

CONFIDENTIAL (FR)

CURRENT ECONOMIC COMMENT BY DISTRICT

Prepared for the
Federal Open Market Committee
by the Staff

May 12, 1982

TABLE OF CONTENTS

SUMMARY	i
First District - Boston	I-1
Second District - New York	II-1
Third District - Philadelphia	III-1
Fourth District - Cleveland	IV-1
Fifth District - Richmond	V-1
Sixth District - Atlanta	VI-1
Seventh District - Chicago	VII-1
Eight District - St. Louis	VIII-1
Ninth District - Minneapolis	IX-1
Tenth District - Kansas City	X-1
Eleventh District - Dallas	XI-1
Twelfth District - San Francisco	XII-1

SUMMARY*

Overview: Economic activity in most sectors slackened further in April and early May, according to District reports. Consumer spending was generally lackluster although automobile sales picked up in a few Districts. The weakness in manufacturing became more pervasive, spreading to energy-related and high technology fields. Layoffs did not appear to slow, and capital spending continued to decline. New residential construction remained depressed, but some very modest improvements were noted in a few local housing markets. In the agricultural sector, liquidations and bankruptcies rose as farm incomes and land values continued to fall. Consumer borrowing was sluggish although commercial lending varied somewhat among Districts. In contrast to last month, none of the District reports expressed any optimism that a turnaround was at hand.

Consumer Spending: Retail sales were lackluster in most areas of the country although automobile sales picked up in a few Districts. Despite the general weakness among department stores, merchants in Boston, Philadelphia and Dallas experienced moderate gains in their overall sales. In many Districts, increased reliance on markdowns and promotional activity spurred lagging sales but put considerable pressure on profit margins. Only retailers in Cleveland, St. Louis and Kansas City reported excessive inventories. As for automobile sales, strong response to rebates and special financing plans was noted in St. Louis and Minneapolis but such measures did little to stimulate sales in San Francisco.

* Prepared at the Federal Reserve Bank of New York.

Manufacturing Activity: Throughout most of the country, conditions worsened in the manufacturing sector, with weakness spreading even to industries which had been weathering the recession well. In many Districts, already distressed industries deteriorated further, including steel, machine tools, building materials, and textiles. The weakness spread to other, previously strong industries which had bolstered the economies of several Districts. Conditions softened in such high technology industries as computers and telecommunications equipment, according to the Boston, Atlanta, and Minneapolis reports. Orders for oil production equipment dropped sharply in Dallas, Atlanta, and Chicago. Cutbacks in state and local government dampened purchases by the public sector. Layoffs and reduced hours were widespread, and many Districts reported several plant shutdowns, both temporary and permanent. Capital spending was being postponed or cancelled. Inventories were generally lean, although manufacturers in Richmond still viewed stocks as excessive.

Construction: New residential construction was uniformly described as depressed, although modest improvements were noted in a few local housing markets. Demand for luxury cooperative apartments remained high in Manhattan and housing sales showed some strength in other parts of New York City. In Dallas, housing sales and new starts regained year-ago levels, but the slight upturn in new housing starts in San Francisco--February had marked a post-World War II low--was offset by further declines in the sales of new homes. Creative financing was cited as providing some support to sales in a number of Districts. In the nonresidential sector, construction activity remained strong in a few urban centers, but San Francisco reported the cancellations of several commercial projects. Some softening was evident in New York's previously buoyant office rental market.

Agriculture: Conditions in the agricultural sector remain generally grim, especially in the midwest and California. In California, heavy rains impeded the Spring plantings, according to the San Francisco report. With crop prices having fallen to low levels, crop farmers throughout the country are caught in a squeeze of high interest charges and low income. As a result, land prices have fallen sharply, and farmers have had difficulty in paying their bills. Farm foreclosures and bankruptcies have increased sharply. Livestock producers, however, have benefited from the recent rise in livestock prices which, in combination with the low crop prices, have widened their profit margins. Nevertheless, the generally bleak conditions in agriculture have strained the solvency of such related businesses as farm machinery, seed and fertilizer sales, and elevator operations according to reports from Cleveland and Minneapolis.

Finance: Consumer borrowing was generally weak, while commercial lending varied somewhat among Districts. In Philadelphia, business borrowing was slightly ahead of last year, but bankers expected loan demand to soften. Slackening in the energy sector had divergent effects on loan demand, increasing lending activity in Dallas and decreasing it in Kansas City. Flat loan demand was reported in Cleveland, St. Louis, and Minneapolis. San Francisco banks experienced a sharp rise in problem and delinquent loans as bankruptcies increased among forest products and construction industries and small firms in general.

Outlook: In contrast to last month none of the District reports expressed any optimism that a turnaround was at hand. Instead, conditions appear to have worsened and forecasts of a

recovery have been postponed until later in the year. Economists in Boston felt an upturn, albeit an "anemic" or "modest" one, would begin in the second half of the year despite deteriorating conditions in April and early May. Among manufacturers, some were looking for a pickup in business activity within the next six months, while others were less sanguine. Retailers, too, were divided with some expecting an upturn to follow the July tax cut while others, such as those in Richmond and in Kansas City, did not see any imminent upturn in sales.

As for the price outlook, there was little feel for whether the recent slowdown was cyclical or permanent. In Chicago, price discounting is more common than at any time since the 1930's and is especially prevalent in steel, nonferrous metals, building materials, paper, and transportation, though a large surge in these prices is anticipated with recovery. Similarly, in Kansas City, prices for new materials were down between 5 and 18 percent from last year but are expected to be stable or rise slightly for the rest of the year. Wage settlements not far below those of a year ago were reported by several Districts. For example some Chicago firms in depressed industries recently negotiated contracts calling for 8 to 10 percent first year wage increases.

FIRST DISTRICT - BOSTON

Economic conditions in the First District vary considerably from sector to sector. Retail sales have been stronger than expected. Department stores cite an increase in the importance of promotional activities as the most important effect of the recession. Manufacturers, on the other hand, report a pronounced decline in economic activity since the first of the year. Although the rate of decline seems to have slowed, signs of an upturn are few and far between. As production and employment levels have been cut back, a number of firms have adopted work-sharing arrangements. Reports from the banking sector range from "an excellent year" to very poor.

Retail

Retail conditions in the First District appear to be stronger than the retailers themselves expected. Although sales are not booming, dollar sales are running above last year and in some cases, ahead of department store prices. Promotional activities are reported to be increasingly important in generating sales.

Several retailers expressed surprise that the slack in the national and local economies was not having a larger effect on their sales figures. This was mentioned both by merchants with a predominance of high income customers and by those serving primarily low income consumers. A representative of a New England department store with a nationwide parent company reported that the New England sales increase was second highest of all the parent's stores. Seasonal factors, such as the timing of Easter, distort

comparisons with last year; but among those reporting, first quarter (February through April) sales were up 4 to 12 percent over the first quarter of last year.

All those contacted described inventory management as especially difficult under current business conditions, but all reported success in their ongoing inventory control efforts. Promotional activities have been an important inventory reduction tool, and several mentioned a heightened consumer response to well-advertised specials. Price reductions, they noted, increase profits proportionally less than sales.

Price increases from suppliers have not moderated as much as the CPI; but some retailers report fewer or slower increases. This slowdown will appear in retail prices with a lag, since the goods being purchased now will be sold in the fall.

