activity in November. C&I loan volume is up 3 to 10 percent over year-ago figures, generally a little ahead of budget. Consumer loans, on the other hand, are down by about 4 to 5 percent, but are expected to level off. Looking ahead to the next six months, area bankers project an increase of about 5 percent in business loans, while retail loans are expected to remain flat, as consumers wait to see what the new Reagan Administration does economy-wise. Some area bankers expect a double-dip recession, with a final pick-up expected around the second or third quarter of 1981.

Local banks are currently quoting a prime rate of 15 1/2 percent. They expect the prime to peak shortly, and then to slide back by 200 basis points by mid-1981.

Area deposit flows show little change from recent trends, with deposits running about 2 percent over November '79 levels.

HOUSING

Housing sales in the District have dropped off sharply in the last few months as mortgage money has gotten tight. Sales are reported down 20 to 60 percent below year-ago levels. Prices are reported to have been stable over the last six months, particularly because mortgage rates ranging from 14 1/2 to 15 percent have discouraged many buyers. Rates are expected to drop between 12 and 13 percent in coming months, though, thereby giving sales a boost. In the meantime, contractors and developers are holding off on new groundbreakings until sales pick up.

FOURTH DISTRICT--CLEVELAND

Summary

Respondents in the Fourth District anticipate a 1.5 percent increase in real GNP in 1981 from 1980, despite rising interest rates. Inflation continues to be the major threat to the recovery. A boomlet has developed in steel orders, but may reflect price hedging that is borrowing from orders in 1981. Consumer goods producers expect little near-term improvement in consumer spending, but auto dealers are encouraged by new model sales. Bankers report business and consumer loan demands are weak, but not worsening since the latest interest rate increases. However, S&L officials and home builders report a substantial decline in buyer interest and applications as mortgage rates average nearly 14 percent.

Outlook

Economists who attended the Fourth District Economists Round Table Meeting held at this Bank on November 7 expect the recovery to be sluggish and a typical for the early stages of an expansion. The median of 28 forecasts, made shortly before the election, shows real GNP increasing at annual rates of 1.5 percent, 2.7 percent, 4.6 percent and 3.4 percent from the first quarter of 1981 through the fourth quarter, respectively. Most of the step-up after mid-1981 is expected to come from higher consumer spending, residential construction and a recovery in business fixed investment. Mild inventory liquidation is expected to continue into 1981. Real GNP this quarter is expected to increase by about the same rate as last quarter, because of smaller gains in consumer spending and net exports. Five of the economists expect real GNP to decline in the first quarter of 1981 before resuming growth, and one expects a decline in the fourth quarter of 1981.

Prices

Inflation is reaccelerating and is the key factor underlying a slow recovery, according to several district economists. The latest run-up in food prices stems partly from increased grain exports and a shortfall in farm output, according to a bank economist. Despite oil price increases in spot markets, the Iranian-Iraqi war should not have a significant effect on prices, according to a petroleum industry economist, unless damage to production facilities is substantial and OPEC allows the spot market to run prices up. However, several energy economists expect oil production losses to be made up by other countries. Some economists who expect a small-V shape recovery in 1981, anticipate that accelerating inflation will contribute to a softening economy late in 1981 and another recession in 1982. Several expressed preference to check inflation expectations now even at the expense of retarding a recovery.

Steel

The steel industry has made a sharp turnaround recently, with order levels currently at 75 percent of operating capacity and possibly reaching 90 percent in November or December. Steel economists believe this bubble in demand will be temporary, and represents, in part, a slight improvement in consumption (mostly from autos), a decrease in imports, but mostly a vigorous shift in inventory replacement by steel service centers. Imports have been dampened by the reinstatement of trigger pricing at levels above domestic mill prices. Shipment levels could reach as high as 23 million tons in the fourth quarter and 85 million tons in 1980, depending on the ability of plant facilities to shift from a shut down condition. After January, steel operations will likely fall back into the 70 percent to 80 percent range, according

to a steel economist, unless the economy is stronger than currently expected.

