

SUMMARY OF COMMENTARY ON CURRENT ECONOMIC CONDITIONS  
BY FEDERAL RESERVE DISTRICTS

MARCH 1988

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## SUMMARY\*

Without exception, reports confirm a moderate expansion of the nation's economy. Strength in the manufacturing sector and continued moderate growth in employment are sustaining the current expansion. Consumer spending, which had provided much of the earlier stimulus to the economy, has continued to expand sluggishly. Auto sales, however, improved and have risen strongly in some districts. Construction activity remains mixed, while bank loan demand is generally flat. Consumer lending has declined sharply in keeping with the slower growth of consumer spending. The farm sector outlook remains positive.

Manufacturing

Most districts report a general expansion of manufacturing activity. The declining foreign exchange value of the dollar is credited with spurring manufacturing growth in many districts. Orders for steel or fabricated metals produced in the Boston, Chicago, St. Louis and Dallas districts are increasing rapidly. Many producers are using all available capacity causing higher prices in some areas. Paper production is growing rapidly according to Boston, Atlanta and San Francisco. Several districts also mention growth in electronic equipment orders. Atlanta, Dallas and St. Louis report strong gains in textile and apparel orders, with labor shortages reported by Atlanta. Tight labor markets are also mentioned by Boston and St. Louis. Despite manufacturing's general strength, Chicago and St. Louis note auto production declines.

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\*Prepared at the Federal Reserve Bank of St. Louis based on information gathered prior to March 8, 1988.

Dallas and San Francisco also report weakness in defense and construction-related manufacturing.

Boston and Dallas find manufacturers' inventories generally at satisfactory levels, but Kansas City reports higher-than-desired inventories of material inputs. Of the six districts that mention manufacturers' input prices, most report price increases. Boston, Philadelphia and Richmond report generally stable prices for manufacturers' products. Prices of some products, such as paper and steel, however, are up sharply.

#### Employment

Most Districts indicate generally favorable employment growth. Declining unemployment rates are mentioned by New York, Cleveland and Minneapolis. Areas of weakness include layoffs in New York's financial sector and in the auto industry of the Chicago and St. Louis districts.

#### Consumer Spending

Retail sales for January and February are flat or weak in all districts. Despite the weakness, retail inventories are near or slightly below desired levels in all districts except Minneapolis. New York and San Francisco point out that many retailers are reserving their judgment on the outlook for the year pending the results of Easter sales. Boston and San Francisco report that prices of imported consumer goods have risen. Kansas City found only modest general price increases.

Strong auto sales are reported by Cleveland, Atlanta, St. Louis and Minneapolis. Other districts indicate that auto sales are on target or slightly ahead of last year. A number of districts find that domestic autos are selling better than imports because of import price increases and domestic manufacturers' incentive programs.

### Construction

The performance of the construction sector is mixed. Boston, Chicago, Kansas City and Philadelphia report an improved construction environment, whereas St. Louis, Dallas and San Francisco report a weakening in overall construction activity. Residential construction, while expanding in the Atlanta, Boston, Philadelphia and St. Louis districts, is declining in most other districts. Boston and Philadelphia report strong new home sales. Commercial construction continues to show mixed results. Construction activity in the Chicago district is likely to remain at a high level in 1988. The Minneapolis district reports that January nonresidential building contracts were three times higher than in January 1987. In Dallas, construction continues to decline and remains the weakest sector of the economy.

### Banking

Loan demand at the nation's largest commercial banks remained generally flat. Most districts report that reductions in lending rates during February have not triggered a significant increase in loan applications. Richmond was the only district reporting an increase in loan demand across all major loan categories. Two-thirds of the bankers surveyed by Richmond anticipate increased demand over the next six months for both consumer and real estate loans. Cleveland, Kansas City, Philadelphia and St. Louis report a slowing in consumer lending. Cleveland, Richmond, Philadelphia and Atlanta report strength in real estate and commercial lending. Atlanta cites rising exports as the primary reason for the increased commercial loan volume. New York reports that demand for commercial mortgages for office construction is particularly weak, and some bankers believe the suburban office space

surrounding New York City is overbuilt. Dallas reports further declines in deposit and loan growth due to widespread concern about the stability of District financial institutions.