Manufacturing

Signs of continuing weakness far outnumber signs of an upturn, according to First District manufacturers. In an April survey of local purchasing managers, substantially more firms reported decreases over the month than increases for production, employment, new orders and backlogs. There have been order cancellations for aircraft equipment; the airlines' financial position has suffered as the recession has reduced business travel. A manufacturer of household products, for whom the rehabilitation and remodelling business had sustained sales through 1981, has seen a sharp downturn since the first of the year; sales are not falling as rapidly as earlier in 1982 but they are still falling. A producer of energy saving capital equipment reports that firms have been postponing projects since the

first of the year; in a number of cases, firms have the resources to proceed but they are uneasy about the future. Orders for heavy capital equipment for the petro-chemical and auto industries remain depressed. The problems of the auto industry are also causing production cutbacks and layoffs among the region's machine tool makers. Some of the region's fastest growing high technology firms have begun to feel the recession; revenue growth has slowed, profit growth even more so and several of the largest have curtailed hiring.

Among the more encouraging reports was the observation by two firms that business at European plants has picked up. However, one firm described the strength in Europe as uneven, while a manufacturer of specialized industrial equipment said most of the increased demand at its European plants was from the developing nations, not Europe itself. Also encouraging were reports from a manufacturer of semi-conductors and a supplier to the semi-conductor industry that bookings have picked up in that industry.

Many firms which have reduced production and employment levels have adopted work-sharing arrangements. The most common approach has been to shut down whole plants for several weeks. A number of firms have also introduced four-day workweeks; in others, employees work for four weeks and are off the fifth. The firms which have adopted four-day weeks and rotating schedules say they have done so in order to hold onto their workforces. It is not clear whether such practices are more common now than in other recessions of comparable severity; they are certainly more common than in 1980.

Banking

Reports from the banking sector are mixed. One bank contacted was enjoying an excellent year, while another reports that loan losses are up

sharply and first quarter earnings were very disappointing. One banker noted that passbook savings deposits seem to have stabilized; while his bank was continuing to lose accounts to the money market funds, this outflow was being offset by funds from the thrifts. He did not think his was an isolated situation.

Professors Eckstein, Samuelson, Solow and Tobin were available for comment this month. Eckstein believes that the risks associated with continued high interest rates have become uncomfortably high. If rates do not decline soon on their own, the Fed will have to ease up on the monetary brake to insure that a series of cascading bankruptcies do not drag the economy into a deeper, more prolonged recession. With respect to inflation, he anticipates a reversal of food and fuel prices will soon end the days of a declining CPI. He foresees no budget agreement until after the November election, although the recent unity among Republicans is an encouraging development. Eckstein envisions a final budget including \$20-\$30 billion in tax increases and \$30-\$35 billion in expenditure reductions, yielding a 1983 deficit of about \$125 billion.

Solow expects an anemic recovery in the second half and notes that most risks are on the downside. Interest rate declines due either to a weak economy or a resolution of the budget stalemate cannot be interpreted as an easier monetary policy or as enhancing the prospects for recovery. In fact, if current monetary policy is appropriate for the current stance of fiscal policy, a move to fiscal restraint surely implies an easier monetary policy is needed. Solow argues that a budget compromise would be the most advantageous occasion to adopt a more lenient monetary policy without raising inflationary

expectations. He believes continued progress in reducing the Federal deficit would be facilitated if monetary policy were to offset the effects of fiscal restraint. He fears that, after three years of no economic growth, a stagnant economy will bring "semi-permanent" damage to the economy's productive capacity, and preclude strong capital formation and productivity growth.

Tobin also favors a shift in policy mix. Given the likelihood of high unemployment this year and next, he doubts that monetary ease would set off an economic boom that would raise inflation. Even when inflation has receded, he fears that the Fed may not tolerate a healthy recovery for fear of throwing away its victory won at such great cost.

Samuelson believes that given the prevalence of "monetarist monomania," the Fed should not respond to a budget compromise by violating its targets only slightly. The amount of stimulus gained would not be commensurate with the credibility lost. Nevertheless, he strongly urges the Fed not to abandon its role of lender of last resort if unemployment is still 10 percent by the end of the year and the economy is in real danger of a depression. He believes that high interest rates will come down sufficiently to permit a modest, if delayed, recovery in the second half of the year.

SECOND DISTRICT--NEW YORK

Economic activity in the Second District remained lackluster during April. Major retailers reported that consumer spending was weaker than expected. New residential construction continued to languish although some brokers noted a few signs of modest improvement. Nonresidential building was still brisk but there was softening in the office rental market. Widespread layoffs were noted in the manufacturing sector. Except for the defense industry, few firms experienced any increase in new orders. While the region's unemployment rate remained below the nation's, business leaders expressed growing concern that the recession would spread to more sectors of the region's economy.

Consumer Spending

Retail activity in the Second District was weak during April, as most department stores failed to meet plans which had been considered to be conservative. Business appears to be getting tougher for many retailers. One symptom is the increasingly widespread use of markdowns and promotional activity; another symptom is the greater difficulty we have had in getting retailers to return our phone calls. One retailer who works for a department store in New York City which caters to a well-to-do clientele told us that this was the "most difficult period in his memory." While apparel, housewares, and other nondurable goods were reportedly doing all right, such things as sporting goods, horticultural items, and big-ticket products were selling poorly. Despite lagging

sales, inventories at most stores were at acceptable levels. Retailers--perennial optimists that they are--remain hopeful about their prospects for the second half of the year, expecting their sales to improve in response to the July tax cut.

Construction and Real Estate Activity

Residential construction remained depressed, but there were a few signs of modest improvement in the housing market. In New York City, a broker reported that sales of existing homes in Queens increased markedly; he attributed the gains to wider acceptance of high but renegotiable interest rates. In Manhattan, a continued influx of very wealthy buyers, frequently paying cash, maintained high demand for luxury cooperative apartments. In suburban areas, a better understanding of "buy downs" was helping to bolster sales.

Nonresidential construction activity remained strong with work continuing on many new office buildings. At the same time, however, the rental market for office space has softened throughout the District, perhaps foreshadowing a future fall-off in new construction projects. In New York City, for example, landlords granted more concessions to prospective tenants, including slower escalation of rents and more structural improvements. Space available for subleasing rose significantly as firms which had been holding the space deferred expansion plans. One just-completed building had been entirely pre-leased a year ago, but almost a third of its space was again available. Outside of New York City, rents also stabilized, and in

western Connecticut, leasing during the first quarter was the lowest in five years. Respondents believed, however, that the slowdown was only temporary.

Business Activity

The District continues to weather the recession relatively well, with the region's unemployment rate holding steady in April at a level below the nation's. The manufacturing sector, however, has been deeply affected by the recession. Layoffs were widespread with only scattered recalls. Except for the defense industry, few firms reported any pickup in orders. Indeed, capital goods producers in western New York experienced further cancellations. A producer of traffic and airport lights shortened its workweek apparently because cuts in state and local spending dampened public sector demand. A list of new capital projects compiled by the New York State Department of Commerce indicated that fewer major projects are being undertaken this year than last.

Outlook

As we found last month, few respondents outside of retailing expect a general economic recovery to begin soon. Most expressed growing concern that the recession would spread to more sectors of the region's economy, including business services. The gloomiest assessment came from a business leader in western New York who did not foresee any turnaround there for another two years. Many observers were disturbed by talk of further bankruptcies in the manufacturing sector if conditions did not improve soon. Almost all respondents believed that a fall in interest rates was essential for a recovery. However, one Port Authority official

did point to a recent increase in piggyback rail traffic as a possible sign of an incipient upturn.