Consumer Spending

The improvements in consumer spending in the early part of the third quarter have leveled out in recent weeks, according to several consumer-goods producers. An appliance producer reports his firm has not yet experienced a recovery in either shipments or orders, and a bank economist anticipates no increase in purchasing power until after a tax cut in the second quarter of 1981. While nondurable goods remained flat in recent months, sales of food-store items have held up well relative to past recessions, even during the sharp decline in the second quarter, according to a producer of consumer soft-goods. However, year-to-year volume on consumer-packaged products is currently increasing at only a 2 percent rate, compared to a normal 4 percent rate during a recovery. Fourth District economists expect about a 2 percent gain in real PCE between the fourth quarter of 1980 and fourth quarter of 1981. A typically cautious economist with a major retail chain in the district expects a somewhat larger gain. According to a bank economist, the financial position of households remains weak for a recovery; the debt-repayment burden is still high, liquidity is low, and delinquency rates are rising.

Autos

Although auto sales should gradually improve throughout 1981, no major comeback is expected before 1981, according to an auto industry economist. Auto sales are expected to average a 9.0 million unit annual rate in the fourth quarter of 1980 and 9.6 million units in 1981. Small cars are selling well, reports an area dealer, but sales of larger cars are sluggish despite improved mileage ratings. Capacity of domestic small cars is limited currently by engine and transmission production. An area dealer reports that 1980 models

are closing out satisfactorily, but not at the expense of 1981 models. Ohio consumers continue to benefit from a \$600 average savings on select new models as a result of the temporary tax cut, manufacturers' rebates and the temporary price freeze.

Housing

Loan commitments are weaker than last month, and larger-than-seasonal declines are expected in December, January and February, according to several S&L officials. Mortgage lending rates, which rose further in recent weeks, range from 13.5 percent to 14.5 percent and are expected to reach 15 percent soon, according to an Economist for a regional FHLB in the District. However, rates are already close to a point of shutting off demand, with loan applications in November falling behind last month's pace. Deposit flows have weakened, but even large inflows are unlikely to cause mortgage rates to differ from other long-term rates, according to an S&L official, as more S&L operate like mortgage brokers. Consequently, affordability of mortgages is an increasing problem. An area builder reports housing starts are down drastically and the volume of shoppers is now beginning to fall substantially.

Banking

Business and consumer loans continue to be weak, according to several district bankers, but lending rates continue to rise. A bank economist, however, cites uncertainty and declining real income in the local economy as more important factors in discouraging borrowers than higher interest rates. Auto loans may not pick up much for another six months because of a usual lag in recovery in local economies, according to a banker. Also, usury ceilings tied to the discount rate have made auto loans unprofitable in Pennsylvania. Business loan demand from large national firms is stronger than from smaller

local firms, partly because large firms have substituted short-term financing for long-term until bond markets turn around, according to a bank economist. Interest rates are expected to continue under upward pressure in the near-term, according to several economists, because financial markets anticipate further tightening actions by the system.

FIFTH DISTRICT - RICHMOND

There is little indication of any significant changes in the level of business activity in the Fifth District over the past month. In the manufacturing sector shipments and new orders increased, on balance, but only very slightly. Backlogs of orders and inventories declined somewhat. Among retailers there were some gains as total sales and relative sales of big tickets rose slightly. There is little evidence of any broad recovery in consumer durables, however. Employment around the District held steady on balance. Prices continue to rise across a broad front. The view that business activity generally will improve over the next six months gained adherents over the last month.

Consumer Spending

Despite continued resistance to prevailing prices most retailers surveyed report a pickup in total sales over the month. Apparel items seem characteristic, with consumers responding enthusiastically to price cuts. There are also reports of small gains in sales of big ticket items but overall sales of durables, particularly furniture, television sets, and radios, continue to lag. There are isolated reports of increased activity in more practical appliances such as washing machines and refrigerators. Auto sales vary widely from area to area, ranging from severely depressed to moderately robust. Reports on housing sales range from "no activity" to moderate.

The Manufacturing Sector

Activity in the manufacturing sector, even within individual industries, has been mixed in recent weeks. On balance, shipments and the volume of new orders were up narrowly. Backlogs of orders and inventories are down from last month. Stocks of both materials and finished goods were worked down leaving

manufacturers, as a group, more comfortable with current levels. Employment and the length of the average workweek apparently declined slightly during October. Current plant and equipment capacity remains somewhat above desired levels.

Economic Outlook

Survey respondents are becoming increasingly optimistic about the prospects for business activity over the next six months. A majority of respondents now expect the level of activity nationally and in their own firms to improve while about half expect improvement in their respective market areas. Despite this optimism about the direction of change over the next two quarters there is little support around the District for the view that the level of activity will soon reach what would be considered normal levels. Only moderate gains are expected over the next year.

