

CONFIDENTIAL (FR)

CURRENT ECONOMIC COMMENT BY DISTRICT

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Federal Open Market Committee
by the Staff

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SUMMARY*

Overview: Economic activity in most Districts showed some signs of improvement except in the manufacturing sector. Weakness in manufacturing remained pervasive with some further layoffs reported and, for the most part, little or no upturn in new orders. Consumer spending strengthened in November but several Districts noted sluggish early-December sales. Housing sales and starts registered gains in most regions although the oversupply of office space kept nonresidential construction generally slow. In several agricultural areas a further decline in farm income and land values overshadowed the few bright spots that appeared. Commercial bank lending was essentially flat in most reporting Districts. The general outlook ranges from a slight upturn during the next six months to little pickup until late 1983.

Consumer Spending

Since the last report, consumer expenditures posted some gains on both a month-to-month and year-over-year basis, helped in part by promotional activity. Nonetheless, no real exuberance was displayed. Auto sales picked up in several areas in response to lower finance charges but these lower rates are scheduled to end soon. With regard to the overall outlook for retail sales during the holiday season, the most optimistic report was from Boston ("solid but unspectacular"). Several Districts experienced good consumer buying immediately after Thanksgiving but sluggish sales thereafter. One factor cited was the trend in recent years of a shift in sales to the end of the holiday season. Inventories were generally in line though one District reported that inventories

* Prepared at the Federal Reserve Bank of New York.

overall were high. The San Francisco and Atlanta Banks noted relatively strong tourist demand at areas in Hawaii, Oregon and Florida.

Manufacturing and Mining Activity

The manufacturing and mining sectors continued to languish throughout the nation. Although a few Districts observed scattered signs of improvement, most reported that shipments and new orders remained stagnant or declined further in a broad range of industries.

San Francisco, Minneapolis, and Chicago reported that timber mills, iron mines, and producers of steel, industrial equipment, and castings were operating at half capacity or less. In Cleveland, manufacturers of steel mill and other industrial equipment were hurt by the cancellation of customers' capital expansion plans. Boston and New York expressed some concern for future bankruptcies in manufacturing if sales did not turn up soon. Even the business of high technology firms slackened in some areas. In many industries, widespread cost-cutting measures continued, including layoffs, shorter workweeks, and longer-than-usual Christmas shutdowns. Despite the pervasive sense of sluggishness, however, a few bright spots emerged. In Richmond, sales of textile firms increased significantly, and in St. Louis, food processors noted a slight improvement. Several Districts indicated that suppliers of building materials and selected home furnishings were beginning to feel a pickup from the increased activity in the residential construction sector. Defense contractors were still doing well.

Construction and Real Estate

The housing market improved in many parts of the country. A few Districts even experienced substantial gains. St. Louis, for example, reported that new home sales were greater this November than in any other November in recent years. In Kansas City, increased activity reduced new home inventories to an all-time low, and led to a significant increase in housing starts. These improvements in the residential real estate market were largely attributed to the decline in interest rates and to stable or lower home prices. The office market, however, continued weak in most areas of the country due to a glut of existing office space from overbuilding and decreased demand. Chicago and San Francisco were especially hard hit, whereas New York and Richmond reported modest strengthening in some areas of their Districts. These latter two Districts, along with Dallas, also noted a slight pick-up in industrial construction activity.

Agriculture

In general the agricultural sector continued to experience low net income resulting from depressed prices and little or no decline in overall costs. Grain, corn, and soybean farmers saw only a small chance of profit from the 1982 crops and Dallas beef producers were preparing cattle for slaughter rather than for breeding because of unfavorable economic conditions. Some farmers, however, were doing well. For example, prices were up and the cost of feed held steady or declined for Minneapolis and St. Louis hog producers, and good crop yields were expected to bring a profitable year for Atlanta cotton growers. The downtrend in the price of farmland continued in areas such as the

Richmond District where, in addition, farm business failures were still above normal. In the Northwest the timber industry remained depressed due to low domestic and foreign demand.

Finance

Commercial bank lending was essentially flat in most reporting districts. In Minneapolis and Philadelphia corporate lending was down as businesses turned to the bond market, but consumer borrowing strengthened. In Kansas City, however, the reverse occurred: corporate loans increased while consumer loans were flat. Deposit flows improved somewhat at most commercial banks and at some thrift institutions.

Outlook

In many Districts, a number of signs pointed to somewhat brighter prospects for consumer spending and construction. Retailers were cautiously optimistic that recent gains would continue into the new year. While the outlook for commercial construction remained weak, homebuilders were hopeful that their modest pickup would accelerate. As for manufacturing, there was no consensus on how soon the advances in retail and construction activity would result in increased production. Several Districts did note that orders of a few firms were beginning to improve. But manufacturers in many Districts saw little chance of a general upturn before the second half of 1983 or even early 1984, and many have turned more pessimistic because the recovery has been so slow in coming. Inventories in manufacturing are lean in most regions and when business activity does turn up, production should rise quickly to meet the higher demand.

FIRST DISTRICT - BOSTON

Economic conditions in the First District are much the same as they were last month. Retailers continue to experience relatively good sales growth and look forward to a "solid" Christmas season. Retail inventories are generally satisfactory. Among the manufacturers contacted, most of whom produce capital goods, orders are flat to down and no recovery is expected until the second half of 1983 or later. Firms are using combinations of wage freezes, reduced hours, plant shutdowns and layoffs to bring down costs. Among the few positive developments was a report that sales of hardware for new and remodelled homes have picked up. Also suggestive of a recovery in housing was a report by a banking director that his bank did more mortgage business in the month of October than in any previous month.

Retail

Most retailers contacted in the First District reported "high single digit" sales growth in November compared to a weak November last year. Those with branches or associated stores elsewhere in the nation said sales were much stronger in New England than in the Midwest or Sunbelt regions. In some local stores durables seem to be selling better than soft goods. The merchants expect solid but unspectacular Christmas sales.

One of the area's major department stores experienced a sales increase of 9.2 percent over November 1981. This growth was attributed to the strength of the New England economy and the store's moderate - upper income customer base. A discount chain with 9.6 percent sales growth in

New England encountered sales declines in their Midwest and Southeast stores. The growth in New England was especially strong in hard goods; kerosene heaters were very popular. Both chains claimed that unseasonably warm weather had reduced sales of cold weather-related goods.

On the whole, inventories were reported to be at satisfactory levels. The two department store chains had "excessive" inventories last year; this year they are keeping stocks tighter but flexible. A mail order outdoor specialty firm and a pet store chain have increased inventories well above last year to improve customer service and encourage impulse holiday buying.

Several of the merchants contacted said that sales results so far are consistent with the trend over the last few years for Christmas sales to occur closer and closer to the end of the month. They also expressed concern that heroic promotional efforts would be required once the snowballing effect of holiday purchasing ends.

Manufacturing

For most of the manufacturers contacted, order rates are unchanged or declining. The Redbook group includes firms in such high technology industries as computers, telecommunications equipment and control instruments, as well as manufacturers of machine tools and specialized industrial machinery. Neither the high tech firms nor firms from more traditional capital goods industries expect a significant pickup in their own operations until the second half of 1983 or the early part of 1984. However, one machine tool maker said that if present conditions persist for another six months, many firms will go out of business and the capacity of the domestic machine tool industry will be permanently reduced. This

sentiment was repeated by a bearings manufacturer, who also pointed out that while book prices for bearings are rising, large buyers are negotiating discounts of 20-30 percent. All the firms contacted are trying to bring inventories and employment levels into line with current orders with combinations of layoffs, wage freezes, reductions in hours, and Christmas shutdowns. The high tech firms, which fared relatively well earlier in the recession, seem to be relying more on wage adjustments and Christmas shutdowns.