As for the price outlook, there was little feel for whether the recent price slowdown was cyclical or permanent. A number of respondents echoed the sentiment that, "We'd prefer to go back to the good old days when the economy was expanding even if that meant higher inflation." Wage settlements are now lower than a year ago; for example, central New York firms are projecting overall increases 1 1/2 percentage points below last year's average of 9 percent.

Financial Panel

This month we have comments from Donald Riefler (Morgan Guaranty Trust Co.), Francis Schott (Equitable Life Assurance Society) and Alfred Wojnilower (First Boston Corp.):*

Riefler: The Fed should being to modify its monetarist approach because of the poor correlation between M1 as currently defined and nominal growth in the economy. An acceptable range of "real" interest rates should be developed as a policy guide in addition to monetary targets. Federal Reserve credibility would not suffer from this adjustment.

Schott: Institutional cash flow remains severely constrained by high interest rates. Improvement in Federal budget prospects is essential, although a modest decline in rates is widely anticipated anyway because of the recession and favorable inflation figures.

* Their views of course are personal, not institutional.

Federal Reserve policy continues to be appropriate. Despite much carping over the level of interest rates and over technical points of monetary policy, responsible executives see no credible alternative to moderate restraint on the aggregates.

Wojnilower: The contraction in business activity appears to be near a bottom. Capital spending is being cut sharply but the decline in other final demand has probably ended.

Far too much is being made of the near term impact of the Budget on interest rates. The behavior of longer term interest rates over the next few months will be mainly governed by perceptions of the business outlook. It is unlikely that these perceptions will be significantly influenced by the Budget debate.

THIRD DISTRICT - PHILADELPHIA

Reports from the Third District in May continue to point to a bottoming out of the slump, but hard signs of a pickup are scarce. Manufacturers say industrial activity is flat in May, compared to a month ago, and industrial prices reflect that softness. This is the third straight month in which manufacturing activity has remained unchanged. Retail business, on the other hand, is showing some signs of life after an illness that lasted through the winter and early spring. An announcement of total recovery for the retail sector, however, is still premature. Bankers say business is mixed.

As for the outlook, Third District contacts are reasonably optimistic. Manufacturers are predicting an upturn within six months, and retail merchants expect sales to continue at their current pace through summer. Bankers are forecasting falling interest rates through the third quarter, but weakness in commercial borrowing.

MANUFACTURING

Stagnation is the keyword for Third District manufacturers in May, according to preliminary results from the most recent Business Outlook Survey. Those results agree with earlier indications that the downward slide in the local industrial sector has stopped. There are no signs yet, however, of an upturn. Two-thirds of the manufacturing executives polled this month say general business activity is unchanged from April. Specific indicators such as new orders and shipments are also flat, but producers' backlogs and delivery times have slipped marginally. Liquidation of manufacturing inventories also continues in May, especially in the durables industries. And, while two-thirds of the survey respondents say payrolls are at the same level they were a month ago, a significant number report further cuts in employment. Workings hours have been shortened fractionally as well.

Looking ahead, Outlook Survey participants continue to forecast gains. Nearly 70 percent of the respondents say the general business climate will improve

within six months; climbing new orders and shipments are projected by a similar portion. Concomitant with the expected expansion are plans to hire more workers and lengthen the workweek. Only marginal inventory building is in the picture, though, and capital spending plans are very weak for the second consecutive month.

Industrial prices in the Third District remain generally stable in May. Prices paid by manufacturers for raw materials are up only very marginally over last month, and prices received for finished goods are virtually flat. There are reports of price cuts in both categories. As for the future, survey participants think prices will pick up with the projected recovery. About half expect input costs to be higher six months from now, while a third are planning price hikes for the goods they sell.

RETAIL

Department store sales in the Philadelphia area are stronger in early May than in recent weeks. Current dollar sales volumes are reported to be running four to five percent ahead of year-ago figures, compared to only a one-to-two-percent gain for the three months ending April 30. While such a gain was expected, a good portion of it comes from aggressive promotions and price reductions, which has put continued pressure on profit margins. Area retailers say the real strength in sales comes from nondurables, especially popularly priced apparel, while hard goods continue to lag. Sluggishness in durables is attributed to consumer uncertainty about future employment and income, given the current economic environment.

Local merchants remain cautious about the coming months. There is some feeling that both the July 1 tax cut and the July Social Security increase will be used by consumers to restore liquidity and will therefore be of little help to retailers. Sales are expected to continue at about their current pace at least through midsummer. A tight rein will still be held on inventories, however, and they'll be kept at their current trim levels.

FINANCE

Third District banking business is mixed this month, according to current Redbook information. Consumer borrowing is still off substantially, by design, while reports of commercial loan activity put current business borrowing three-to-four percent ahead of the corresponding period in 1981. Business in both categories has improved from last month, when compared on a year-over-year basis. The outlook for C&I loans, though, is not optimistic. Area bankers are forecasting softening demand for business loans based on: 1) lower inventory financing requirements in coming months; 2) low levels of capacity utilization and capital spending; and 3) an expected drop in interest rates over the summer which may bring long-term corporate debt offerings off the shelf. Just how much further interest rates will have to drop to make the bond calendar perk up is open to question. At least one contact thinks they are within 100 basis points of that level.

Local bankers are currently quoting a prime rate of 16 percent, and see further cuts on the horizon. Most contacts anticipate a trough between 14 and 15.5 percent in the prime sometime in the third quarter. After that, they say, they expect a continuing hard line policy by the Fed to put upward pressure on rates again.

Deposit flows at Third District banks have pretty much worked through the usual April seasonal problems, and are now showing firmness which some bankers have termed "surprising." Demand deposits are slightly higher than they were a year ago, and savings are up sharply. Neither the new 91-day money market certificate nor the new 3 1/2 year certificate can be credited with that strength, however. Consumer response to both of those instruments has been very weak. Bankers feel that savers still prefer money market funds to the 91-day certificate, and that 3 1/2 years is too long-term for most depositors at this point.

FOURTH DISTRICT - CLEVELAND

Summary. Retail sales have flattened but retailers are reluctant to indicate the timing of recovery. Demand for capital goods continues to decline. Demand for steel may have bottomed at a very low level. Manufacturers expect inventories to decline again in May. Retail inventories have become more burdensome. Unemployment is rising as plant closings continue. Ohio farmers are in great financial difficulty. Business loans and NOW accounts were flat in early May.

Consumer Spending. Retailers generally believe that declines in sales have flattened but are reluctant to indicate the timing of recovery. Several retailers report deferring or cancelling plans to build and open new outlets over the next few years because of high interest rates and uncertain profit margins. One major retailer places the trough in consumer spending in April. He points out that declines in spending in March and April offset nearly one-half of the increase in spending that occurred between last October and February. Auto producers are not optimistic that sales will improve much until well after the scheduled tax decreases in July.

Capital Goods. Capital goods producers continue to face declining demand for their products. A manufacturer of machine tools, continuing to experience lower orders and falling backlogs, is "gearing operations down to the lower level of business anticipated in 1983." Another machine tool manufacturer recently laid off another 250 employees because of weak orders and declining backlogs. A bearing manufacturer expects second quarter orders to be 8% below first quarter, and backlogs to fall further. He anticipates some upturn in demand from auto and farm machinery producers in the second half but

no recovery before yearend in demand from railroad car and machine tool manufacturers. A major supplier of heavy-duty truck equipment reports that sales continued to decline in April and expects no recovery in heavy-duty trucks before yearend.