Agriculture

The serious impact of 1980's drought on farmers' financial and credit conditions is pointed up more and more as the harvest season progresses. With farm income significantly lower, loan repayment rates in the third quarter were down sharply from both the previous quarter and a year earlier, while renewals or extensions were substantially higher. Farm loan demand continued to be considerably weaker than usual. Bank supplies of farm loan funds were up from both the summer quarter and year-ago levels, however. Interest rates on farm loans were up slightly, and collateral requirements were much stiffer.

The Financial Sector

Consumer borrowing has picked up in recent weeks. Year-to-year gains are now considerably higher than in most recent months. The feeling, however, is that overall borrowing has not yet reached what would be considered normal

levels. Despite holding recent gains in some localities mortgage lending activity continues quiet. Many lenders have become more restrictive in their lending practices in expectation of slowing deposit growth. Recent interest rate increases have caused some lenders to fear disintermediation in favor of money market funds should rates rise much further. For the most part, however, such effects have not been felt to date. Our directors in the banking and thrift industries find personal bankruptcies in their markets rising in line with recent national patterns.

SIXTH DISTRICT--ATLANTA

Economic activity has been "better than expected" recently in the district. Merchants are optimistic about Christmas sales, and industrial concerns are lengthening their workweeks and recalling workers as orders have picked up. Business men are concerned, however, that the rapidly escalating cost of money may forestall a strong recovery. Recent increased weakness in housing markets lends substance to their fears.

Consumer Spending and Inventories

Retail sales contacts indicate sales about even with or up slightly from last year at this time. Apparel sales, which had been sluggish, picked up, and appliance sales have strengthened, especially microwave ovens. Home furnishings remain a weak area. Although many customers are burdened with debt and requests for payment extensions are still common, there was a report of a large department store soliciting new customers for the store's credit card. Merchants are building stocks in anticipation of strong holiday sales and are determined to move their inventory even if strong pre-Christmas promotions are required.

New car sales are holding up, particularly x-cars and k-cars, but there is dealer concern about rising interest rates. Good sales in northern Alabama were attributed to customers rushing to get the 1980 models still in stock. Relatively strong demand for mid-size and large used cars reflects buyer resistance to the prices of the 1981 models. Many buyers are paying cash and are more willing to draw down or borrow against savings rather than pay the high conventional finance.

Financial and Construction

Mortgage lending is beginning to weaken due to rapidly rising interest rates. Commitments are slowing and speculative builders are being squeezed. In Atlanta, savings and loan associations reported that increasing interest rates are dampening applications. Many potential home buyers are being forced out of the market by the 14 percent mortgage rate now common throughout the region. Existing homeowners are choosing to stay with their low mortgage rates rather than "trade up." Corporate transferees provide the bulk of sales in some areas. Builders are reportedly reducing outlays by acquiring smaller lots and cutting back on square footage and other amenities. A builder of large homes reports a recent slowing of unit sales. One very large savings and loan association suggested that it would be out of the fixed rate mortgage business in the near future, reflecting a growing trend toward renegotiable and variable rate mortgages.

In general, not much optimism can be found about the real estate and home construction industries. Nonresidential is doing well in comparison, with several large office building projects announced recently. New Orleans, in particular, is quite strong.

Employment and Industry

Most industrial contacts note a feeling of optimism due to the results of the presidential election. Defense spending is expected to increase, affecting many industries in the district. The lengthening of the factory workweek and reopenings after partial shutdowns of numerous plants indicate that industries are moving back toward full production. Workers are being recalled by steel, textile, and equipment manufacturers. Oil support companies are bolstering the economy in south Mississippi, and in Louisiana,

the petrochemical industry is still expanding. Industrial orders posted gains over the last month.

Recent statistics indicate that Florida attracted more investment in the first six months of 1980 than for all of 1979. Local option tax breaks are expected to benefit industry-hungry north Florida communities, which in the past have had little to offer to compete with tax incentives offered by bordering Alabama and Georgia. Alabama's liberal program offers property tax exemptions for as long as 40 years and easy-to-obtain revenue bond financing.

Georgia has topped the \$1 billion mark in new and expanding manufacturing investment in 1980. Pratt and Whitney aircraft has recently announced plans to build a \$100 million plant in Columbus, Georgia, to produce parts for its civilian and military engines. Plans call for a major expansion and upgrading of the state docks at the port of mobile, following a record year of tonnage handled.