Agriculture and Natural Resources

Of the districts mentioning agriculture, all describe strength in the farm sector. Richmond and San Francisco report stronger farmland values, while Chicago and Kansas City report increased farm equipment sales. St. Louis and San Francisco find that farm loan demand has fallen, while Kansas City indicates flat loan demand.

Three districts indicate increased oil drilling activity. The lumber and forest product industry and the West's mining industry are strong.

## FIRST DISTRICT-BOSTON

Economic reports were quite mixed in the First District in February. Retail results were mostly disappointing while manufacturers generally reported improvement. Manufacturers' shipments ran 2 to 10 percent ahead of last year and new orders ranged from flat to 20 percent higher than a year earlier. Most of the retailers and manufacturers contacted have satisfactory inventory levels, but a few are overstocked. The outlook is generally upbeat, as evidenced by plans to increase capital spending or continue opening new stores. A recent pickup in the region's residential real estate market makes realtors optimistic as well.

Retail

Sales at most of the First District retailers sampled were slack in February, although one contact, a mass-market discount chain, reported brisk activity. The weakness was most noticeable in soft goods; sales of hard goods reportedly dropped off only in the last two weeks of February. Despite lackluster activity, only one respondent expressed discomfort with "over-stocked" inventory levels.

In the area of pricing, respondents reported no change in their own markup or promotional policies. At the wholesale level, however, prices are reported to be rising on imported hard goods while remaining flat or falling in the weaker market for soft goods. In response to exchange rate shifts, upscale merchants have been unable to find acceptable substitutes for Japanese electronics or European housewares; low-end discounters, on

the other hand, are turning to alternate foreign sources or domestic manufacturers.

The retail outlook is mixed, but hardly pessimistic. Most of the retailers surveyed had non-economic explanations for the current softness, citing bad weather, management failures, and the lack of an accepted fashion trend. Thus a majority expect sales to rise - some moderately and some rather smartly.

Respondents are proceeding cautiously with their investment programs. Some of this investment is aimed at increasing efficiency rather than expanding capacity. But most chains are adding new outlets, albeit at a slower pace than in recent years.

### Manufacturing

First District manufacturers' reports on new orders range from flat to "startlingly" strong compared with their year-ago levels. The best reports come from respondents in paper products, fabricated metals and transportation where new orders are up 8 to 20 percent from early 1987. Demand emanating from the electronics and auto industries is described as improving, but reports on government orders vary. Only a few respondents said exports or the weak dollar contributed to their gains. Current shipments are running 2 to 10 percent above year-ago levels.

Materials prices are rising modestly (2 to 3 percent) except for paper and metals. With availability a concern, paper prices are up 10 percent and are expected to go on rising. Nickel prices have doubled recently. High copper and aluminum prices, in contrast, are now thought to be headed down. Manufacturers' own prices are generally stable, but there

are exceptions. For example, a tool maker recently raised prices 10 to 15 percent and manufacturers of paper products have passed most cost increases on to their customers.

Inventories are generally termed satisfactory, but a third of the respondents find them higher than they would like. Employment levels are stable, although a minority would hire a few production workers if they were not facing tight labor markets and "incredible" turnover rates in New Hampshire and the Greater Boston area. One firm, however, expects a layoff later this year.

As for capital spending, most respondents plan increases of 10 to 25 percent from 1987 levels while a minority expect little change or declines. Contacts in paper, fabricated metals and transportation are expanding capacity slightly, but most spending programs are aimed at modernization and efficiency improvements.

In general, First District manufacturers are "cautiously optimistic" about 1988 and expect a "decent" year with slow growth. One third of those contacted recently revised their post-October forecasts upward, and no one expects a recession in 1988.

#### Residential Real Estate

Residential real estate sales in the First District picked up in February compared to recent months and now exceed year-earlier levels. The improvement is especially pronounced in the Boston area, where realtors report very brisk activity. Less expensive houses and condominiums are more in demand than expensive homes. Realtors look forward to a very busy spring.

## SECOND DISTRICT--NEW YORK

Economic activity in the Second District has continued mixed. Retail sales were relatively strong in January, but a decided slowing occurred during February. While overall business conditions were generally satisfactory, demand for new homes and office space varied among areas. Business borrowing at small and medium-sized banks was somewhat spotty.