Steel. There are some indications that demand for steel may have stopped declining. One major producer says orders have stabilized at a very low level but expects industry shipments for the year may be as low as 70 to 75 million tons. That firms notes that "low volume and very weak prices are putting the steel industry under great financial pressure. Marginal producers probably will not survive." Another major producer, operating at 48% of capacity, says "the order book is flat." The firm expects second quarter shipments to be no better than in the first quarter, which had the lowest non-strike level of shipments in 40 years.

Inventories. A sample of manufacturers report that their inventories fell in April and will fall again in May. Most producers of primary metals and industrial machinery expect to continue to cut inventories. A producer of paint and a paper manufacturer expect to add to inventories. A petroleum company expects crude oil inventories to continue the decline that began in mid-February. Petroleum product inventories dropped sharply in the first quarter and should, on balance, decline slightly in second quarter. Bearing inventories held by producers and customers fell in first quarter, but little change is expected in the second quarter. Inventories of heavy-duty trucks were reduced substantially in March but the further decline in sales in April has deferred the completion of the inventory liquidation. Automobile producers are no longer concerned about new car inventories, except on a spot basis.

Retail inventories of department-store-type goods have become more burdensome because of declines in sales in March and April.

Unemployment and Plant Closings. The effects of recession continue to spread and deepen throughout the Fourth District. The April SA unemployment rate was 12.4% in Ohio and 10.7% in Pennsylvania, well above the nation's 9.4%.

Plant closings continue in the District although some have been avoided or rescinded because of worker concessions. National Steel wants to sell or close its 11,500 employee steel plant in Weirton, West Virginia and Colt Industries wants to sell or close its 4,300 employee Crucible Steel Division plant in Midland, Pennsylvania. AM International wants to close or sell its 500 employee duplicating machine parts plant in Cleveland. B. F. Goodrich recently agreed to continue operating its 2,000 employee Akron industrial products plant for 3 years in exchange for union contract concessions. GMC is closing a 1,200 employee stamping plant in Cleveland but has rescinded the planned closing of a 1,400 employee trim plant in Cleveland in exchange for union concessions.

Agriculture. The widespread nature of the recession is illustrated by the increasing plight of farmers, especially those in southwest Ohio. Many are finding it hard to obtain credit. The Ohio Department of Agriculture expects four times the usual number of Ohio farmer bankruptcies this year and expects nearly one-fourth of the state's farm machinery dealers to close or be sold. The Department also notes that a number of grain elevator operations are in financial difficulty.

Financial Institutions. Business loans and NOW accounts were flat in early May, and one banker reported more switching of deposits out of

S&L's. Two major banks report C and I loans declined during the last two weeks of April, were flat in the first few days of May, and are expected to be flat for the month. Another large bank reports that C and I loans have remained strong in recent weeks but a definite slowing in commitments will show up in reduced loans in the months ahead. Some bankers characterize much C and I activity as "distress borrowing" and "not for expansion but just to pay bills".

NOW accounts at two large commercial banks declined in the last two weeks of April and were flat or down a bit in the first week of May. One banker reports that the silent run on S&L's has been augmented in the last month by frequent instances of early withdrawal of small CD's by depositors who accept the penalty and shift funds to sometimes lower yielding certificates in commercial banks.

FIFTH DISTRICT - RICHMOND

Overview

Fifth District economic and business activity continues almost uniformly weak. There is virtually no evidence that conditions have begun to improve. District manufacturers report further declines in shipments and new orders over the past month. In addition, order backlogs, inventories, and employment are said to have fallen broadly. Retail sales activity has been essentially flat in recent weeks and remains moderately weak. Housing activity is pervasively weak. Business lending, as well as mortgage activity, is said to be generally soft, nil in some areas. Consumer lending is somewhat stronger. Most of the manufacturers surveyed expect business conditions to improve over the next two quarters. Few Richmond directors, however, expect the recession to end before fall.

The Manufacturing Sector

District manufacturers report further declines in shipments, new orders, and order backlogs since the last survey period. Materials inventories also fell while stocks of finished goods were stable. Employment and the length of the average workweek were also said to be down sharply. Reductions in manufacturing employment have spread across the District and along with the construction sector have resulted in unemployment rates above the national in some Fifth District states. In some cases current rates were topped only in 1975. Construction and automobile related industries are among the most severely affected. Layoffs and plant closings in such industries as textiles, tires, furniture, glass, building materials, and others have contributed significantly.

Despite the decline the inventories, manufacturers still view stocks as excessive and nearly half our respondents find current plant and equipment exceeding present needs. The survey further suggests that prices, including wages, have fallen, on balance, in recent weeks. Furthermore, respondents are considerably more optimistic than in recent months. Over half the manufacturers expect the level of business activity nationally, as well as in their respective markets and firms, to improve over the next six months.

Consumer Spending

Retail sales also remain generally soft. There are few signs of any pickup in activity and little expectation that any will develop over the next few months. Responses from our directors and our survey of retailers suggest that some recovery in housing is essential to a general recovery in the consumption sector. Our contacts in the financial sector indicate that although installment lending has shown some signs of life, consumers generally are paying down debt and increasing savings.

Housing and Construction

Housing remains uniformly weak and other construction sectors seem to have lost some of the buoyancy of recent months. There remains little optimism concerning the short term prospects in this sector. Richmond directors, for instance, do not now expect stronger new housing activity any time this year.

Agriculture

Farm credit conditions in the District generally remain depressed. Foreclosures on farm borrowers at the end of 1981 were reported by more than one-fifth of our banker respondents. The number of foreclosures represented a relatively small share of all farm borrowers at the respective banks, however.

In general, requests for refinancing farm loans to avoid default were greater than usual.

Credit conditions during the quarter ending March 31, 1982 were characterized by soft farm loan demand, further deterioration in the quality of farm loans, and a modest rise in interest rates. Bank funds available for lending to farmers remained at a high level--up from both the previous quarter and a year ago--but collateral requirements jumped sharply. Loan-to-deposit ratios of banks reporting averaged slightly higher than in the previous quarter but were still fractionally below a year ago.

The Outlook

The outlook can only be described as mixed. Manufacturers have become more and more optimistic in recent months. As noted, most expect conditions to have improved by late fall. Retailers on the other hand, do not seem to feel that any recovery is imminent. Richmond directors clearly believe that any recovery is still several months away, probably not before fall.

SIXTH DISTRICT - ATLANTA

Business conditions in the Sixth District are somewhat mixed at this time. Limited signs of recovery are evident in tourism and construction, but other sectors remain depressed and firms are hesitant to expand employment and inventories. Heavy industries are more depressed than in years, and industry spokespersons are not optimistic about any near-term upturn. Higher prices for calves and hogs have improved cash flow for farmers, but a high level of debt remains difficult to carry.

Consumer Spending. Reports on retail sales in the District are mixed. Big-ticket appliance sales are up noticeably in Miami and New Orleans, and home entertainment products are showing widespread strength in the District. There are reports that Easter buying of clothing was lower than last year, and wholesale buyers say consumers are very quality- and bargain-conscious. Traffic in furniture stores remains slow and the floor-covering business is poor. Retailers continue to keep a tight rein on inventories, and wholesale clothes buyers are even delaying purchases for the fall season.