While reports from the manufacturing sector were generally discouraging, there were a few positive developments. Orders were up for hardware used in building and remodelling residential housing. Orders were also up for machinery to make circuit boards. Products which save money, for example, energy efficient lighting, and which increase productivity, for example, office automation equipment, continue to sell well. The defense business is strong.

Professors Eckstein, Samuelson, and Houthakker were available for comment this month. All agree that the economy is still weak and that the recovery is not yet assured. They all predict that some sort of recovery will begin soon. However, they differ in their assessment of the probability of recovery and what the Fed should do to help the economy turn the corner.

Eckstein was the most pessimistic of the three. He believes that before it is over the slide in business fixed investment will be the worst since 1931. His confidence in a consumer-led recovery has diminished because he foresees no growth this quarter and little growth next quarter in real disposable income. His pessimism about next quarter is partially

attributable to scheduled increases in excise taxes and the social security tax base and the proposed hike in gasoline taxes to finance public works. He also feels the inventory-sales ratio is too high for this stage of the business cycle.

Given his uncertainty about the recovery, Eckstein strongly urges the Fed to do everything in its power to bring interest rates down at least to the point where the prime rate is 9 percent. When asked about the current search for a reliable aggregate he exclaimed "aggregates, shmaggregates!" He'd like Congress to help out by accelerating the 1983 tax cut, but he doesn't think it is politically feasible.

Samuelson believes that the economy will probably turn the corner if the Fed continues its "slight departure from narrow monetarism to ease nominal and real interest rates." In his opinion, such a policy would not regenerate inflationary expectations or damage the Fed's credibility. However, because he thinks that further increases in the 1983 deficit would rekindle such expectations, he is opposed to short-term temporary jobs programs at this time.

Houthakker believes that, in light of recent improvements in housing and autos and the continued improvement in inflation, the economy will not deteriorate further and a recovery will take place in early 1983. He urges the Fed not to "pump up" the money supply to accelerate this process. If it did, renewed inflation would push interest rates back up, plunging the economy back into a recession. He thinks that setting of growth targets for business loans is a promising idea that merits further consideration. He is encouraged by Secretary Regan's proposal for a new international monetary conference. He favors less flexibility in exchange

rates and believes that many of our economic problems in the 1970s are attributable to the breakdown of the Bretton Woods agreement.

SECOND DISTRICT—NEW YORK

In recent weeks the Second District economy showed a few signs of improvement, but the manufacturing sector remained depressed. Promotions sparked early holiday shopping in the District and resulted in a further strengthening of retail sales. Declining mortgage rates produced a modest rise in home sales, and builders were cautiously optimistic about further growth. Recent developments in the nonresidential real estate market were mixed, but some improvement did occur on balance. In manufacturing, however, business leaders saw no pickup and reported increasing pessimism about the short-run outlook.

Consumer Spending

Promotional efforts spurred early holiday shopping in the District, and pushed year-over-year gains in November above those of earlier months. This strength was expected to continue through the holiday season. The eastern region in general met or exceeded sales plans for those national retailers contacted, while sales in much of the rest of the country continued to lag behind. Apparel, cosmetics, housewares, and consumer electronics were all reported moving well. Seasonal increases in employment matched year ago levels for most stores, and inventories were generally in line with planned sales. Retailers who had experienced a poor fall season expected business to be difficult again in 1983, but those with better sales in September and October looked forward to further gains in the new year.

Construction and Real Estate Activity

The residential construction market showed additional signs of life during November though the rise in new home sales was modest. Moderately priced homes geared to first-time homebuyers sold well. The existing home market also experienced a pickup in sales activity. Declining mortgage rates were cited as a major factor in the sale of both new and existing homes. As a result of the renewed interest on the part of actual and potential buyers, builder optimism increased though some expressed concern that interest rates might rise again because of high credit demand.

The nonresidential real estate market also improved but demand for space continued weak in many areas of the District. Activity and planning by office developers increased in midtown New York City even as the downtown market remained soft. The pattern was also mixed in the suburbs: leasing activity was up in New Jersey and new construction occurred in Westchester and Long Island, while in Connecticut the slow pace of previous months persisted. Industrial construction remained depressed throughout the District, although some pickup was reported on Long Island.

Business Activity

The manufacturing sector continued to be very weak except for the relatively healthy high technology and defense industries. Overall sales remained poor in industries ranging from metal fabricating to furniture. Many companies were finding it difficult to maintain steady production. At a few concerns, however, orders were bolstered by a unique product line or the closure of a competitor. Cost-cutting measures continued, including layoffs and the spreading out

of pay increases over longer periods of time. Shutdowns for Christmas were expected to be longer than usual. Scattered recalls of workers occurred only in response to specific orders and therefore were viewed as temporary. Although the recent drop in interest rates eased liquidity problems somewhat, several companies were thought to be bordering on insolvency and in need of buyers to bail them out. The nonmanufacturing sector still has not suffered a severe downturn, with some expansion continuing in the financial and service industries.

Outlook

The outlook for retailing and construction brightened, but our manufacturing contacts reported a deepening pessimism about the future. When the rate of deterioration slowed in September, these same contacts expressed a "glimmer of hope" that an upturn would begin within a couple of months. Since then, the recovery has proven elusive and that glimmer has disappeared. If demand should pick up, however, companies will be able to increase production quickly since inventories, except for cars, have been reduced to very low levels. One of our respondents cited a lack of a coherent policy at the national level as the source of the pervasive gloom.

Financial Panel

This month we have comments from Donald Maude (Merrill Lynch), Donald Riefler (Morgan Guaranty Trust), and Francis Schott (Equitable Life Assurance Society):*

Maude: A sustained economic recovery cannot get under way unless interest rates are brought down further. However, the Fed is running out of leeway for bringing down these rates by pushing down the funds rate and the discount rate. The credibility issue is growing and

* Their views of course are personal, not institutional.

will become more real once the markets see signs of economic recovery. To bring rates down in a credible fashion, the Fed should quantify publicly to the markets the magnitude of precautionary balance building that has bloated M-1 over the past year, go back to shift adjusting other checkable deposits and come up with 1983 M-1 targets more realistic with trend changes in velocity and M-2 targets that net out the bloating of interest-crediting to those components earning market rates of interest.

Riefler: There is a real danger that the specter of higher interest costs that may be incurred by banks in competing for deposits in new DIDC authorized accounts will slow banks' willingness to reduce lending rates. This in turn may delay the rebound in consumer spending that would be normal at this stage of the business cycle.

Schott: Signs of revival in housing and automobiles and improved cash flow at thrifts and life insurance companies raise the question whether the Fed has done enough to stimulate recovery. An evaluation period may be appropriate. Nevertheless the number and extent of trouble situations domestically and internationally suggest that the indirect assistance of a further easing of credit conditions may well be advisable.

THIRD DISTRICT - PHILADELPHIA

Indications from the Third District are mixed in December. Activity in the industrial sector declined fractionally from November levels and manufacturing prices reflect that slump. Retailers say spending has risen slightly since the last Redbook but Christmas sales are still slow. Loan activity is mixed at area banks, but deposit flows are healthy. Most Third District business contacts are projecting some improvement in economic conditions over the next six months. Manufacturing executives are looking for increased activity by June but remain cautious nonetheless. Department store sales are expected to show modest gains, although the 1982 holiday season will be below average. Bankers are forecasting some gains for commercial and consumer lending in the first half of 1982.

MANUFACTURING

Third District manufacturing activity has resumed its downward slide in December, according to respondents to the most recent Business Outlook Survey. Specifically, shipments are down at over one-third of area plants and new orders fared only slightly better. Although there has been further tightening of industrial stock levels recently, there are some signs that inventory run-down has abated somewhat. Setbacks for labor, on the other hand, continue with no apparent moderation. Reports of reduced payrolls and shortened working hours are as prevalent now as they were in November.