Consumer Spending

The pattern of retail sales in the District has been mixed since the last report.. Respondents stated that consumer spending was relatively strong in January, due in part to continued heavy promotionals. During the first half of February, however, sales activity showed a decided slowing, which they viewed with some concern. Nonetheless, District retailers were hopeful that, given the early occurrence of Easter this year, activity would soon improve.

Over-the-year gains during January ranged from 9 percent to 15 percent and were reported to be on or above plan. Demand was strong for a number of categories including adult and children's apparel, accessories and home furnishings. Buying by foreign consumers continued somewhat heavier than usual according to New York City retailers. As a result of the strong sales activity, inventories were generally pared in January. Respondents described their inventory situation as ranging from on plan to 3 percent above. Some unwanted accumulation occurred over the first half of February, however, when consumer demand weakened.

Residential Construction and Real Estate

Conditions in the District's market for new homes are varied. In some areas of speculative building and high prices, developers are offering a variety of

incentives in order to try to sell new houses and condominiums. In many other areas, however, overall demand remains strong, and the need for affordable housing is unabated. Several large-scale residential projects have recently begun or will soon be undertaken. In downtown White Plains the foundation was poured for a 316-unit apartment building--the largest in Westchester County--which will provide medium-priced housing for some of the workers in the many new office buildings there. Elsewhere, a residential community is developing in what has been an industrial area of Queens, a desirable site located on the water and facing the Manhattan skyline. One apartment building has already been constructed, another is underway, and a third will probably be started there this spring.

The pace of commercial leasing activity has also varied during recent weeks. Demand for office space is strong on much of Long Island, due in part to last year's moratoriums on construction in some areas. Moreover, despite the fact that their vacancy rates remain well above 20 percent, Fairfield County and northern New Jersey have seen some improvement in leasing activity. In Westchester County, however, net absorption of office space has been minimal due to lackluster demand and corporate relocations and downsizing. Leasing has also slowed in New York City where a substantial amount of office space was recently added as the result of a merger of two financial services firms. Midtown and downtown Manhattan vacancy rates have risen and are expected to move higher in the months ahead. Six years ago the City offered zoning incentives to stimulate the commercial development of Midtown west. Since developers wanted to meet the May 1988 deadline for laying foundations, an additional 12 million square feet of office space is now under construction in midtown.

#### Business Activity

Economic conditions in the Second District have generally been satisfactory with the major exception being the widespread layoffs which are taking

place in the financial services sector. Despite these layoffs however, February unemployment rates in New York and New Jersey fell further to 3.9 percent and 3.4 percent, respectively--the lowest in 18 years. The New York City rate also remains some two and a half percentage points below its year-earlier level. While further cutbacks by the City's financial services firms are in the offing, several other areas report that their economy continues to expand. In Rochester, for example, where 84 percent of surveyed purchasing managers found current business conditions to be the same or improved in January, 60 percent anticipated further gains over the next three months.

#### Financial Developments

Demand for commercial loans in the Second District has been somewhat spotty in recent months based on a survey of senior officers of small and medium-sized banks. Though most stated that the level of borrowing activity was about average, some reported strong demand while others noted sluggishness. Reductions in lending rates at these banks during early February have not triggered a significant increase in loan applications. Several bankers commented that businesses tend to be less sensitive to interest rate changes than individuals. Among the different sectors, demand for commercial mortgages for office construction is particularly weak. Some of the bankers believe that suburban office space surrounding New York City is overbuilt, a troublesome situation given the weakness of the securities industry. One bank reported a dramatic drop in demand for import loans, particularly those for Taiwanese products. Most respondents anticipate that 1988 will eventually prove to be a year of healthy growth for their banks. Though they were generally less optimistic about the U.S. economy at large, most were confident that a recession would be avoided and the second half of 1988 would show stronger growth.

## THIRD DISTRICT - PHILADELPHIA

The Third District economy in early March was making only modest progress. Manufacturing activity was advancing marginally and retail sales were level with, or slightly above, the pace of the year-ago period. Auto sales are considerably higher than they were in early 1987, although the increase is less than dealers had expected. Banks report very little growth in consumer loans, but note an improvement in commercial lending; real estate lending remains strong. Commercial real estate markets are softening in some suburban areas but are otherwise healthy. Residential real estate activity is picking up slightly and builders report a good sales rate at new projects.