Auto sales remain poor. Domestic car sales in most of the District are below year-ago levels but are stronger than foreign car sales. High interest rates still limit sales and squeeze profit margins, but dealers are hanging on. Dealer closings do not appear to be accelerating.

Financial and Construction. The behavior of loan demand is generally consistent with geographic differences in the severity of the recession. Bankers in the more depressed areas of the District told of weak demand for both consumer and business lending. By contrast, lenders in Georgia and Florida, where unemployment rates are well below the national rate, spoke of strong loan demand. A few bankers expressed concern that strong lending may be an indication of poor sales.

Residential construction is showing some sign of improvement. Permits issued to build single-family houses are up in April and early May in many areas of the District. Permits are being issued to home purchasers with cash in hand, ready to build. Realtors report a slight pickup in sales. Atlanta's "mini-boom" in sales is being supported by relocation of employees of Georgia-Pacific. Throughout the District, homes have been moved primarily with innovative financing; conventional rates are reported still too high for home buyers. Realtors feel the worst of the recession is over but remain cautious. Homebuilders remain very pessimistic, since sales are almost entirely existing homes and new home inventories remain high. Throughout the District, vacancy rates for both residential and commercial dwellings have increased.

Employment and Industry. Unemployment rates continued to drift upward in the District in March as employment contracted and the labor force continued to expand. The six-state average jobless rate reached 9.9 percent in March, 0.7 percent higher than the February rate and 0.8 percent higher than the national rate in March. Except for services and paper, job declines are still prevalent in many industries.

Alabama has been particularly hard hit, with an unemployment rate of 13.6 percent. The situation there may deteriorate even more as U. S. Steel Corporation is considering a temporary shutdown of its operations near Birmingham because of declining orders and competition from imported steel. The plant, Birmingham's largest, has 3,200 people currently at work with close to 7,000 of its May 1980 work force on layoff. The state's important textile and forest product firms have hundreds of workers on layoff due to the weakness in construction and auto sales.

Layoffs have surfaced even in industries thought to be insulated from the recession. In Louisiana, orders for oil-field structures and drilling rigs, in particular, have taken a nose dive, prompting layoffs in the oil rig and equipment fabricating business. Phosphate mining has slowed noticeably in central Florida. Recent closing of

a phosphate-based fertilizer plant in Savannah, Georgia, is indicative of weakness in the farming area. The region's largest manufacturer of satellite and telecommunications equipment has laid off workers for the first time in years. For Florida, a bright spot continues to be foreign trade. A new record was set in 1981 as the actual value of goods exported increased \$1 billion over the previous year. South Florida has contributed heavily to these exports.

The tourism industry appears to be reviving in Florida, following what was characterized as a ho-hum start to the season. Low hotel/motel occupancy rates for the month of February were reversed during March and April. Lower gasoline prices and discount air fares have stimulated travel to the state. Traffic counts are up and reports of heavy summer bookings at lodging places suggest a healthy summer for tourism. Attendance at the World's Fair in Knoxville, Tennessee, has not kept pace with projections in spite of heavy promotion. Officials predict a surge of visitors when school is out. The fair is scheduled to run for six months.

Agriculture. Rising prices of calves and hogs have somewhat brightened the agricultural picture in the Southeast; however, crop prices are not yet offering much encouragement to farmers who need increasing profits to repay large debt overhangs from prior unfavorable seasons. Many farmers owe more than their assets are worth in current markets. However, lenders are continuing to work with borrowers if there is any hope of recovery from current financial straits. Foreclosure sales of farm property have produced few bidders for either land or machinery. In most cases, lenders have purchased property at the loan value in order to prevent losses of loan principle. There have been few actual sales of farmland, and a representative market value is difficult to establish. Estimates of the decline in land value from year-ago levels range from zero to as much as 20 percent.

District Economists. District bank and business economists polled this month agree that the FOMC is on the right track and should stick to its announced policies. They believe these policies will soon result in reduced inflationary expectations and help to lower interest rates. The panel is concerned that projected budget deficits will keep interest rates high in the coming expansion and, consequently, limit private sector growth. Some panelists argue that the relatively high current interest rates for this stage of the recession are causing more severe liquidations and pressure on profit margins than usual. They say the liquidations are, in turn, providing earlier-than-usual inflation relief.

SEVENTH DISTRICT--CHICAGO

Summary. Seventh District economic activity remains very weak. The expected, or hoped for, spring upturn has not developed. At best the decline is leveling off, but further softening is evident in producer goods. There is no evidence that a significant pickup will occur soon. Consumers are very cautious. Deepening financial problems are causing corporate executives to push austerity programs. Purchasing managers reported continuing declines in output, employment, inventories, and orders in April, but the rate of decline apparently moderated. Inventories are said to be low, but are being reduced further. Price cutting is widespread. The high value of the dollar is aiding foreign competitors. Construction activity probably will set a postwar low this year. Farmers are encouraged by the rise in livestock prices, but income prospects, overall, remain poor and farmland values have been declining since last fall.

A Dismal Profile. The region of the Seventh District has been in a depressed state for three years. In March, total payroll employment in the five-state area was 7 percent below March 1979. Nationally, despite the recent decline, it was still up 2 percent. Manufacturing employment was down 19 percent in the district, compared to a decline of 8 percent for the nation. The situation appears to have worsened somewhat since March, with further layoffs in a wide variety of activities. Weakness is pervasive, not only in manufacturing, but in construction, transportation, trade, agriculture, and state and local government. Michigan has the most serious employment problem, but all district states compare unfavorably with the nation.

Austerity Programs. With hopes fading for an early recovery, many individuals, businesses, farmers, and state and local governments are retrenching on new outlays and commitments. Businesses are cutting staff, reducing compensation (when possible), paring inventories, and postponing or cancelling capital expenditure projects. Less essential outlays on travel, public relations, market research, advertising and sales promotion are under very close scrutiny. Under the circumstances, the danger of a cumulative downturn is greater than at any time since World War II.

Bankruptcies and Closings. Financial stress is reflected in a wave of bankruptcies and closings of factories and retail establishments. Chapter 11 filings have shot up. In one jurisdiction there were more Chapter 11 cases in March than in all of 1981. Bankruptcies of smaller manufacturers, retailers, truckers, real estate companies, and farm-related enterprises are most frequent. Some larger firms, technically insolvent, are operating under special arrangements with creditors or are being kept afloat by parent companies. Many stores have been closed either because of bankruptcy or unprofitable results. Permanent plant closings are also frequent, especially manufacturers who have lost supplier contracts with OEM's. One result of shutdowns is the large volume of forced sales of relatively new vehicles and other equipment.

Inflation. A dramatic shift in the inflation picture has occurred since the start of the year. Price discounting is more common than at any time since the 1930's, and is especially prevalent in steel, nonferrous metals, building materials, paper, and transportation--rail, truck, and air. Many observers believe that discounted prices will surge once sales improve. The drop in petroleum prices is believed to have ended. Prices of medical and

utility services, and many manufactured goods, continue to rise at a rapid pace. Nevertheless, assumptions on the long-term inflation rate have been scaled back from 10 percent to 8 percent or less.

Employment. Layoffs, either temporary, indefinite, or permanent continue not only in manufacturing but also in trade, transportation, real estate, and finance--particularly S & L's. Facilities of state employment offices are hard pressed. Many workers are exhausting unemployment benefits.