Survey participants remain optimistic in their projections of industrial recovery over the next six months. Local manufacturers' outlooks have, in fact, brightened a little in December, in spite of the continuing slump. Respondents are expecting a strong push in new orders that will rebuild backlogs and allow employers to expand both payrolls and the average workweek by June. Fractional additions to

inventories are forecast, as well. There are few plans for increases in plant and equipment expenditures, however.

Industrial prices also show further softening in December. Prices of finished goods have been cut again and input costs have not changed from their November levels. Prices are expected to start climbing again between now and June, coincident with the projected rebound in activity.

RETAIL

December sales at Third District department stores are building slowly as the holiday buying season ends its second week, but area sales volume is still fairly soft overall, according to retail contacts. Current dollar sales are ranging only 3 percent to 4 percent ahead of last year; real gains are slim at best. Sales of Christmas related items, while pretty much in line with merchants' expectations, are considerably below past holiday experiences. Ten days of unseasonably warm weather following Thanksgiving put a damper on holiday shopping spirit and thus kept the lid on spending. In addition, local store officials say the Philadelphia retail market has become exceptionally tough over the last two years as economic conditions deteriorated. Seasonal sales are heavily dependent on promotions and price discounting, often at the expense of full price sales. As a result, merchants are starting their big holiday pushes earlier and more forcefully. Recently, one local retailer extended an 18-hour "one-day-only" sale to three days in an effort to encourage spending.

Retailers predict that sales growth will remain slow but steady throughout the holiday season. Contacts believe that shoppers are watching their dollars closely though, and that the usual late season surge may be relatively minor. An extra shopping day on the retail calendar this year will help a little, but sales gains for the season and the year as a whole should remain in the 3 percent to 4 percent range. Projections for

1983 show more of the same for retail sales. Next June's current dollar sales volume will be 4 percent to 6 percent ahead on a year-over-year basis, according to merchants' forecasts.

The pickup in sales, though small, has helped bring inventories more in line. Stock levels are lean but generally in "good shape" and comparable to levels of a year ago. Industry representatives say they will keep stocks in check until the sales outlook improves.

FINANCE

Third District banking contacts report mixed loan activity in December. Commercial loan demand, as expected, has softened even more since the last Redbook. Chiefly responsible is the move toward the corporate bond market. Distress borrowing has faded somewhat, as well. As a result, overall C&I loan volume is now running only barely above last December. On the other hand, lower interest rates have made retail loans more attractive. Activity in consumer loans has increased since November, but, for the most part, volume still trails year-ago levels. One contact noted that some consumer loan dollars were being diverted away from automobile loans to new leasing arrangements because customers have been unwilling to make large auto downpayments.

Forecasts of loan activity over the next six months are mixed but point to some improvement. Bankers agree that further retail loan growth is likely, especially if rates drop further. Projections for commercial lending range from flat activity, if economic recovery stalls, to a modest upswing if business conditions improve.

Third District bankers are quoting a prime rate of 11.50 percent, down from 12 percent a month ago. The slide in the prime has slowed recently and caused many local seers to revise their outlooks for interest rates. A trough for the prime of around

11 percent is forecast for early 1983 and any movement in the next six months is likely to be "slow and modest."

Deposit flows are very strong again this month. Demand deposits have improved since November and are now running 3 percent to 4 percent ahead of a year ago. Time deposits gained strength as well, with unexpectedly robust growth in the 7 to 31-day time deposits leading the way. One reason cited for this burst of activity is that dollars intended for the new money market deposit accounts are being held in the 7 to 31-day accounts temporarily, until MMDAs are offered on December 14th. Bankers have high hopes for the MMDA, and expect to attract a significant amount of deposits away from the money market funds.

FOURTH DISTRICT - CLEVELAND

Summary. Economic conditions and the outlook in the Fourth District remain dismal. Unemployment is high and rising. Early December retail sales are sluggish. Little near-term improvement is seen for the automobile industry. The steel industry is in desperate condition. Survey results and leading indicators point to further contraction of manufacturing. House construction is showing only a little improvement. On the bright side, scattered indicators of disinflation continue.

Labor Market Conditions. Unemployment continues high and rising. The November unemployment rate was 14.2 percent (sa) in Ohio and 12.1 percent in Pennsylvania. The District's eleven major SMSA's unemployment rates (nsa) in October ranged from 8.9 percent in Columbus to 19.7 percent in Youngstown, and averaged 3.2 percentage points above the national rate. The unemployment rate has reached 21 percent in Lorain County, adjacent to Cleveland, as shipbuilding, automobile and steel industries have stagnated. The United Mine Workers union reports only 40 percent of active members in Ohio are working.

Consumer Spending. Two major department store chains in the midwest report Christmas season sales are moderate to sluggish so far, perhaps because of unusually warm weather. Both expect real sales this season about 1 percent above the year-ago level. One chain reports inventories are somewhat high and expects it will take a record amount of price promotions to achieve their forecast; the other says inventories are smaller than usual and promotions won't be as aggressive as last year. Both expect sales volume to be concentrated closer to Christmas than in previous years because of a secular

trend in that direction and because unseasonably warm weather has delayed sales of apparel. One chain expects real PCE to rise 4% (saar) this quarter from last and, assuming a continuation of automobile purchase incentives, to rise 2 1/2% in the first quarter.

Automobiles. Automobile inventory adjustment appears near completion but a near-term sales reduction is expected by industry economists. November sales were better than expected by one major producer, who believes some of the sales were borrowed from next quarter. The firm projects import and domestic sales at 7.4 million units (saar) next quarter, unless all domestic producers were to give sales incentives on 1983 models, in which case sales might reach 8.0 million. Current sales are divided about evenly between 1982 and 1983 models. Inventory will still be a little too high at yearend. The firm sees no change in inventory next quarter, and industry production will be only slightly above fourth quarter levels. Employee recalls to produce certain models will be offset by temporary layoffs from other model production facilities, so there will be little net increase in employment next quarter.

Another major automobile producer expects December sales will drop about 8 percent from November, partly because fewer of the popular 1982 models are left. First quarter sales will be down slightly from this quarter, as sales incentives terminate at year-end. Production will rise somewhat next quarter to build inventories for second quarter sales, but seasonally adjusted, inventories will be flat. Some employees will be called back next quarter.

Manufacturing. Manufacturing activity continues to contract, although less rapidly than earlier in the year. A survey of purchasing managers reveals further reductions in inventories of raw materials, supplies, and

finished goods. A record percentage of firms are purchasing production materials on a hand-to-mouth basis. The survey shows new orders, production, and employment continue to decline. A diversified producer of parts for cars, trucks, and materials handling equipment reports his orders are weak because many customers are cancelling capital expansion plans. Orders for heavy trucks are the lowest since 1967. He expects no upturn in his business before 1983:IVQ. A producer of consumable equipment for the mining industry sees no sign of an upturn in orders. This bank's survey of Fourth District manufacturers shows December declines in new orders, shipments, backlogs, inventories, and employment, although the declines are expected to be somewhat smaller than in November. Indexes of leading indicators point to further decline in Pittsburgh but a bottoming in Cleveland. An index of leading indicators for the Pittsburgh area registered its 17th consecutive monthly decline in October, while the index for the Cleveland area has been advancing erratically and in September stood 2.5 percent above its April low.

Steel. The steel industry is in severe distress. A major steel producer reports further declines in shipments, inventories, orders and employment. Fourth quarter shipments are expected to be less than 13 million tons for the industry, 29 percent below the depressed year-ago level, and orders received so far give no indication of first quarter improvement. Another major producer describes the market as "unbelievably weak," and expects further drops in shipments and employment. The firm is operating at 20 percent of capacity, with only one of twelve blast furnaces in operation, and is no longer certain of survival. The firm projects industry losses larger this quarter than last because shipments and transaction prices are lower. Steel mills are reducing inventories to generate cash as working

capital continues to erode. Several firms plan to liquidate inventories, draw down lines of credit, and sell off assets to delay bankruptcy while waiting for economic recovery. Survival of some producers is contingent on economic recovery and strengthening of steel demand by mid-1983. Another firm reports stocks of oil country pipe are still high. Steel producers have sharply reduced capital expenditure plans, hurting steel mill equipment producers, who see no upturn in their sales before 1984.