Expectations in the Third District business community are mixed, but the overall outlook is for a continuation of current trends. Retailers expect the pace of sales to accelerate modestly from spring through fall, achieving an annual increase between 3 and 10 percent. Auto dealers believe cars will sell at about the current rate for the rest of the year. Bankers expect continued strength in real estate lending and look for a modest increase in business loan demand, but they expect consumer lending to remain flat. Real estate agents say home sales will run at a good pace this year if mortgage rates do not rise above current levels, and builders expect new home sales this year to match last year's rate, although they are not optimistic that housing demand will carry strongly into 1989. Manufacturers have the most negative forecast: in February, surveyed manufacturers turned pessimistic, on balance, for the first time in nearly eight years, and they have held to this view in March. Local industrial firms expect slower business in the next six months, and they may reduce employment accordingly.

MANUFACTURING

Industrial activity in the region is moving up marginally, according to preliminary results of the March Business Outlook Survey. Twenty percent of the manufacturers covered by the survey are stepping up operations, 70 percent are running at a steady pace, and 10 percent are cutting back. Nondurables manufacturers report relatively more improvement than durable goods producers.

Specific measures of industrial activity are mixed. In March, new orders increased marginally, but shipments increased at a faster pace; consequently, order backlogs fell slightly. However, the pickup in shipments allowed manufacturers to work down inventories somewhat this month. Manufacturing employment continues to grow: more firms reported adding workers than cutting back in March, marking eleven consecutive months of rising payrolls.

With regard to prices, half of the March survey respondents report rising input costs and half say they are steady; for their own goods, 25 percent are charging more while 70 percent are maintaining steady prices.

The outlook among Third District manufacturers turned pessimistic in February and remained so in March. For the first time in nearly eight years anticipation of slower business is more widespread among surveyed companies than expectations of improvement. Survey respondents also forecast a level rate of new orders and shipments, a further decline in order backlogs, and a weaker employment situation in the next six months.

RETAIL

Third District retail sales in early March were running level with or slightly above last year's pace, roughly according to merchants' plans. Store officials said their inventories were in line with sales. Some reported taking delivery of spring merchandise earlier than usual to get discounts offered by suppliers; none reported undesired buildup of stocks.

Merchants are cautiously optimistic for the year ahead; they expect the pace of sales to be mild in the spring and move up through fall, with sales for the year as a whole 3-10 percent above 1987. Plans to add or remodel stores are being considered by many area retailers.

Auto dealers said sales in January and February ran above sales in the same months in 1987. Dealers said the year-to-year improvement is more than just a rebound from the particularly low sales of the prior year period and reflects healthy demand for new cars. Although they have scaled back the 1988 sales estimates they made last year, they are optimistic that the current rate of sales can be maintained for the balance of the year, even without manufacturers' incentives.

#### FINANCE

Total loan growth at major Third District banks picked up in February after a pause in January. Lending officers say business loan demand has rebounded recently and they are receiving more inquiries from business borrowers. Consumer lending is growing weakly. Bankers say credit card lending is flat while other types of personal installment lending are advancing fractionally. Several banks have been promoting personal auto leasing recently, and these efforts have boosted this form of consumer finance. Real estate lending continues to grow at a strong pace.

Bankers expect current lending trends to continue. They foresee some further growth in commercial and industrial lending, but expect consumer lending to remain flat. Real estate lenders expect real estate loan volume to be strong for the rest of the year.

#### REAL ESTATE AND CONSTRUCTION

Real estate agents described most markets as healthy in early March, with commercial leasing generally steady and residential sales picking up.

Commercial real estate markets in the Third District are active although some pockets of softness are beginning to appear. Commercial real estate agents say office supply and demand in the central business district of Philadelphia are roughly in balance; in suburban locations the picture is mixed. Vacancy rates are rising in areas where construction has been extensive and falling in areas where the pace of building has been slower. Lease concessions are now common in relatively overbuilt areas, and developers in these areas have postponed starting dates for new projects.

Demand for industrial buildings is strong through most of the Third District. As major highway projects in the region near completion, companies from outside the district are locating new warehousing and distribution centers to take advantage of improved transportation links.