Labor Concessions. Negotiations for concessions on labor contracts continue. In the main, these agreements have merely slowed increases in total compensation. Some new labor agreements call for first-year wage boosts in the 8-10 percent range, even in depressed industries. The auto industry seems to have reconciled itself to high domestic labor costs, now \$21 per hour, with a view to substantially increasing foreign sourcing of major components, including engines.

Motor Vehicles. Small truck sales rose sharply in the first quarter, partly reflecting a favorable reception for new domestic compact trucks. Demand for heavy trucks remains very weak. Total car sales slipped back in April after major rebate programs expired. Nevertheless, output of cars will rise substantially in the second quarter because inventories were reduced in the first quarter. Truck output is above last year.

Capital Expenditures. The outlook for producer durables continues to deteriorate. Various manufacturers report orders off 30 to 60 percent from last year's mediocre levels, with backlogs "evaporating". Support for "safe harbor" leasing is very strong. Among the weakest lines are equipment for railroads, trucklines, construction, and agriculture. Machine tools and oil

and gas field items are declining rapidly. The largest locomotive plant, scheduled to close, will remain open due to orders booked recently.

Steel. Demand for steel has been much weaker than expected, especially for heavy products. Estimates for 1982 shipments have been reduced further. Some facilities are being closed.

State and Local Governments. Virtually all state and local governments are seeking to prevent or reduce large prospective budget deficits. Efforts to reduce employee compensation, or moderate increases, are meeting strong union opposition. Various programs are being scaled down and facilities are being closed.

Construction. Home sales and residential construction remain at a very low ebb. Housing permits in the Chicago area were under 800 in the first quarter, compared to 2,300 a year ago, and over 7,000 in the first quarter of 1978. Creative financing is helping to move some existing properties but is not boosting new construction.

Agriculture. Although the district agricultural picture remains bleak, livestock producers are enjoying modest profits due to higher prices and low feed costs. Capital expenditures by farmers remain weak overall, especially for machinery, but orders for grain storage facilities have improved recently. Our latest quarterly survey of agricultural banks shows district land values down 4.5 percent since the beginning of the year, and down 7.5 percent since last September. The number of real estate transactions is down and foreclosures and forced sales account for a small, but much higher-than-normal, share of the total. Field work, after a somewhat late start, has progressed rapidly.

EIGHTH DISTRICT - ST. LOUIS

During April and early May, business activity in the St. Louis District was virtually unchanged. Most respondents feel that the economy is at or near the trough of the recession. Retailers and most manufacturers continue to experience weak sales. Although respondents anticipate a recovery beginning within the next few months, they expect that the early upswing will be sluggish. Yet, with a gradual acceleration of economic activity and with the pace of inflation receding, they expect the expansion to be sustained for a relatively long period.

Major department stores in St. Louis and smaller merchants scattered across the District report continued weak sales in April and early May, particularly for durable goods. Farm equipment dealers have made few sales, although farmers continue to buy large amounts of herbicides. Retail sales picked up temporarily following the severe winter, and some store managers, anticipating a prolonged upswing in activity, increased orders from suppliers. Since sales soon fell again, these excessive inventories must now be worked off. Some retailers noted that consumers are saving at a greater rate than in the past several years, reflecting the high interest rates available to savers and a lower expected rate of inflation.

One bright spot is that automobile dealers have increased car sales in the past two months--a continuation of the uptrend reported in the last redbook. Despite the gains, automobile sales remain relatively depressed. In St. Louis, the demand for mid-sized cars has strengthened,

whereas in some smaller cities, the greatest improvement has been in larger- and smaller-sized rather than medium-sized cars. Financing purchases with below-market 12.8 percent loans and the granting of direct rebates have helped car sales.

Industrial activity has been unchanged on balance since March. Defense procurement remains vigorous, while sales by food producers were about normal. Orders remain at relatively depressed levels at firms producing consumer durables, chemicals, aluminum, wood products, industrial equipment and refined oil products. Because of the continued economic weakness and expectations of only a gradual recovery, several medium-to-large producers have trimmed capital spending plans in the past two months.

Most manufacturers have held inventories at or near desired levels. In order to avoid inventory accumulation, they have maintained production at relatively low levels. A major chemical company operated at 67 percent of capacity in April, about the same rate as in the first quarter. One specialty food processor closed down its operations for two days to avoid inventory expansion--an unusual development in this industry.

Employment has remained relatively stable since March. Several firms, however, have imposed a "freeze" on new hiring, allowing employment to decline with attrition. On the other hand, a few smaller firms, especially in the service industries, have increased their work forces. Several firms noted that employee dedication had improved, and absenteeism had declined recently.

Throughout the region, residential home sales continue to be weak. Some dealers claim that the market is virtually dead; one real estate agency that had been reporting to us went out of business in April. According to most respondents, high interest rates, high home prices and a low level of economic activity are major factors contributing to the lack of sales.

Commercial banks, both large and small, have experienced only minor changes in loans and deposits since March. Deposits and loans at most savings and loan associations have also changed little. Most savings and loans are still operating at a loss, estimated at an annual rate of 1 to 2 percent of total mortgage loans outstanding. This negative margin is rapidly eating into their capital. Five associations located in the St. Louis area are currently being liquidated.

Weather conditions have been favorable for land preparation and planting in the District. Also, relatively wide feeding margins are benefiting most livestock producers. Farmers, however, are registering complaints about high interest rates and low grain prices.

NINTH DISTRICT - MINNEAPOLIS

Whatever the harbingers of economic recovery are indicating at the national level, we see scant evidence of a turn-around in the Ninth District so far. Instead of recovering this spring as we had earlier hoped, the Ninth District economy has continued to atrophy. The decline in farm income persisted, and this has hurt farm-related businesses and agricultural land values. High technology manufacturing, which had been an important source of strength until recently, started slowing, and other industrial activity continued to decline. In addition, general merchandise and home sales remained poor in April. Reflecting these weaknesses was the continuing softness in bank lending. The only bright spots in the District this spring were some signs that agricultural conditions may be improving, and a continued strengthening in motor vehicle sales.

Agricultural Conditions

Agricultural income slipped further this spring. For the third consecutive year, over 50 percent of district bankers responding to our spring Agricultural Credit Conditions Survey indicated that their areas' farm incomes were down from a year ago. During each of the last three years this percentage has increased, and this spring 94 percent reported falling farm incomes.

The persistent decline in farm income has strained farm-related businesses. Rural bankers and farm suppliers indicate that many farmers are having difficulty paying their bills which, in turn, has hurt the liquidity of farm-related businesses. Consequently, many of these businesses have either reduced credit to farmers or eliminated it. Also, with incomes so low, many

farmers have cut back sharply on their purchases of feed, seed, fertilizer, and machinery, which could reduce output next fall. This combination of falling sales and a liquidity squeeze has driven some farm-related firms out of business. The number of Small Business Administration (SBA) loans in South Dakota liquidated in March, for example, was up 50 percent from a year ago. An SBA official attributes a substantial part of the increase to failures of farm implement dealers.

Reduced farm income has also, not suprisingly, eroded the value of the farmer's principal asset--land. Conversation with bankers, Federal Land Bank officials, and real estate agents indicate that farm land values throughout the district are down, or at best unchanged from a year ago. An informal survey of farm real estate agents in west central Minnesota, for example, indicated that area's farm land prices were down 5 to 10 percent in the last year. This is in marked contrast to the previous five years when the average annual increase in Minnesota farm land values was about 13 percent. Farmers may be having trouble getting even the currently asked prices, for our contacts indicate that very little farm land is actually changing hands.