Construction. A major builder of houses forecasts national housing starts of 1.3 million units in 1983, up from about 1.1 million this year. However, builders see a slower recovery in this District, where there are scattered reports of mild increases in house construction. In the Cleveland area, bankruptcies among contractors and building-material suppliers in 1982 are up 36 percent from last year, and will account for one-third of total corporate bankruptcies.

Prices. Scattered indicators of disinflation continue. Retailers in Cleveland are offering unusually extensive pre-Christmas price reductions. Some Teamster Union locals in Cleveland have been bidding against each other with wage concessions to obtain employment, but steelworker union local presidents recently rejected concession adjustments to the current labor contract. Industrial vendors are reported to be offering deep discounts to obtain orders. A survey of purchasing managers reveals more price declines than increases, while a survey of manufacturers predicts prices they pay will not change from November to December.

FIFTH DISTRICT - RICHMOND

Overview

Recent economic and business activity in Fifth District could best be described as flat. On balance, manufacturing activity showed little change over the past month, although within the sector substantial differences persist among industries. Shipments and new orders were essentially flat, overall, and manufacturer's inventories were down slightly, as was employment. Retailing showed much the same pattern with total sales, relative sales of big ticket items, and inventories all holding at month earlier levels. There appear to be significant differences among areas and among product categories, however. According to some reports, housing sales and construction have been picking up, perhaps substantially. Expectations are more positive than in recent weeks as most respondents anticipate improvement in their business activity in the near term.

Manufacturing

Manufacturing activity across the district held its own over the past month, although for a number of industries current operating levels are quite low. Survey responses suggest little, if any, net change in the level of shipments, new orders, or order backlogs. This aggregate stability, however, masks some interesting developments. Chief among them is an apparent sharp rebound in the textile industry where several respondents report gains in shipments and orders. Another is the at least temporary arrest of the decline in activity among building materials and furniture manufacturers. Also, there is no discernible concentration, but only isolated reports of further declines in activity over the past month.

On the other hand, there is no evidence of any improvement on the manufacturing employment front. In fact, responses suggest further declines in

employment since the last survey. Inventories were brought down somewhat, and most respondents are now comfortable with current levels.

Consumer Spending

By all accounts the consumption sector has been a mixed bag in recent weeks. Reports vary widely from sector to sector and from locality to locality. It appears that consumer activity is picking up, but that it remains very spotty. Consumer durables other than autos continue to languish nearly everywhere. Auto sales are showing marked improvement in some areas, but continue generally weak. General merchandise lines are experiencing typical holiday buoyancy in some localities, continued softness in others.

Housing and Construction

There is growing evidence that the housing sector is in a modest upswing that began some 2-3 months ago. Permits and construction activity seem to be up generally, although this is not true everywhere. Also, sales activity is reported to be improving in many areas, significantly in some. Commercial and industrial activity is very strong in some areas and reports of improved conditions in markets for this property are becoming more widespread.

The Financial Sector

Financial institutions are generally preoccupied with the coming of the MMDA. Promotion has been moderately heavy but short on the specific terms to be offered on the accounts. Bankers seem to be expecting relatively little new money to be available to individual banks as a result of this account. Most bankers contacted expect only very modest inroads against MMFs in the near term. They see perhaps 5-10% of MMF assets as potentially available initially. Further, they expect most of the growth in MMDA in the early stages

to be at the expense of savings accounts. Most District institutions have been holding back on announcing pricing arrangements. Some advertising of specifics has been designed to capture new deposits at the outset and offers initial yields in the 12-15% range and 2-3 points above the 91 day T-Bill rate beyond that. It is too early to tell what will happen beyond the first month or two of the new deposit instrument.

Agriculture

Fifth District farm credit conditions in the third quarter of 1982 were marked by declining interest rates, continued sluggishness in farm loan demand, slow farm loan repayment rates, and an increase in requests for loan renewals and extensions. Fund availability again improved, and liquidity pressures on rural banks eased. The downturn in farmland values continued, further eroding farmers' equity positions. Moreover, the proportion of District farmers that went out of business, filed for bankruptcy, or liquidated part of their assets in the past six months was said to be much larger than normal.

SIXTH DISTRICT - ATLANTA

Late fall economic conditions in the Southeast show mixed signs. Construction continues to improve, generating optimism among construction-related manufacturers. The labor market appears to be stabilizing, and job growth in some sectors is accelerating. Optimism prevails in the travel industry. However, the profit potential for most farmers remains clouded and consumer spending has yet to show a pre-Christmas surge.

Employment and Industry. Latest available statistics on employment imply an end to the deteriorating labor market conditions reported previously, but unemployment continues to rise, and reports from industry representatives on capital spending plans indicate that the outlook for increased hiring is inauspicious. October figures indicate that declining construction employment finally may have reached bottom. Rates of decline are decelerating in several construction-related manufacturing sectors, such as lumber, wood, stone, clay, and glass. Bankruptcies among lumber-related manufacturers are reportedly on the wane, although some smaller firms may have trouble surviving until the seasonal spring upturn in housing. Except in government and trade the rate of growth in other nonmanufacturing sectors accelerated in October. Job attrition continued in most manufacturing sectors, and for the first time since World War II the District's unemployment rate reached 10.5 percent.

Our survey of firms and trade associations reveals moderate optimism among producers of construction-related goods, such as lumber and carpets, and among makers of structural steel. The latter expect government spending on defense and infrastructure to stimulate demand. However, chemical manufacturers do not share this optimism. Even in industries with capital spending plans, job creation is likely to be minimal because the impetus is cost-cutting efficiency rather than growth-related expansion.

Consumer Spending. District retailers report generally higher promotional activity compared to the same period last year. They regard immediate post-Thanksgiving consumer buying to have been good, as expected, but the subsequent lull is lasting longer than usual. Consumers are delaying holiday purchases in hopes of deep discounts in the last few weeks before Christmas. Big-ticket home furnishings continue to show improvement in some areas. Purchases of personal computers, tools, exercise equipment, small appliances, and cosmetics generally remain strong. Unseasonably warm weather has caused winter apparel to move slowly, but luxury wear has noticeably improved. In contrast to 1981, retailers are comfortable with inventory levels and are not likely to reduce prices more. Thus, profit margins are unlikely to narrow further. However, sales volume and profits will depend upon the strength of last-minute buying.

Southeastern auto sales slightly outpaced the nation's rise of 31 percent in November. Cut-rate loans are successfully stimulating sales and helping to reduce car inventories. Nevertheless, the short-term sales outlook is not bright because consumers remain troubled by rising unemployment and high real interest rates.

Construction and Finance. For the near future, realtors and thrift officials feel that the post-election November 15 drop in the FHA/VA rates may have "propped a stick" in the mortgage "window," which the pre-election slide in mortgage rates opened. Confidence in the future of housing is slowly returning as concern diminishes that political engineering occasioned earlier drops in mortgage rates. Single-family building permits show the greatest degree of recovery. Other construction sectors are faring less well, and industry representatives expect slack demand and overbuilding to keep nonresidential contract construction sluggish well into 1983.

Thrifts have been slow to accrue benefits from the housing recovery, but total loans closed by S&L's have finally begun to improve. Industry spokesmen attribute

the delayed recovery of thrifts vis-a-vis other construction indicators to increased competition from seller financing and mortgage companies and to a longer "wait and see" period by home buyers.