Residential real estate markets in the Third District are generally healthy. Sales activity slackened in January, but real estate agents contacted at the end of February said home sales were increasing by what appeared to be more than a seasonal amount. Some agents said houses in the higher price ranges were not selling as quickly as lower priced houses; and their forecast calls for average selling prices to rise, but not by as much as they did last year. Nevertheless, real estate agents believe the residential market will remain healthy, barring any upward thrust in mortgage rates.

Residential builders contacted in early March generally report new house sales running at a good pace, and some are unable to complete houses as quickly as buyers would like. Overall, developers in the Third District expect sales in 1988 to be around last year's level; however, they are not as optimistic for 1989, and some large companies are trimming their long-range development plans.

## FOURTH DISTRICT - CLEVELAND

Summary

Economic conditions in the Fourth District remained optimistic, exhibiting little change from the previous report. Manufacturing output and new orders continued to grow, fueled in part by continued improvement in exports. Employment growth in both goods-producing and service-producing sectors held unemployment rates steady. Strong auto sales contributed to a slight increase in retail sales, offsetting weak apparel sales.

Retail Sales

Auto dealers reported surprisingly strong sales during February, while retailers posted generally weak sales. Auto dealers felt that buyer incentive programs were responsible for much of the surge in sales. The sluggishness in retail sales was attributed to weak apparel sales, especially women's clothes, and to slow sales in consumer durables. Retailers continued to express concern that their lackluster sales figures were still reflecting consumer caution in the aftermath of the stock market.

Housing

Recent housing activity throughout the District was mixed. Akron area home sales fell 10.5 percent in January from a year ago, but sales in the Canton-Massillon market edged up 2.4 percent, according to monthly reports by boards of realtors in the two areas. One realtor attributed Akron's decline in home sales to a combination of local economic

conditions, poor weather in January, and the possibility that home-equity lines of credit may have reduced the number of homeowners seeking to move up to more expensive housing.

Cincinnati realtors also reported a decline in the number of home sales in recent months compared with a year ago. However, new home construction in the Cincinnati area from October through January rose 10 percent compared with the same period the previous year.

The Columbus area housing market continues to show the most consistent growth. Home sales and new housing construction are reported to be above the levels set a year ago. The strong housing market is reflected in housing prices. According to a recent survey, house values in Columbus have appreciated 110 percent over the last 10 years, exceeding price increases in the other major cities in the District.

#### Manufacturing

The export boom continues to have favorable effects on the Fourth District's manufacturing sector. Local producers reported that they are capturing some of the markets lost to imports in recent years not only because of a lower dollar but also because of more technologically advanced products. One machine tool manufacturer attributed his increased foreign sales to several years of intense engineering and marketing efforts.

Reports from purchasing managers indicated broad-based strength in manufacturing. Nearly 50 percent of the Cleveland area producers surveyed reported increased production, and only 7 percent reported declines. Representatives from some companies commented that they are producing all they can, and a few said they are even looking for

subcontractors. In the Cincinnati area, production was reported higher by over 40 percent of the purchasing managers surveyed. Only 16 percent said it was lower.

Increases in new orders and a sizable backlog of existing orders point to continued expansion of production in both areas. However, purchasers expressed some concern that steady price increases, key material shortages, and some inventory buildup may dampen this outlook.

#### Labor Markets

Ohio's employment level in February surpassed 5 million workers, marking the first time monthly statistics have reached this level. The increase of 25,000 jobs during February contributed to a slight reduction in Ohio's unemployment rate from 6.5 percent in January to its present level of 6.4 percent. Unemployment rates within various regions of the District also remained roughly the same. The Cincinnati and Columbus area reported unemployment rates of less than 5 percent, while the Cleveland and Pittsburgh area recorded unemployment rates around 6 percent.

Ohio's employment growth in January was divided evenly among goods-producing and service-producing sectors, adjusted for seasonal factors. Two-thirds of the new jobs in the goods-producing sectors came from construction, with manufacturing contributing the rest. Employment growth in the service sector was dominated by employment gains in wholesale and retail trade.

The average workweek of manufacturing workers in January dropped by half an hour to 42.8 hours.