Ground was recently broken for the only world's fair scheduled for the 1980s. It will be held in Knoxville, Tennessee, from May through October of 1982. The theme of the fair is "Energy turns the World." Financing for the World's fair will come from private sources.

Agriculture

Crop production estimates were lowered again in the southeast, reflecting the drought's severe impact. Prices of cotton, tobacco, and vegetables (crops of great significance to this region) declined from September's levels. The Florida citrus Corp., however, exceeded growers' expectations. Grain prices were higher. Most livestock prices declined from a month ago.

SEVENTH DISTRICT - CHICAGO

Summary. Activity in the Seventh District shows mixed trends, but remains depressed overall, especially in contrast to the nation. Reaction to the election was very favorable on the part of management. But sharply higher interest rates are causing great uneasiness. Price inflation has accelerated, partly because of rising labor costs. Retail sales have improved somewhat, but sales of autos and trucks have been disappointing. Airline traffic is sharply lower. Producer equipment output is declining. Steel demand has improved further. Housing remains bleak. The financial position of farmers has improved, and farmland values are on the uptrend again.

Reaction to election. Business and financial executives seem to be almost unanimous in their enthusiasm over the extent of the conservative shift registered in last week's election, unmatched since 1952. They realize that any policy changes will take time to implement, but anticipate less onerous administration by regulators and less antagonism toward the profit system, which should encourage risk taking.

Prices. Wholesale prices are rising at a faster pace again. Utility rates are about 20 percent above last year, but are still deemed inadequate. The CTA might raise transit fares in Chicago from 60 to 85 cents at year end, and to \$1 next June. Airline fares are sharply higher.

Labor costs. Labor organizations, which now include many municipal workers, display an unswerving militancy in contract negotiations despite widespread layoffs, especially toward attempts of management to change work rules to improve productivity. The GM-UAW pact of September 1979 was valued

at 34 percent over three years, assuming an 8 percent annual CPI rise, much less than has occurred. The GM formula set the pattern for other major industries. In several recent instances managements at various district plants have told workers covered by national labor contracts that labor costs are about 25 percent less at competing plants in the South. Some or all of the jobs at these plants are in jeopardy. Higher energy costs in the North are also an adverse factor.

Retail sales were somewhat improved in October, with seasonal merchandise aided by colder-than-normal weather. Retailers are said to have ordered cautiously for the Christmas season, which will not begin in earnest until the second half of November. Some retailers insist that last year's federal bankruptcy law must be revised because of growing abuse. "Slow pay" problems on professional bills have increased demands for cash payments and improved business for bill collectors. Many established fixed-price retailers are said to be ready to "deal" with customers to meet competition. Manufacturers of riding mowers, RVs, outboard motors, and other luxury goods are holding production at a very low level.

Autos and trucks. Sales of autos and trucks have been somewhat disappointing thus far in the model year. Various assembly plants are being closed periodically for a week or more, including the plant where Chrysler assembles its smallest compacts, which were in short supply in mid-1979. Heavy truck demand appears to have stabilized and is expected to rebound in 1981. Indefinite layoffs in the auto industry have dropped from over 250,000 to 191,000, but little further improvement is expected.

Airline travel. Airline passenger miles in October were down about 11 percent from last year. Traffic was down 17 percent for the largest

airline, partly because of the stimulus of half-fare coupons last year. With increases totaling 26 percent since June, standard air fares are now 40 percent above last year, an unprecedented development. Another 6 percent boost is set for later this month. Higher fares are a major factor depressing both business and pleasure travel.

Capital goods. Order backlogs for most producer equipment continue to decline. New orders are weak. Some analysts expect the producer goods downturn to persist past mid-1981. Some of the largest construction equipment plants are shut down temporarily. A revival in demand for construction equipment depends on housing. Orders received by a producer of capital goods components have increased for two months, reflecting needs for replacement and maintenance.

Steel. Bookings of a leading steel company are running at 80 percent of capacity, with sheet products leading. Shipments will continue at an improved level through year end, but will remain well below last year's peak. Substantial price increases are being posted. A hot strip mill, closed last May after demand suddenly dried up, has been reopened. Steel companies producing oil country goods are planning increases in capacity, because current facilities are running at full capacity--a unique situation for the various product groupings.