Tourism. Optimism, predicated upon national economic recovery, discounted airfares, and the popularity of EPCOT, is widespread among the tourist industry representatives in our survey. Preliminary, partial data and reports from those polled indicate that out-of-state travel in the upper-price brackets (air travel and lodgings) has already begun to rise. November attendance at EPCOT remains ahead of projections reportedly because Florida residents and out-of-state retirees are flocking to the new attraction. Nonetheless, several sources maintain that EPCOT's effect elsewhere in Florida is negligible or negative. Business and convention travel shows mixed signs. Contacts report that Atlanta appears to be improving while South Florida, Alabama, and Louisiana remain weak. Respondents in Georgia, Tennessee, and Alabama blame rainy weather rather than economic conditions for the more than seasonal decline in local tourism.

Agriculture. Southeastern cotton farmers are experiencing extraordinary yields in 1982. The most recent USDA projections estimate five of the six District states will enjoy record yields; Georgia should surpass its previous record by 20 percent. Yield is likely to determine profitability for most cotton producers, but some Mississippi farmers are facing losses of both their crop and income as a result of an apparent business failure. A large cotton company, already in receipt of substantial cotton, is unable to pay farmers or to return the cotton for which warehouse receipts are now held by a creditor of the company.

Most grain farmers face only a small chance of profit from the 1982 crop, notwithstanding a recent 5 percent rise in prices. At present, widespread flooding in the Mississippi valley has done little injury to crops, but potential damage is of concern,

and extension personnel in Mississippi report other weather-related damage. Recent aberrations in temperature and a surfeit of rain have adulterated the quality of the remaining soybean harvest. One estimate suggests a possible loss of 10 million bushels, valued at approximately \$52 million. Large supplies have thwarted efforts to sell low-quality beans.

Finance. A survey of a cross-section of District banks and savings and loans regarding "bridge" and Money Market Deposit Accounts (MMDA's) indicates a substantial response to the new instruments. Although few institutions in the District are offering rates as high (21-22%) as those in Atlanta, the premiums are enough above current money market funds to attract considerable corporate and personal interest throughout the District. Insurance, which the MMDA's provide, is another factor of particular attractiveness to retired and large personal account holders. Except in institutions offering low rates, early indications are that most of the funds are being attracted from money market mutuals. The probability of continued substantial shifts between money market mutuals and the new accounts appears high. Such shifts may create either liquidity problems or an atmosphere of potential problems. In such a climate even more funds would be transferred out of money market mutuals.

Panel of Economists. In response to our request to assess the strengths and weaknesses of their respective economies in 1983, most members of our panel of economists cite construction as a probable leading sector. Several respondents are pessimistic regarding nonresidential construction though. Reflecting in part the economic heterogeneity of the District, little consensus exists otherwise regarding either strengths or weaknesses. Construction-related manufacturing seems likely to improve, in the opinion of many panelists. Chemicals, textiles, oil, gas, exports, and agriculture were each cited by a few respondents as potentially weak sectors.

SEVENTH DISTRICT--CHICAGO

Summary. The sorry state of economic conditions in the Seventh District reported in earlier Redbooks has not improved. Employment, output, and new orders in the manufacturing sector continued to decline in November. Normal plant shutdowns over the holidays commonly will be extended. The retrenchment in capital goods is unprecedented in the postwar era. The industrial base of the equipment and automotive industries is contracting as more plants are closed. Retail sales continue sluggish, with the Christmas season disappointing so far. Residential construction should improve significantly in 1983 if interest rates stay down. The heavy oversupply of new office space is causing rents to decline. Widespread price cutting in wholesale markets frequently means sales below cost. No sign of improvement from depressed levels is noted in the agricultural sector. Business demand for short-term funds is down sharply.

Business Sentiment. Chronic hard times are taking a toll in reduced long-term confidence for both managers and workers. Morale has been depressed by abortive improvements in demand, which were assessed, erroneously, as heralding solid revival. In the past month, District analysts in retailing, paperboard, and cement have noted the evaporation of what had appeared to be promising signs. The Chicago Purchasing Management Association summarized the views of its members on December 7: "The expected recovery has not materialized. All key indicators remain strongly negative."

Lower Break-Even Points. Some companies are confident that they can maintain profitability at sharply reduced levels of operation. Breakeven points have been drastically lowered by large, permanent cuts in personnel,

closing of marginal facilities, sales of unprofitable divisions, scaling down operations by purchasing more parts and services, elimination of less essential functions, and stringent cost control. Such restructuring could bring rapid increases in profits if and when revenues rise significantly.

Consumer Purchases. General merchandise retailers have been unhappy with Christmas sales after a promising start in November. Part, but not all, of the shortfall is attributed to unseasonably warm weather in some weeks, including early December. Virtually all product lines are slow. One large chain has increased sales of household durables by heavy promotions. The largest airline reports passenger traffic up substantially since August, but this reflects bargain fares and free bonus flights.

Employment Losses. Payroll employment in the five Seventh District states in the fall was 8 percent below the same period of prosperous 1978, while employment in the U.S. was one percent higher. Many manufacturing employment in the District was down 25 percent in this comparison. Michigan, of course, has the largest decline. Wisconsin, specializing in capital equipment, has the smallest decline in the District, but its situation has deteriorated very rapidly in the past 12 months. Many manufacturing jobs are gone forever as plants have been closed.

Jobless Funds. State jobless pay funds have been strained as unemployment has remained at high rates for extended periods. The Illinois and Michigan funds each have debts of almost \$2 billion to the federal Treasury. Debts of Iowa and Wisconsin are growing. Indiana, despite its severe unemployment problem, has no such debt because of legal restrictions. Proposals to raise employer contributions to jobless funds are opposed as

likely to encourage additional migration of industry.

Labor Negotiations. The Caterpillar strike that began October 1 has affected many smaller companies that supply components. Management insists that substantial labor contract concessions must be made to reduce an estimated 40 percent cost advantage held by foreign competitors. The Chrysler dispute apparently is being resolved, with the UAW winning its key demand for an immediate wage hike. With the year drawing to a close, it appears that, by-and-large, organized labor is winning its fight to prevent "take-aways of hard-won gains". (The rank-and-file has been more adamant against concessions than union leaders.) Unfortunately, the failure to cut unit production costs substantially in major hard goods industries implies a further erosion of the region's industrial base as producers step up efforts to seek foreign sources for components or finished goods.

Inventories. Although most businesses are still attempting to cut inventories, holdings remain excessive in lines where sales have been even weaker than expected, e.g. apparel, paperboard, and some motor vehicles. Nevertheless, inventories will have to rise in some sectors, including residential building, if demand increases only moderately. A major producer of diesel engines that are mainly used in heavy trucks has recalled some workers. Demand for trucks has not improved, but engine production had been below usage and inventories had been exhausted.

Capital Goods. Prospects for business equipment in the Seventh District are even worse than in earlier months. Conditions vary by company and line but, overall, no earlier post-war recession was nearly so bad. Bookings are off 10 to 65 percent from reduced levels of a year ago at various companies.

One diversified equipment producer is operating at 50 percent of capacity, while another is at 25 percent. Castings production also is at about 25 percent of capacity. Foreign demand, which had been relatively good for some products, has ebbed in recent months. Among the worst lines are equipment for railroads, trucking, agriculture, construction, mining, and metalworking. Capital goods firms have drastically cut corporate staff, including those in design and development, to an extent that could harm competitive positions in future years.

Motor Vehicles. The spurt in auto sales in November, aided by favorable credit terms, is not regarded as a clear indication of an improvement in demand. Some auto dealers dislike temporary incentive programs, because sales almost invariably decline afterwards. Instead, they would prefer lower prices.