Banking

On balance, district loan demand has been relatively flat over the last month and a half. Total loans outstanding at large banks fell at an annual rate of 2 percent from the beginning of January to mid-February. The marginal loan contraction was attributed to a large decline in consumer installment loan volume. Seasonal factors and the wariness of consumers to assume additional debt may have accounted for the recent weakness in the demand for consumer installment loans.

In contrast, the demand for business and real estate loans has picked up. Real estate mortgages outstanding grew at an annual pace of 23 percent as homebuyers took advantage of falling mortgage rates. Business loans outstanding increased at an annual clip of 12 percent.

## FIFTH DISTRICT-RICHMOND

Overview

District economic activity expanded in February, although homebuilding and housing sales were unchanged, and retail sales declined. Manufacturers reported strong growth, and they are optimistic about growth prospects in the next six months. District retailers, too, are optimistic about growth in the coming months, despite sluggish sales in recent weeks. Financial institutions report higher loan demand in all major categories, and bankers share the optimism of retailers and producers. Agriculture is reported to be in generally better condition than a year ago.

Consumer Spending

Thirty-eight percent of the District retailers responding to our regular mail survey reported declines in sales in February, while 30 percent reported increases. Many respondents indicated that they had increased discounting and promotions since the beginning of the year. Although the majority of respondents indicated no change in inventories, 32 percent reported increases. Two-thirds of the retailers expect increases in sales in the next six months, compared to 14 percent who expect declines.

Reports from department stores generally indicated weaker activity than in the retail sector as a whole. Half of the department store respondents said sales declined during February, while 25 percent said sales had increased. Nearly 70 percent experienced declines in sales of big ticket items. Department stores also reported slight declines in employment and little change in inventories.

### Manufacturing and Mining

District manufacturing activity increased in February compared to its pace in January. Forty-six percent of the respondents to our survey reported higher shipments in February, up from 34 percent who reported increases in January. Reports of reduced shipments remained at only about 15 percent. Increases also were reported in new orders, backlogs of orders, employment, and the length of the workweek. About half of our respondents reported that inventories of finished goods and raw materials were unchanged from a month earlier, while about one-third reported increases.

The prices of raw materials and finished products rose further, according to District manufacturers. One-third said they had raised their product prices, and 64 percent said the prices they paid for raw materials had risen. Almost none reported price reductions. In addition, two-thirds of our survey respondents who use imported materials noted price increases in these inputs since the beginning of the year.

Manufacturers expect their activity to continue to rise in the next six months. About 48 percent of the respondents believe their shipments and new orders will rise--a proportion almost equal to the high recorded in the early fall of 1987--while about 14 percent expect orders to decline. One-third expect the lower dollar to boost their sales this year. Thirty-nine percent plan to increase their capital expenditures in the next six months--the highest percentage reporting such expansion plans since last August.

Coal production in the District during the first three weeks of February was slightly above production during the same period last year. Although the United Mine Workers' contract expired on January 31, there were no reported work stoppages. Most union-affiliated coal companies in the District are operating under new contracts, although a few are still negotiating.

### Housing

Half of the District realtors and builders surveyed by telephone reported that home sales in February were unchanged from a year ago. The remaining half was about evenly split between those reporting increases and those reporting declines. Most of the activity in the market was in homes priced above \$150,000. In the Washington, D.C., area, however, condominiums priced near \$100,000 were selling well. In Baltimore, sales of new homes in the \$80,000 to \$100,000 range have been depressed in recent months, although lower and higher priced houses have been selling well.

### Agriculture

Our contacts in the agriculture sector report that farmland prices appear to be strengthening throughout the District, and that farmers are generally optimistic about their income prospects. Tobacco exports are expected to continue strong. Peach growers expect a good crop as the winter weather has been cold enough to keep buds from swelling and opening prematurely. However, poultry processors and pork producers are in the down phase of their cycle, with lower prices expected to persist. Subsoil moisture conditions are reported to be good in Maryland and Virginia, but conditions have been dry in parts of the Carolinas, prompting alerts of forest fire dangers.

### Financial

Our telephone survey of District financial institutions indicated slightly higher demand for commercial, consumer, and home mortgage loans in February. Two-thirds of the respondents said they anticipate increased demand for both consumer loans and loans secured by real estate over the next six months. Bankers also reported that prospects are good for commercial and industrial loans in the months ahead. Respondents attribute their optimism to lower interest rates and to their belief that rates will not rise.