Housing. Residential construction and transactions are very weak throughout the district. In the first nine months single-family permits in the Chicago area were 66 percent below last year and 84 percent below 1978. Multi-family permits were off somewhat less. Sales of existing homes were down 33 percent from last year, and 41 percent from 1978. Mortgage rates have risen further to the 14-15 percent range, but few loans are being

negotiated. (One large Chicago S&L stopped making loans on November 5.) Some S&Ls are offering only variable rate mortgages. Many home builders, and some mortgage bankers, have ceased operations, at least temporarily. A leading producer of building materials is raising its forecast of housing starts in 1981 to 1.45 million. This is based on (1) growing evidence that the housing stock is inadequate, and (2) an expected decline in the basic mortgage rate to the 12-13 percent range.

Agriculture. Rebounds in commodity prices and farm income prospects in recent months are credited with sparking a rise in farmland values in the district, up 5 percent in the third quarter, and enough to wipe out the decline of the first half. Farm loan demand remains soft despite a marked improvement in availability of loans. Deposits at rural banks have increased and loan repayments have accelerated as farmers increased cash marketings. Transportation problems are not nearly as significant as last year, because of smaller crops and an increase in the number of hopper cars. Purchases of farm implements have increased, but only moderately, and not for all types.

EIGHTH DISTRICT - ST. LOUIS

Economic activity improved moderately in recent weeks according to Eighth District businessmen, several of whom expressed confidence that the worst is over and that a slow recovery is likely in 1981. Although consumer spending in nominal terms is expanding, it does not appear to be increasing as rapidly as inflation. Inventories are generally lean and in line with sales. Sales gains have recently occurred in manufacturing industries such as steel, automobiles, chemicals, and appliances. Although demand for capital equipment is still declining somewhat, there are indications that this sector will bottom out soon. On the negative side, home sales have become severely depressed again and mortgage loans have fallen off with the reoccurrence of sharply higher mortgage interest rates in recent months. Business and consumer loans at banks have continued to increase.

Overall, consumer spending continues to increase at a modest pace. One retail representative noted that sales were larger than anticipated for this time of year and that he was optimistic about Christmas sales. On the other hand, rural retailers in areas which were hit by severe drought conditions during the summer months report that sales are quite weak and, consequently, are cutting back on spring commitments. While auto sales have continued to improve since last spring, they remain well below levels of a year ago.

Most businessmen report that inventories are in line with current sales. Appliance inventories may be even less than desired in some cases.

The steel inventory liquidation is reportedly completed, and some planned buildup is underway. A few smaller firms report that inventories are high because they kept their work force intact during periods of weak product demand. Also, some rural retail stores in drought-stricken areas have excessive inventories because of depressed sales.

Manufacturing industries including steel, automobile, chemical, paper, and appliances registered some sales gains in recent weeks. A steel industry representative noted that the industry is in the early stages of a recovery based on modest increases in demand for steel from the consumer product sector. However, no sizable increase in steel output is anticipated until capital spending gains momentum later in the decade. Although some automobile workers have been called back to work in the St. Louis area, the industry remains relatively depressed. For example, at the 1979 peak, automobile manufacturing jobs in St. Louis totaled at nearly 30,000 compared to about 12,000 at present. A representative of a major appliance firm, noting that sales have trended up since last summer, is optimistic about continued gains.

Capital spending is still declining and manufacturers of some equipment, such as machine tools, and lubrication and welding equipment, report that previous backlogs have been depleted and that operations are now on a hand-to-mouth basis. A machine tool manufacturer reported that the worst is over. In contrast to the overall picture, expenditures on oil and natural gas equipment and military hardware remain at a high level. Arkansas, for example, reports considerable investment in the drilling of shallow oil wells which are expected to pay off in about 12 months.

Construction activity, which gained momentum in the summer months, has lost ground again. Home sales represent the most affected area and the decline here is largely blamed on the sharp rise in mortgage interest rates. Nonresidential construction, remains relatively strong. Although total volume is down, one contracting firm reported that bids are being made on a considerable number of projects and that funds for the projects are available.

Loan demand continues to increase with business and consumer installment credit being responsible for most of the gain. While mortgage interest rates have remained around 14 percent in recent weeks, banks lending rates have continued to increase and mortgage lenders generally expect increases in mortgage interest rates in the near future. One saving and loan official noted that margins have again become depressed, and he charged that competition for funds from the Federal government is responsible for the continuing high interest rates.