Despite these poor conditions, area bankers expect that most farmers will survive, and there are some indications that the situation may be improving, at least for livestock producers. A reduction in hog output began to boost livestock prices late last year, and these prices are expected to continue to rise into the summer. Combined with low feed costs, these higher prices should provide at least some temporary relief. Also, the possibility of a rapid cut in dairy price supports, which according to some Minnesota and Wisconsin bankers would have caught many dairy farmers unprepared, apparently has been postponed.

Glimmerings of near-term optimism are fainter for crop growers. Despite recent strengthening in grain and soybean prices due to seasonal factors and concern over Argentina's ability to export, these prices remain low. The best that can be said is that grain export shipments have recently firmed a bit and that the sign-up for the U.S. Department of Agriculture's set-aside acreage program was high, with farmers at least contemplating reduced seeding on 80 percent of the eligible acreage. The set-aside program will probably not reduce grain output much. However, farmers who continue to participate in the program will be able to receive government loans in return for storing their crop next fall, thereby guaranteeing their cash-flow and strengthening fall prices.

Industrial Activity

High technology manufacturing has been an important prop to the district economy during the past three years when farm income was shrinking. Very recently, this group began to wobble too. Declining orders for computers and peripheral equipment caused one manufacturer in the Minneapolis/St. Paul area (24,000 employees) to encourage its employees to take unpaid vacations. A spokesman for another computer manufacturer in the Twin Cities (10,500 workers) states that his firm's business has recently "stalled." Also, a local manufacturer of super computers recently cut the number of computers it plans to ship this year from 16 to 14.

Along with the very recent let-up in high technology manufacturing, the decline in other manufacturing, as reported in recent Redbooks, has continued. Firms producing temperature controls, packaging materials, industrial filters, and mobile homes have all recently reported reduced orders and pro-

duction. Confirming these declines, a spokesperson for a large Minneapolis/St. Paul trucking firm states that recent shipments from manufacturers have been falling.

Mining and forest products also continue in the doldrums. Shutdown iron mining operations are going to be resumed later than expected; and, except for paper mills, forest product operations have been cut back further at both ends of the district.

Consumer Spending

Consumer spending has continued to slip. Two large Minneapolis/St. Paul retailers report weak sales in April as they have for several months. Also, after home sales showed some signs of reviving in February and early March, the president of the Greater Minneapolis Board of Realtors indicates that they leveled off in April and were down 42 percent from a year ago.

In contrast to home sales, motor vehicle sales have continued their earlier improvement into April. Regional sales managers for two large domestic motor vehicle manufacturers attribute this improvement to rising light truck sales. Their companies' small truck sales in the district in April were up about 15 percent from a year ago, and they are even worried about the sufficiency of current inventories. Auto sales, they report, have been substantially less strong.

Financial Developments

The slippage in the district's real economy is reflected in continued weakness in bank lending. According to a Minneapolis/St. Paul banker, loan demand at Twin Cities banks remained sluggish in April. Outside the Twin

Cities, 47 percent of the bankers responding to our spring Agricultural Credit Conditions Survey termed their loan-to-deposit ratios as "lower than desired." This was the highest percentage of respondents expressing this view in the 17-year history of the survey.

TENTH DISTRICT—KANSAS CITY

Overview. Business conditions remain generally weak in the Tenth District, although pockets of optimism and strength do exist. Recent weakness in retail sales is expected to continue into the fourth quarter, although automobile dealers evince some guarded optimism. Industrial materials prices are still falling, but are expected to stabilize soon. Manufacturers are attempting to trim their inventories further, and retail inventories are also viewed as somewhat excessive. Although there are some signs of improved profitability in livestock production, agricultural loans are being put under increasing scrutiny. Total loan demand at commercial banks remains flat, with some weakness evident in energy sector loans.

Retail Trade. Except in the energy producing areas of the Tenth District, retailers report small declines in nominal sales in the first four months of 1982 relative to the same time period in 1981. In the areas where energy development has spurred the economy, sales were reported as 10-20 percent higher than last year. Throughout the District, sales slowed in March and April. Weakness was apparent in appliance, lawn and garden, and home improvement merchandise. Due to recent slack sales, most retailers have excess inventory which has put some downward pressure on profit margins. Retailers, however, report merchandise, utility, and labor costs have stabilized so profits may be down less than might have been expected. Most retailers indicate that they expect the weakness in sales to continue through the first two months of the fourth quarter. In those areas where energy production is important, however, retailers expect sales to continue to be well over 1981 levels.

Automobile Dealers Associations. Automobile dealers in the Tenth District are more optimistic than they were six weeks ago, in spite of continued slow sales and high interest rates. With the exception of Oklahoma's 9 percent increase, Tenth District automobile sales remain depressed, in some areas down 5 to 10 percent from a year ago. Inventories have now stabilized at low levels. Dealers intimate a sense of guarded optimism, convinced of the existence of pent-up demand.

Purchasing Agents. Almost all purchasing agents report prices for major new materials ranging from 5 percent to 18 percent lower than a year ago. Stable or slightly increasing prices are expected for the remainder of the year. Input availability is not a problem within the Tenth District, with the exception of the heavy metal industries where 2-3 weeks lead times are being experienced. Most of the companies contacted are continuing to trim inventories.

Agriculture. Many Tenth District bankers are currently increasing their loan loss provisions. It is estimated that an average of 30 percent of agricultural loans and 20 percent of nonagricultural loans are receiving careful scrutiny on a monthly basis by commercial bankers within the District. Some of the more careful monitoring by bankers is due to increased numbers of customers with adequate cash flow but insufficient collateral. Banks and Production Credit Associations report a slight increase in voluntary business liquidations as a last resort method of preserving remaining assets prior to forced bankruptcy.

District bankers report some damage to the winter wheat crop as a result of the recent freeze, but not nearly as severe as last year's frost

damage. Recent improvement in cattle prices has had a significant impact on the profitability of cattle producers in the first quarter of 1982. Hog production likewise is showing signs of improved profitability.

Banking Developments. Reported loan demand is generally characterized as flat throughout the Tenth District. The energy sector, previously a source of strength, continues to weaken resulting in slower demand for commercial and industrial loans and commercial construction financing. The recently announced shutdown of the Exxon shale oil project is seen as having an adverse effect on the economy and financial institutions in western Colorado. More generally, several bankers express concern over the profitability of energy loans in light of the decline in world oil prices. Consumer, residential construction, and agricultural lending activity continue to be depressed.

Much of the deposit activity in recent weeks is seen as tax-related or seasonal in nature. However, some banks report an increase in receivables and inventory financing. In addition, several banks indicate that customers are continuing to transfer funds out of thrift institutions into small time and savings deposits at banks.

ELEVENTH DISTRICT--DALLAS

The repercussions of the drop in crude oil prices have weakened the Eleventh District economy despite encouraging signs from the housing markets and a few other sectors. Housing sales and starts are still increasing, as are business loans and department store sales. And, despite the April decline in U.S. auto sales, District auto sales appear to have remained at March levels. Nevertheless, declines in oil and gas drilling and low production at oil refineries and petrochemical plants have reduced orders in the steel, fabricated metal, and oil well servicing industries. Total employment is declining and the unemployment rate is on the rise.