## SIXTH DISTRICT - ATLANTA

Recent economic activity in most sectors of the southeast has maintained the moderate pace of the previous reporting period. Regional manufacturing continues to expand especially for textiles and paper. The petroleum and coal extraction industries are reviving. Although retailers' sales are not increasing much when compared to last year, inventories are not excessive and auto sales are improving. Loan demand has turned up at commercial banks and tourism has posted healthy gains. The outlook for agriculture is positive thanks in part to government programs. Although commercial construction continues at a low ebb, residential building is improving in some areas.

Employment and Industry. Increasing exports of nondurables continue to bolster the southeast economy. Textile mills and apparel manufacturers are optimistic that they will continue to do well in 1988. Several apparel manufacturers who were shut down a year ago now speak of labor shortages. The paper industry has been unusually strong, reflecting rapidly increasing demand from both foreign and domestic sources. Industry contacts report rising prices and exceptionally low levels of inventories for pulp and linerboard.

A number of plants in the region's petrochemical industry have announced expansion plans for 1988 and are increasing employment. Foreign sales in that sector have been greatly helped by the decline of the dollar. Oil service manufacturers are expecting a profitable year due to the continuing increase in oil rig activity both on and offshore.

Consumer Spending. Retailers around the District reported moderate or no increases in February sales over those of last year. Inventories are reported to be in line with desired levels heading into the spring selling season, although retailers indicate that they are concerned about the potential for an unwanted inventory buildup. Retailers are targeting this season's inventories to match last year's levels, an indication that they

expect no increases in sales over last year. All retailers surveyed indicated that prices are drifting upward both for foreign and domestic merchandise.

Fueled by a new wave of buying incentives, district car sales improved markedly in February from the weak sales volume in February 1987. Dealers are optimistic that the recent extension of incentive programs will continue to boost car sales at least through the end of April.

Construction. The region's stronger states (Florida, Georgia, and Tennessee) are optimistic that housing starts will increase following a pick-up in sales due to a lowering of mortgage interest rates. Meanwhile weaker states (Alabama, Mississippi, and Louisiana) report that the decline in interest rates has had little impact on both sales and construction of homes.

There has been considerable overbuilding of residential structures throughout Florida, despite high housing demand aided by the continuing influx of new residents. At the same time, Georgia is experiencing a decline in the housing industry's growth rate. January's single family building permits dropped 22 percent below the year-ago level.

The overall outlook for Tennessee is bright. The major exception is the overbuilt market in Nashville. Alabama's housing industry outlook remains optimistic due to the influx of high tech industries which are attracting residents from outside the state. Housing markets in both Louisiana and Mississippi remain weak primarily because of depressed incomes of residents; however, home prices in New Orleans have recently begun to stabilize because of improving conditions in the oil sector.

Southeast commercial construction, although emerging from its seasonal slowdown, is still being restrained by lenders who are requiring stringent preleasing before financing is provided.

Financial Services. Business loan demand is strong among small to mid-size companies, and appears to be related to the surge in exports resulting from the decline in the dollar. Part of the demand is for working capital and part for purchase of new

equipment. However, concern about the economic outlook has caused some banks to be more cautious about granting loans.

Tourism. Florida experienced a 25 to 30 percent increase in the number of foreign visitors from 1986 to 1987 and while expectations for 1988 are for some slowing, the overall outlook remains bright. There was a 12.5 percent increase in visitors from Canada in 1987 and gains in 1988 are projected at 7 percent. Elsewhere in the District, New Orleans posted a successful Mardi Gras Festival which attracted approximately 500,000 people over the 11 day period, reportedly the best attendance in years. The New Orleans Jazz and Heritage Festival next month is expected to bring at least 300,000 people to the city.

Mining, Agriculture and Forestry. Oil and gas exploration in the District is increasing. Drilling rig activity is 50 percent higher than a year ago. In early 1988 coal production has continued increasing at a rapid pace. Relative to a year ago, production is up 19 percent.

Prospects for the region's agriculture continue to improve as the government's farm program pumps large amounts of revenue into the District. The export market for grains remains active as indicated by shipments from District ports. Both cattle and pork producers are enjoying relatively high prices for their products. Florida's vegetable and citrus growers are also benefiting from good crops and strong prices.