In the agricultural sector, lower crop yields in many areas is leading to severely depressed farm income. Harvesting and fall plantings are proceeding rapidly with generally favorable weather conditions possible. Chicken production in Arkansas is resuming normal levels after last summer's losses. Placements of broiler chickens are now running somewhat ahead of a year ago.

NINTH DISTRICT - MINNEAPOLIS

With interest rates continuing to rise, the district's recovery was sluggish in October. Although there were modest gains in merchandise and auto sales and in manufacturing production, there was no change in mining or agricultural activity and there was a sharp decline in home sales. Reflecting these lackluster economic conditions, bank lending did not increase.

Consumer Spending

Consumer spending was frugal. According to bank directors and large Minneapolis/St. Paul retailers, general merchandise sales increased modestly between September and October. Likewise, car sales accelerated modestly in October, according to regional sales offices of domestic automobile manufacturers. However, home sales, which are very sensitive to interest rates, declined as the dollar value of mortgage loan applications at Minneapolis/St. Paul area S&Ls dropped 36 percent between September and October.

Industrial Activity and Inventories

In October, industrial activity shifted to low gear. After improving adequately for three months, manufacturing production grew more slowly in October, directors reported. This slower growth, one director believes, stems from recent interest rate increases which pushed up inventory costs and caused businesses to curb their orders. While manufacturing production slowed, mining output remained below grade. In northern Minnesota and the Upper Peninsula of Michigan, iron ore shipment continued to be depressed in October, and in Montana copper mines remained shut down by a labor dispute.

Agriculture

The favorable agricultural conditions that existed in the district in September remained unblighted. Favorable weather continued into October, so crops properly matured and farmers had ideal conditions for harvesting corn, soybeans, and sunflowers. Like the weather, favorable prices continued into October. In Minneapolis, the average cash prices for corn and soybeans were unchanged between September and October, and wheat prices rose 8 percent. In St. Paul, average cash prices for cattle and hogs were close to their September levels.

Financial Developments

Because of the district's sluggish recovery, there was no advance in bank lending. Loans outstanding at Minneapolis/St. Paul area banks were essentially unchanged between September and October. Directors from outside the Minneapolis/St. Paul metropolitan area also reported no lending increases at commercial banks in their areas.

TENTH DISTRICT—KANSAS CITY

Overview. Economic activity in the Kansas City District remains sluggish. Purchasing agents report excess plant capacity and workers still on layoffs. Auto dealers report new models to be selling moderately well, but homebuilders report construction activity has slowed dramatically. Retailers report continued sluggishness in sales, although their expectations are for improvements in coming months. Corn and soybean yields are reported lower-than-normal because of drought conditions earlier this summer. Except for those regions involved in energy-related industries, both loan demand and deposit growth are reported by Tenth District banks to have been flat-to-slightly improved over the past month.

Manufacturers' Inventories and Input Prices. Purchasing agents contacted report that the growth in input prices has slowed in recent months, but that they expect renewed acceleration over the coming months. Most materials are in adequate supply and are expected to remain so throughout the winter. Most District firms are maintaining lean inventories and are ordering smaller quantities of materials than last year. Almost half the firms contacted have excess plant capacity, and still have some workers on layoff.

Automobile Sales. Automobile Dealers Associations report that the new models are selling moderately well and are expected to continue to do so in the coming months. High interest rates are inducing dealers to hold lower stocks which, along with tight manufacturer allocations, has caused some bottlenecks in the supply of some popular new models.

Homebuilding and Home Finance. Homebuilders Associations indicate that housing starts have stagnated after a brief upturn last summer. Prices

of new homes are rising only slightly and excess inventories of unsold homes have not yet developed. High interest rates are expected to curtail sales in the near future, however. Savings and Loan Associations report savings inflows to have been quite strong recently. Demand for mortgage funds has slackened considerably since mortgage rates have again risen above 12 per cent. It is feared that mortgage rates, currently at 13 to 13 1/2 per cent, may rise further.