Oil field related activity continues to decline despite some evidence that crude oil prices are beginning to rise again. The number of drilling rigs operating in the District states has fallen 22.5 percent since the peak in mid-December. At 2,305 rigs, the count is currently 200 units less than a year ago. Oil well completions have fallen as well. Hence, oil well servicing contracts are also down.

The slow downward trend in manufacturing output spread to oil industry suppliers. While oil refining and petrochemical production stagnated, the production of machinery and equipment used in these industries fell. Steel firms, already hurt by declines in other industries, saw demand drop further as new orders for oil field equipment dried up. Demand for steel products by the commercial construction industry, however, held firm. Orders in the electronics industry have risen due to increased defense spending and greater demand for semiconductors. Apparel production remains at low levels.

Residential Construction continues to show minor improvement. New housing starts and sales are up to roughly the same levels as a year ago, when the housing industry entered the current slump. In addition, new mortgage commitments at Texas S & L's are increasing, although they are still below year-ago levels. Condominium sales are slowing. Condominium starts are approximately the same as they were in March. Apartment construction appears to be picking up from the slow growth of last fall.

The pace of commercial construction remains steady at a high rate. The majority of the activity is still in office building construction where it is estimated that there are enough projects already started to sustain the industry for two years. Announcements of new projects, however, remain below last year's heady pace.

Domestic auto sales have not changed much, but their product mix has. GMAC financing (12.8 percent) has increased GM sales at the expense of other domestic and imported autos. Large model domestics continue to sell well even though gasoline prices are showing signs of reversing their decline. Inventories have begun to creep upward in response to slipping sales at non-GM dealers. No significant change in sales is expected for the remainder of the month.

Lending activity at commercial banks has picked up. The percentage increase in the dollar value of loans for the year to date is well ahead of the average increase of the past five years. Loans to the petrochemical and refining industries show major increases since January.

Real estate loans are trending upward. The decline in consumer loans has not yet abated. Construction loans, while showing a net decline since January, are well ahead of last year. Total deposits have increased since March as a result of strong growth in time deposits.

Department store sales have increased moderately. However, soft lines have sold below expectations due to unseasonably cool weather. Big ticket items continue to move slowly. Retail sales along the Mexican border still suffer from the peso's February devaluation, and probably will for some time. Department stores there are scaling down future purchases and trying to work off their swollen inventories.

The unemployment rate for Texas rose to a seasonally adjusted 6.5 percent in April, from 5.9 percent in March. A moderate increase in employment since February was overshadowed by a large increase in the number of people looking for work. The rise in unemployment is attributed mainly to layoffs in manufacturing, although in-migration of unemployed workers from the industrial Midwest was also a clear contributor.

Farm liquidations are numerous as high operating costs, coupled with low prices, keep farm incomes down. Increases in farmers' equity from inflation in land values have slowed. In some parts of the District, land values are deflating. The result is that farmers are increasingly unable to borrow to finance current production.

TWELFTH DISTRICT - SAN FRANCISCO

The Twelfth District economic recession does not appear to have ended. The general pattern of economic activity since the last report has continued to be downward. Consumer spending during the Easter season was disappointing, with sales in April just about matching the year-ago pace, representing a decline in real terms. In the manufacturing and mining sectors, a number of industries are undergoing a new wave of production cutbacks. The only notable improvement in sales has occurred in electronic equipment. Homebuilding has picked up recently, but the continued decline in home sales suggests the recovery may not be sustained. Storms have inflicted serious damage on the California agriculture industry, and crop prices generally remain below the level of a year ago. Bank credit growth at Twelfth District banks has slowed considerably since February, as the weakness in the regional economy and the heavy debt burden of borrowers has stifled business loan demand.

Consumer Spending

Respondants report that retail sales throughout the Twelfth District continue to be slow. Department store sales in April apparently just about matched the dollar volume of a year-ago, representing a decline in real terms. Easter business picked up seasonally but was disappointing relative to the level of a year-earlier. Not even price discounts and heavy advertising campaigns were effective in significantly spurring sales. Sales of durable goods, such as furniture and appliances, continue to be particularly weak, due both to the housing slump and the reluctance of consumers to incur new debt. Sales of nondurable goods have been holding up better, but even grocery stores have been feeling the effects of recession. An increasing number of small retail outlets are going out of

business. Sales of new automobiles declined in April, despite offers of below-market financing and free warranty programs.

Manufacturing and Mining

Twelfth District manufacturing and mining industries have been undergoing a new wave of layoffs and production cutbacks in recent weeks. While employment in the lumber segment of the forest products industry has stabilized, the paper industry continues to cut back production. Layoffs also continue in the construction, commercial aircraft, and metals industries. Due to numerous commercial aircraft order cancellations, the Boeing Company in Seattle now plans to layoff at least 8,000 workers by year-end, instead of the 5,000 announced earlier. Partly as a result of these cutbacks, Pacific Northwest aluminum producers also are cutting production further. Other regional metals industries are sinking deeper into recession as a result of depressed demand from the national automobile, appliance and construction industries. In mid-April, Phelps Dodge Corporation closed nearly all of its copper mines and smelters in Arizona and New Mexico for an extended period, laying off 3,800 workers. Declining world oil prices also are forcing cutbacks in such energy programs as oil drilling, oil shale development and coal production. The only significant improvement in sales is occurring in the electronic equipment manufacturing industry, both as a result of a pickup in commercial orders and continued strength in defense business.

Construction and Real Estate

The Twelfth District is finally experiencing a pickup in homebuilding. But regional housing starts had dropped to a post-World War II low in February, so residential construction remains extremely depressed. Moreover, sales of new homes have continued to drop, and since inventories of unsold homes are still high, it is doubtful the recovery can be

sustained until those inventories are worked off. California realtors are concerned that the Supreme Court may rule that home buyers in the state may no longer assume existing low-interest loans. Such a ruling would further reduce sales of older homes. Meanwhile, the slump in sales is further eroding selling prices for both new and older single-family homes and condominiums. Nonresidential construction activity also is slowing substantially. Developers are cancelling some planned commercial projects, such as shopping centers and office buildings. Due to soaring costs, utilities in Washington have been forced to terminate construction of three nuclear plants.

Agriculture

Recent storms in California have inflicted serious damage on the agriculture industry. Heavy rains and flooding prevented planting of an entire strawberry crop, delayed planting of such important crops as cotton, rice and tomatoes, and drowned much of the State's asparagus crop. Experts fear that the roots of a wide variety of fruit and nut trees may rot due to flooding. Thus, even if crop prices rise this year, California farmers could experience a decline in receipts. In other Twelfth District agricultural areas, crop prospects are favorable. The increase in livestock prices in recent months also is a welcome improvement. Nevertheless, district bankers express growing concern over the heavy debt position of the agricultural sector generally.

Financial Institutions

Bank credit growth in the Twelfth District has slowed considerably since February. In particular, the pace of business lending has levelled off, as the weakness in the region's economy and the heavy debt position of borrowers has stifled loan demand across nearly all industries. Twelfth District banks report a sharp increase in business loan delinquencies over

the past few months and expect loan losses to be double those reported in the last normal year of 1980. Bankruptcies are up in the forest products and construction industries, as well as for small firms generally. Furthermore, cash-flow problems that are generated by firms' inability to collect receivables on time are becoming much more widespread throughout the business community. Because of this increase in delinquencies and problem loans, as well as continued pressure on net interest margins, many banks in this region are undertaking programs to bolster earnings by cutting noninterest costs.