Steel. Steel demand remained very depressed in December. Bookings are beginning to show up for January, but probably because of the desire of customers to have inventories at rock bottom for year-end financial statements. Steel companies have learned that customers' normal holiday shutdowns will commonly be extended into January, perhaps into February.

Construction. While residential building is expected to increase significantly in the new year, nonresidential construction is almost certain to be down. Capital expenditure programs are being cancelled or stretched out by manufacturers and public utilities. The glut of new office space in the Chicago area has caused rents to drop by 11 percent in the past year. A large office leasing firm has filed for bankruptcy because of its liability on blocks of space contracted for at rates above the current market level.

EIGHTH DISTRICT - ST. LOUIS

Consumer spending increased during November and early December in the Eighth District, an indication that the economy is about to move out of the business trough. Respondents noted marked increases in purchases of homes and automobiles, and other retail sales began showing signs of life. At the same time, however, industrial production and employment changed little from their depressed levels.

Just as a recovery appeared to be developing, the District's economy was dealt a blow by the weather. Heavy rains over much of the area in late November and early December, accompanied by several tornadoes, and followed by flooding of the Mississippi River and many of its tributaries, caused widespread damage. Estimates of the direct loss of wealth are running into the hundreds of millions of dollars. Moreover, operations of many businesses were severely interrupted, and the cleanup will place a further burden on the economy.

Automobile sales have strengthened. Ford dealers in the St. Louis sales district reported that passenger car sales in November were up 26 percent from last November and that truck sales jumped 71 percent. One large dealer said that his used car sales in the month were comparable to previous peaks. Two dealers in the Memphis area reported a moderate improvement in sales, and dealers in Arkansas have been encouraged by the lifting of the 10 percent usury ceiling which should facilitate credit sales.

New home sales in the St. Louis area during November were greater than in any other November in recent years, according to the St. Louis Homebuilders Association. Home prices have declined slightly since the spring of 1981, and have fallen strikingly in real terms. This decline has been even sharper because prices have been effectively reduced through "creative financing" offered by sellers to consummate deals.

Sales at major stores in the District (Sears, J.C. Penney, May Company, and Woolworth) were, on the average, 6.4 percent higher this November than during November 1981, an increase of nearly 3 percent after adjusting for merchandise price increases. Early December sales were running at a similar pace above those of last year. Five smaller retailers reported gains of 9 percent since October in year-over-year nominal sales. Consumer demand has probably strengthened more than the sales data alone indicate as managers made fewer price concessions this year than last. A shoe chain reported an 11 percent increase in sales from November 1981 to November 1982.

Orders, production and shipments at most District manufacturing firms were slightly lower in November and early December than in the early fall. Companies producing business equipment, chemicals, metals and wood products were particularly depressed. On the other hand, a supplier to firms producing consumer durables noted the first improvement in orders and production in many months. Businesses producing food, defense goods and boxes noted a slight improvement in activity. Employment declined at many industrial firms; a chemical company retired over 1,200 workers. At many smaller businesses, however, employment continued to increase.

Deposits changed little at District savings and loan associations in November and early December. Several associations continued to report a moderate net outflow of funds, but others gained funds by bidding aggressively for them. Most associations still report the current rate of earnings on assets to be slightly less than the cost of obtaining funds, but the negative yield spread has narrowed.

The agricultural situation appears to be near a trough. Favorable selling prices and low feed costs are generating profits for livestock raisers, particularly those engaged in hog production. Prices of grain are holding at current levels, largely supported by government programs. Carry-over stocks of grain, however, are estimated at near 50 percent of annual usage--the highest level since 1960. Many farmers are in severe financial difficulty, reflecting large debts at the beginning of the crop year, high interest rates, and low selling prices for crops.

Scattered farm groups in Illinois, Missouri and Tennessee reportedly have adopted militant tactics to discourage creditors from foreclosing on farm debt. Their activities include blocking entrances to farms, bullying bidders at auctions, and hiding farm equipment. Although the number of actual cases is small, the incidents have received publicity. A few creditors reportedly have agreed to delay foreclosure and negotiate further.

NINTH DISTRICT - MINNEAPOLIS

After many months of waiting, the Ninth District economy has finally begun showing a few definite signs of recovery. In response to lower interest rates, district home and auto sales increased in November. General merchandise sales improved also, and orders of some manufacturers increased. These positive signs are admittedly tenuous, however, and much of the district economy remained depressed. The district had less excess capacity in manufacturing than the nation, but orders continued to decline at many local manufacturers. Although most district farmers were able to complete the fall harvest, poor prices continued to trouble them. Lending at district banks remained weak, and most district financial institutions were slow to formulate plans for the new Money Market Deposit Accounts (MMDAs).

Consumer Spending

Home and auto sales have picked up in the Ninth District. Our last Redbook report indicated that, in October, reduced mortgage rates had increased the number of people looking at homes--but not the number buying. In November, home sales actually picked up. According to the Minneapolis Board of Realtors, home sales in Minneapolis and its suburbs increased 20 percent between October and November, a period during which home sales normally decline. Also, regional sales managers for domestic auto manufacturers indicate that in November district car sales improved. One says that last month his company's 10.9 percent finance rate helped reduce inventories of 1982 models 50 percent. A director reports that, thanks to the pickup in car sales, most

Montana car dealers showed a profit in November, for the first time in many months.

General merchandise sales have also improved somewhat. Two Minneapolis-St. Paul retailers report that their sales increased modestly between October and November, but that post-Thanksgiving shopping was slower than normal. They attribute this to changed shopping habits; consumers are now delaying purchases until retailers cut prices just before Christmas. Thus, these retailers are planning pre-Christmas sales and expect this December to be better than last year's. Directors, however, report that many retailers outside the Twin Cities hope to just match last year's holiday sales. This glum outlook in many parts of the district is directly due to the long-depressed iron mining and farming industries.

Industrial Activity

The pickup in consumer spending has started to carry over to a few manufacturers. Reflecting the recent improvement in retail sales, new orders of microwave ovens increased markedly at one manufacturer. A spokesperson for a large meat packing company in southern Minnesota, which recently opened a new plant, reports that business has been better lately than expected. This firm plans to hire additional people. Due to the upturn in home sales, orders increased at a large manufacturer of windows and doors and another of ceiling tiles.

Most district manufacturing concerns, however, have remained in the doldrums. Eleven of the 23 largest manufacturers headquartered in the district report third quarter sales below those a year ago. Particularly hard

hit have been producers of industrial equipment. A firm making construction and material handling equipment reports that its order backlog shrank from \$150 million at the beginning of the year to \$50 million in early December. A representative for a company producing industrial controls and painting equipment indicates that an anticipated pickup in new orders has not yet materialized. In fact, new orders have declined, leaving its current inventories at higher than desired levels. Growth rates have slowed even at computer and other high technology firms, where sales are generally increasing, according to a Minneapolis security analyst who follows this industry group.

Capacity utilization data can provide some insight on the performance of the manufacturing sector. These data aren't available at the district level, but we can infer some information from differences in the structure of manufacturing between the district and nation and from anecdotal evidence. Approximately 45 percent of district manufacturing is concentrated in two industries--machinery and food processing--compared to 30 percent in these industries nationally. Moreover, within the machinery group, computer manufacturing is about three times more important to the district than to the nation.

According to our recent conversations with industry spokespeople, the district's capacity utilization rates are currently well above the nation's in both the machinery and food processing industries. In machinery manufacturing, where the national utilization rate is 67 percent, the district rate is higher; our contacts indicate that most district computer manufacturers lately have been operating at near capacity. Conversations with representa-

tives of large district food processors indicate that their capacity utilization rates are also above the nation's 80 percent capacity utilization rate for the industry. The district's remaining manufacturing industries are a diverse group, and for them, capacity utilization rates may not be too different than the national rates, at least not on average. Therefore, based on the structural differences between the district and nation and on the anecdotal evidence, the district's current capacity utilization rate for manufacturing is almost surely above the nation's 68 percent.