Retail Sales and Inventories. The majority of Tenth District retailers contacted indicate nominal retail sales since August to have been only slightly better than during the same period a year ago. Current dollar sales have apparently weakened noticeably in automotive and apparel merchandise while durable goods sales have shown slight improvement in the most recent months of this year. Merchandise costs have reportedly slowed in recent months. During the August-October period, most retailers have maintained the same markup over costs as in the past, but have had difficulties maintaining profit margins at past levels because of increased expenditures for promotional advertising and promotional price cutting. Most retailers report existing merchandise inventories to be excessive, primarily because of the weakness in sales. However, inventory levels are not being significantly trimmed because sales are expected to strengthen as the Christmas season approaches.

Agriculture. Harvesting of corn and soybeans in the Tenth District has been virtually completed. Most states report lower yields on both crops, due primarily to the drought conditions earlier this summer. In many areas of excellent cropland, yields fell 10 to 12 per cent below normal years. The number of farmers not expected to be credit worthy during 1981 is about twice what is usual. However, as a result of drought and hail this summer, many area farmers are eligible for low cost emergency loans from the Farmers

Home Administration which may allow many to regain some financial stability. The winter wheat crop is in good condition throughout most of the District, although planted acreage is reported as lower-than-normal.

Banking Developments. Loan demand is reported flat-to-slightly higher at most Tenth District banks contacted this month. Exceptions are some banks in Wyoming and Oklahoma where energy-related loans continued to show significant strength. Demand for real estate loans has been mixed recently, with some bankers in Oklahoma, Wyoming, and New Mexico reporting continued moderate lending for commercial properties. Some of the banks contacted report weakening in consumer loans primarily due to automobile credit. Rural banks report slight declines in agricultural loans. All of the banks contacted have raised their prime or base lending rates within the past month. Some of the metropolitan area bankers currently have prime rates of 14 1/2 to 15 per cent, following the lead of large money center banks. Base fees at some country banks have recently increased to 16 1/2 per cent.

Deposits at Tenth District banks contacted have been flat-to-significantly higher this past month. Regions involved in energy-related industries have recorded the greatest increases. Demand deposits are particularly strong in these areas, as are large CD's and money market certificates. In other regions of the Tenth District, the growth of deposits has been flat-to-slightly higher reflecting the trends in local loan demand.

ELEVENTH DISTRICT--DALLAS

Business conditions in the Eleventh District are somewhat improved from a month ago. However, survey respondents agree that additional increases in interest rates will curtail the current expansion. The growth of department store sales is stronger this month, and car and truck sales are improving. Inventories of unsold homes are accumulating, and housing starts have slowed in response to declining sales. Total loan demand is expanding slowly, while repayments of agricultural loans remain difficult. Factory output remains mixed.

All major urban areas in the Eleventh District show renewed growth in retail sales. Price discounting and sales promotions are active as retailers strive to increase market share. While retailers are optimistic about the coming holiday sales season, they are cautious in expanding inventories, preferring to risk a loss in sales rather than accumulate excessive stocks.

Auto dealers report improved sales. The introduction of the 1981 models is said to be helping sales, although some buyers are deterred by the high sticker prices. Smaller models are selling best. Most sales are financed through auto manufacturers' credit divisions, including those of a large Datsun dealer. Inventories are adequate and closely controlled.

Housing starts continue to slide, and builders' inventories of unsold homes are rising. Still, demand remains strong as people continue to move to the Southwest. Sales of higher-priced homes remain stable although prices are softening.

Commercial construction activity in the District remains very strong, and the outlook is for continued growth in Houston and South Texas. However, a decline in bidding on new construction contracts in North Texas suggests building activity in that part of the state will slow in the future. Heavy construction and highway building continues to decline as Federal funding is curtailed.

Total loans at District banks are growing slowly. C&I loan demand continues to be buoyed by the oil and gas industry, although some is due to inventory accumulation at department stores and in auto-related industries. Permanent construction financing has been almost unavailable since life insurance companies left the commercial mortgage market. However, a few projects are still being undertaken as some banks are willing to make preferred customers interim construction loans that are unsecured by permanent financing.

Consumer credit is softening. Mortgage loan demand is strong, yet commitments continue to decline as fewer potential buyers can qualify for loans. Mortgage companies report loan volume is half of the level six weeks ago. The number of defaults is beginning to grow. FHA-VA foreclosures in Houston are up 32 percent from last year. Demand for home improvement loans is very strong, but credit card usage is flat.

Net inflows of deposits at banks and S&L's are even with last month's levels. Liabilities of S&L's continue to move toward shorter maturity certificates, and liquidity levels are as high as 13 percent.

Conditions in manufacturing remain mixed throughout the District. Sales continue to rise for electronics and suppliers to the oil and

gas industry. Drilling is at record levels, and order backlogs for new rigs exceed 12 months of production. Demand in other industries is less strong. Oil stocks and chemical inventories remain high on the Gulf Coast, but chemical shipments are rising. Lumber and wood shipments are declining from September's peak, and prices remain below the level a year ago. Manufacturers of construction equipment report a slowdown in orders in the last 30 days.

The rise in labor costs shows little sign of slowing. Wage increases throughout the District are averaging 8 to 9 percent annually. The biggest gains are in energy-related industries. A manufacturer of oil tools reports union workers negotiated a 17-percent increase in the first year of their new contract.

Agricultural conditions remain substantially unchanged from last month. Loan repayments continue to slow as crop failures are still adversely affecting farm incomes.

TWELFTH DISTRICT -- SAN FRANCISCO

The Twelfth District is still reporting signs of the continuing recession. Retail sales remain at depressed levels and no signs of growth are being anticipated. Interest rates continue to be a major source of anxiety in the region. It is feared that the rise in interest rates will have a number of adverse effects on the district. The brief recovery of the housing industry is expected to be completely stopped with mortgage rates at 14 1/2 percent and above. The lumber industry is experiencing a further reduction in demand and a number of firms are anticipating closures. Concern is also being expressed over the condition of financial institutions. With the higher interest rates and the approaching changes in the industry, lower profits are anticipated. Brighter notes are expressed over agricultural prospects and activities in oil and mineral exploration. Unemployment figures remain stable.

The volume of RETAIL SALES continues to be low and most areas are reporting little optimism for a quick recovery. Retailers are reporting sales well below last year's levels. Conservatism in new-order policies has kept inventories at low levels. Automobile sales appear to be picking up somewhat as the introduction of the 1981 line of cars has created some consumer interest. It is too early to tell if this interest is sufficient to change the fortunes of the automobile industry.

OIL AND MINERAL exploration continues to create discussion in some parts of the region. A waterflood project, costing \$3 billion, is expected to increase oil recovery in Prudhoe Bay by more than 1 billion barrels

when completed. It is reported that substantial petroleum deposits have been discovered in Beaufort Sea, next to Prudhoe Bay. The mining industries in Utah and Nevada are booming. Activity in the region has increased with the increased interest in synthetic fuels created by recently passed Congressional legislation. Changes in economic conditions of parts of the region, especially Alaska where oil revenues have allowed the State to cut and refund taxes, are being anticipated.

The AGRICULTURAL outlook at harvest time appears to be very good. Many areas are reporting large crops which will push down the prices faced by consumers. Despite the decline in prices, farmers are expecting good profit levels. Conditions for the lumber industry are reported to be bleak. With the rise in interest rates, demand for homebuilding material has come to a standstill and firms are anticipating a number of closures.

A general concern is being expressed about FINANCIAL INSTITUTIONS. An outflow of deposits has occurred with the rise in interest rates. Declining profits are being widely reported. Concern has also been expressed about the upcoming changes in banking. One respondent feared that the relaxation of rate requisitions and the enhancement of competition may increase unsound banking practices as banks attempt to attract business. Policies taken concerning NOW accounts might be able to give a good indication of future behavior.

MORTGAGE RATES in the Twelfth District are in the range of 14-1/2 percent. A few lenders are offering loans at lower rates but they tend to have stricter lending terms. Restrictions are placed on the maximum amount of the loan and loan fees are often higher at financial institutions

charging lower rates. A number of savings and loan associations have stopped offering mortgage loans.

The HOUSING market continues to be weak. The rise in interest rates has inhibited both buyers and new construction. The housing market was said to be holding up in the past months because of mortgage loan applications that were submitted in periods when the interest rate was lower. A better indication of the effect of the rise in interest rates is the number of new loan applications submitted. This number has declined sharply and a decline in housing activity is anticipated. However, the decline is not expected to be as severe as the one which occurred last March.

UNEMPLOYMENT figures remain stable. The lumber and construction industries remain well below last year's employment levels. In some areas employment in housing related industries is down by as much as 50 percent. Some farm laborers have finished their seasonal jobs and an increase in unemployment is expected. There is some concern that there will not be enough jobs in the immediate years ahead to provide employment to those entering the job market.