This same approach may be used to examine capacity utilization in metal mining. Iron mining accounts for 75 percent of metal mining locally, compared to 20 percent nationally, and copper mining accounts for much of the rest of Ninth District metal mining. In September, capacity utilization for district iron mining was around 10 percent, when only two or three out of eleven mines were producing. Utilization is somewhat higher now because several additional iron ore mines resumed partial operation in October. And two more Minnesota iron mines plan to resume operation in early 1983. Even so, an industry official reportedly expects capacity utilization in iron mining next year to average only 55 percent.

Current capacity utilization in district copper mining is also very low. The one mine in the Upper Peninsula of Michigan was indefinitely shut down in early October. And, in Montana, only a small amount of copper is being produced, because the state's one large mine was closed permanently earlier this year. Based on the local mining industry's heavy concentration in iron and copper (especially iron) and on the extremely low output levels

for both metals, it is virtually certain that the district's capacity utilization rate in metal mining is well below the nation's 40 percent rate. Moreover, it seems likely that this situation will continue well into 1983.

Agricultural Conditions

Although recent weather conditions were favorable, agriculture has remained depressed. Our last Redbook report said farmers were concerned that wet weather would interfere with the harvest. Recently, however, the weather has been good for harvesting, and as of November 28, the USDA reports, 84 percent of the corn and 97 percent of the soybeans were harvested in Minnesota. But agricultural prices remain troubling. In November, Minneapolis cash prices for corn and soybeans were, respectively, 4 and 9 percent below levels a year ago; and South St. Paul cash prices for feeder and slaughter cattle in November were down 5 and 1 percent, respectively. Hogs remain a bright spot in district agriculture: in late November their price was up 25 percent from a year earlier. Dairy farms have been doing relatively well also. According to an industry analyst, however, the federal government's assessment of 50 cents per hundredweight of milk produced has put a "good dent" in dairy farmers' income. This assessment began December 1.

Financial Developments

Bank lending has remained weak. In November loans at district banks and S&Ls were essentially unchanged from their lackluster October level. Part of the reason for this sluggishness is that district corporations have increased their use of the primary securities markets, and in some instances, they have been using these funds to reduce bank debt.

Sluggish loan demand may explain the response of local firms to the new MMDAs: most have not been aggressively promoting them. Another explanation, according to our telephone survey of district banks and S&Ls, is that they are waiting for the DIDC's directive on the Super NOW account. They are also frustrated with the short implementation period for the new MMDAs. In fact, most of the banks and S&Ls say they haven't decided yet about the new MMDAs or are "waiting to see what the competition will do."

TENTH DISTRICT—KANSAS CITY

Overview. Business activity in the Tenth District appears to be generally flat, except for slight improvement in the housing sector. Soft retail sales have brought higher than desired retail inventories, but manufacturers' inventories are generally satisfactory. Housing starts are up slightly, as is demand for mortgage funds and commitments. Both deposit growth and commercial and industrial loan demand are up slightly at commercial banks. Tenth District farmers continue to experience financial stress because of poor income prospects.

Retail Trade. Most retailers in the Tenth District report only moderate gains in sales in the first 11 months of 1982 compared to the first 11 months of 1981. Sales improved slightly in November although durable goods sales remained weak. Merchandise costs have not risen recently but slow sales have put downward pressure on profit margins. Inventories are currently higher than desired for most retailers primarily because of slow sales. Most retailers anticipate that gains in sales during the remainder of the Christmas season will eliminate excess inventories and improve profit margins.

Purchasing Agents. Most purchasing agents contacted report modest declines or no change in input prices over the last year, and only minor price increases over the past three months. While purchasing agents expect no major price increases soon, a few expect input prices in 1983 to be about 6 percent higher than in 1982. Most firms contacted are having no difficulties getting materials, but some purchasing agents express concern about possible difficulties in 1983. They feel that if the economic upturn begins, suppliers may be caught understocked, and if it does not begin, more suppliers may close.

Nearly all firms report satisfactory inventory levels. While most firms are trimming inventories in response to general economic conditions and the need for improved efficiency, others have stopped trimming and are trying to maintain inventories at minimal levels.

Housing and Housing Finance. The decline in interest rates has brought a significant rise in housing starts since October 1 in the Tenth District that could result in starts for 1982 exceeding those in 1981 by 25 percent. Respondents see this increase continuing, if interest rates stay at current levels. Sales of new homes have also increased recently. The slack demand in 1982 has resulted in new home prices similar to those in 1981, but respondents expect prices to move up in the spring. Inventories of new homes are at all-time lows. Material prices are reported to be at approximately the same level as in 1981, although some respondents report recent increases in lumber prices. Respondents are expecting a general increase in prices beginning in the spring of 1983.

Officers at Tenth District Savings and Loan Associations generally report little or no change in savings inflows compared to a year ago, but they expect increased activity in the near future. The introduction of money market deposit accounts is the primary source of their optimism. Most officers report recent improvement in the demand for mortgage funds and mortgage commitments, but a minority report continuing slack demand. Additional increases are expected, assuming continued declines in interest rates, but with no significant additional activity before spring. Loans are being made at interest rates of 12 1/2 to 14 5/8 percent, and further slight declines are expected.

Banking. Tenth District banks report little recent growth in loan demand.

Consumer, agricultural, and real estate lending remain flat. About half the banks surveyed note increases in commercial and industrial loans, which is only partly seasonal. Most bankers report that loan quality has stabilized. The prime rate is 11 1/2 to 12 percent, down from 12 to 12 1/2 percent last month. Deposit growth is up slightly at Tenth District banks. Nearly all banks report growth in demand deposits, some of which is seasonal, and in large CD's. NOW accounts, small time deposits, and savings deposits have grown slightly, while money market and small savers certificates have remained constant. All banks surveyed plan to offer the new money market deposit account (MMDA). Very few are offering bridge accounts, however, and no significant movement of funds in anticipation of the new MMDA is reported.

Agriculture. The harvesting of crops throughout the Tenth District is virtually complete, with little damage from frost or recent heavy rainfall. Winter wheat conditions range from poor in Oklahoma to fair elsewhere in the Tenth District. As a result, little pasturing of cattle on winter wheat is occurring. Grain storage capacity continues to be adequate throughout the District. Despite considerable use of temporary storage facilities, the quality of stored grain is not expected to be adversely affected. Without a reduction in grain stocks, however, next year's storage capacity may be inadequate. District bankers report that some local areas are receiving slightly higher cash prices for their crops, resulting in an increasing number of farmers selling grain. Paydowns are being made by farmers on their agricultural production loans but at a slower than normal rate. Tenth District farmers continue to experience financial stress because of poor income prospects. Rural nonfarm businesses in the District are also experiencing nearly as much financial stress as a result of the depressed economy as are farmers.

ELEVENTH DISTRICT--DALLAS

The District economy shows some signs of reviving despite continuing weakness in the durable goods sector. Residential construction is unusually active for this time of year. A surge in smaller commercial projects has lately slowed declines in nonresidential construction. Unemployment seems to have stabilized. Auto sales are up sharply. Drilling activity continues to accelerate, but steel and other oil related industries remain sluggish.

Residential construction continues to gain momentum. New home sales and starts during November were roughly even with October's strong sales and starts. Home construction usually falls this time of year, but falling mortgage rates have abrogated the traditional seasonal patterns. The first signs of increasing costs are appearing as lumber prices are beginning to escalate. Apartment and condominium construction is also proceeding swiftly, although condominium sales in the Border region are depressed.

Commercial construction rebounded somewhat from the large declines recorded in September. Although the pace of office building and warehouse construction continues to slow, retail, industrial, and government construction are picking up some of the slack. The result has been a sharp increase in the number of nonresidential projects accompanied by a more moderate increase in the total project value. For the year to date the value of construction is well behind last year's record.

At worst, unemployment figures indicate that the job market is not weakening. Texas' seasonally adjusted unemployment rate dropped from

8.3 percent in October to 7.6 percent in November. This change is not statistically significant. Total nonagricultural employment was virtually unchanged from September to October. Gains in government employment largely offset declines in durable goods manufacturing and mining.

November sales of new autos surged in response to the discount financing made available by GMAC, Ford Motor Credit Co., and Chrysler Credit Corporation. Sales suffered among import dealers due to their lack of special financing programs. Used car sales also declined. The surge in auto purchases reduced dealer inventories, increased new orders for '83 models, and pushed up overall profits. Nevertheless, dealers have had to sacrifice some or all of their profits from financing in order to obtain the lower rates for their customers.

Real department store sales for the District for the year to date are about even with last year. While sales remain slow in Houston and Border stores, sales in other areas of Texas are picking up. The effects of the peso devaluations are still felt along the Border and in Houston. Houston is also affected by the slowdown in durable goods manufacturing. Respondents in areas that report sales gains are quick to point out that earlier than usual holiday promotions account for the increases.

Drilling continued to pick up throughout November and early December, more so than seasonal patterns would dictate. Six consecutive weekly increases have pushed the Texas rotary rig count to its highest level since May 24, 1982. Analysts point to higher domestic crude prices at refineries and lower labor costs as the reasons for the increase beyond seasonal norms. The outlook for drilling depends on the outcome of the December 19th meeting of the OPEC oil ministers.

Larger future beef supplies were signaled by the number of cattle and calves on feed, which are at the highest level yet for 1982. Unfortunately, much of this increase reflects unfavorable economic conditions for livestock producers, as heifers are being placed on feed rather than being added to breeding herds. Livestock prices have remained steady while crop prices have moved slightly higher. The cost of farm inputs stayed constant. Planting of winter grains is mostly complete.

Manufacturing production is mixed. Steel markets continue to erode as the demand for concrete reinforcing products is slipping and oil related product demand remains depressed. Home computer and defense sales are maintaining electronics production and refinery output is stable. Lumber and wood product suppliers report that business is picking up as a result of increased housing construction.

Deposits at District member banks grew a modest 0.8 percent from September to November as time deposit growth more than offset declining demand deposits. Loans by member banks grew 2.0 percent during this period, while real estate, business, and consumer loans at large weekly reporting banks grew by 5.3, 2.3 and 1.5 percent.

Total deposits at federally insured S&L's increased 0.9 percent in October to a level which was 9.2 percent greater than the same time a year ago. The increase was due to large gains in jumbo CD's and accounts earning the passbook rate or less. Although total mortgage loans outstanding increased a mere 0.6 percent during October, outstanding loans for construction jumped 3.6 percent. The latter usually falls this time of year and is, in fact, 76.5 percent greater than a year ago.

TWELFTH DISTRICT--SAN FRANCISCO

The economy of the Twelfth District appears to have slipped more deeply into recession. Unemployment rates generally rose during November and the District as a whole posts a higher unemployment rate than the national average. Although declines in interest rates have spurred residential construction permit activity (substantially in some cases) the industry is operating at such levels that little absolute stimulus has been felt as a result. The lumber mills in the District are suffering from the combined impact of the continued reduced domestic and foreign demand, and costly timber cutting obligations. Retail sales have been disappointing thus far and conventionally strong industries--such as aerospace and electronics--are experiencing major layoffs. Motor car manufacturing is sagging under the announcement of further plant closures. Financial institutions in the region report deposit outflows or only weak deposit growth except in the high-yield money-market type accounts and loan demand has been flat.

Consumer spending

Reports from major department stores and other retailers indicate "disappointing" sales growth over last year, which was itself a weak year, although there is some early optimism about Christmas season activity. Several major Southern California department stores, when surveyed, indicated that nominal sales growth was up only about 7 percent, barely matching the inflation rate. Penny's and Sears report sales volumes below that of a year ago. In the restaurant industry, the picture is much the same with nominal sales growth of about 6 percent; even that modest growth is attributed to stable food costs and no increase in the minimum wage allowing restaurants to induce continued patronage with relatively low prices. Volume is flat for one

California retail grocery chain and net income is below the level of a year earlier. Only tourism in Hawaii and Oregon are consistently reported as bright spots in the consumer spending picture. Hawaii expects to top its all-time tourism volume record this year, helping to make the Hawaiian unemployment rate one of the lowest in the District and considerably below the national average.

Manufacturing and mining

There are few good reports concerning the condition of the District's manufacturing and mining enterprises. Aerospace and electronics report falling orders and reduced margins on foreign sales because of the unusual strength of the dollar. Boeing's new equipment sales, for example, are at the lowest annualized volume in 20 years. Manufacturers of electronic equipment are experiencing reduced domestic and foreign sales; so many retailers returned merchandise to Atari, Inc., for example, that the price of its stock experienced an unprecedented plunge in early December. The mining of the region's copper, silver and molybdenum remain at low levels of activity, with 10,000 of Arizona's mining employees out of work in copper mines alone. Depressed world oil and gas prices have also affected the economies of Alaska, California and the intermountain states, although Utah's relatively more diversified economy has allowed it to experience "flat" growth rather than absolute declines in overall activity. Although declining interest rates have helped some corporations' profit positions, many remain "locked in" to long term financing agreements at much higher rates, causing a spotty pattern of profit margin changes. Automobile manufacturing in the District was dealt another blow with Ford's announcement that it would close its Northern California assembly plant. Car sales, however, have picked up in the

District, primarily in response to the special interest rate concessions offered by General Motors and Ford.

Construction and real estate

Lower interest rates have undoubtedly provided some stimulus to the housing industry; there have been surges in activity reported throughout the District, with permits increasing as much as 80 percent in some parts of Utah. Homes are selling more rapidly in the low and high-priced ranges than in the medium-price range; the base level of activity is so low, however, that recent upsurges can hardly be called a recovery. Commercial real estate is also beginning to suffer as the traditional overbuilding cycle takes hold and demand for office space weakens. District architects report the lowest levels of backorders in years, an ominous leading indicator for future activity.

Agriculture

Although early rains damaged tomato and wine and raisin grape crops in California, in general the harvest season yielded bumper crops, leading to depressed prices and farm incomes. In addition, there is a growing move toward protectionism among the District's farmers who feels that certain foreign products--particularly cotton and raisins--enjoy the benefit of government subsidies and are hurting domestic producers. The problem is amplified by the relative weakness of foreign currencies. The timber products industry is suffering a three-pronged effect of weak domestic demand (with most mills operating at less than 40 percent capacity), weakened European and Asian demand for stumpage, and costly public timber harvesting obligations. It is estimated that Northwest timber producers will suffer a \$2 billion loss if they are required to comply with earlier contracts to harvest 10 billion board feet from public lands during this period of weak demand.

Financial institutions

District financial institutions report flat loan demand and either flat deposit in-flows or continued outflows; the latter is particularly true of the beleaguered savings and loan industry. Preliminary evidence from October indicates that the outflow from maturing All Savers Certificates may be in the \$6 to \$8 billion range for savings and loan associations. Roughly 25-45 associations are disappearing through consolidation each month. Falling interest rates have improved spreads for some associations, and some will report second-half profits. However, much of the profits are due to sales of loans or trading profits and the picture still remains bleak. The high-yielding money-market type accounts are the only major source of funds in-flows to banks and savings and loan associations. The largest Western banks report continued deterioration in the financial positions of a sizeable number of existing commercial loan customers, as well as in the condition on a major portion of applicants for new business loans. Until firms have seen a significant improvement in the business fortunes and have had time to resolve their current financial difficulties, near-term improvement in business loan demand seems most unlikely.