## SEVENTH DISTRICT--CHICAGO

Summary. Expansion continues in District economic activity. Employment rose in District states in January, seasonally adjusted, except in Michigan where layoffs at auto and parts plants cut manufacturing payrolls. For February, Chicago purchasing managers again report robust increases in orders, output, and backlogs; higher inventories; rising employment; longer delays in obtaining deliveries; and widespread price increases. Reports from industrial concerns show vigorously rising demand for equipment, steel, and other industrial materials. Recently improved car sales and large first quarter production cuts, including many at District plants, are bringing auto stocks into better balance. Construction activity in the District is viewed as likely to remain at a high level in 1988, but some segments are expected to be below 1987, notably starts on commercial projects. Reports on consumer spending in early 1988 were mixed. Conditions and prospects are improving in agriculture and related industries, with land values rising and farm equipment sales higher.

Manufacturing. The industrial sector in the District continues the robust expansion evident late last year. A maker of large construction machinery reports some types of equipment on allocation, and the order backlog highest in several years. Equipment orders from paper and steel mills, for expansion and modernization, are described as "extremely strong." Rising capital spending is also reported by makers of chemicals and plastics. In response to the lower dollar, production of equipment and components is increasingly being shifted back to the U.S. from abroad, but this shift has been gradual because of contractual relationships. Demand is up for mining equipment and railcars, from low levels. Machine tool orders and backlogs are up but remain far below strong levels of the late 1970s and early 1980s. Manufacturers continue to

evaluate expansion projects cautiously, particularly in heavy equipment industries which were hard-hit by the severe downturn of the early 1980s. Closings of older, inefficient plants in the District continue to be reported, as part of producers' efforts to pare costs.

Motor Vehicles. In response to somewhat better than expected car sales, second quarter auto production schedules have been adjusted upward almost to levels of a year ago. The improved second quarter outlook follows sizable first quarter reductions in assemblies at numerous plants in the District. Permanent closing of another assembly plant, in Wisconsin, was announced recently. Truck sales and production have remained very strong.

Steel. Production at steel plants in the District continues strong. Orders for cold-rolled and coated sheet are at good levels into the second quarter, even with the cutbacks in auto output schedules. Hot-rolled sheet and plate orders have increased reflecting investment projects in the paper and petrochemicals industries. Buying of steel for construction projects has been very strong, with no seasonal downturn in bidding after the turn of the year. Increases are reported in industrial construction projects, which are mainly steel. Supplies are tight--customers would take more steel if they could get it--resulting in upward pressures on prices. The volume of steel shipped through steel warehouses continues to set records month after month.

Construction. The picture for construction in the District is mixed, with activity generally at a high level, but declining in some sectors. Building activity in the District in January was lower than last year, attributed to more normal weather this winter after exceptionally mild conditions in early 1987, and lower residential mortgage interest rates a year ago. For all of last year, contracts for construction of nonresidential buildings in District states, in square feet, were 11 percent above a year earlier, and residential contracts were 5 percent higher--both stronger performances than the nation.

Fewer starts on commercial projects in the Chicago area are expected this year, but most of the large amount of office space being built downtown is not scheduled for completion until 1989 or later, implying a high level of activity on projects already underway. Construction of Chicago-area industrial buildings is increasing, mainly light warehouse structures, after being very low. Strong leasing of Chicago-area industrial space is expected to continue. Industrial construction is also rising elsewhere in the District, including some new plants. Public works construction--highway, sewer, and water--will be strong in 1988.

Consumer Spending. February sales reports from large retailers in the District were mixed. A survey of Illinois retailers for January showed a small decline in total sales, attributed to weather, after a "healthy" gain in 1987. A contact with a major retailer believes the consumer sector is in better shape than many people think. Consumer confidence is up; wages have accelerated (though not much); and relatively large tax refunds are expected to boost spendable incomes this year. General merchandise inventories are viewed as in reasonable balance.

Farm Equipment. Unit retail sales of farm equipment continued well above year-earlier levels in January, extending a trend that began in the latter part of 1987. During the past seven months, farm tractor sales were up 35 percent from the year ago pace and the highest for the period in three years. Similarly, combine sales in the five months ending with January were up 46 percent from a year earlier and also at a 3-year high. Because of the surge in sales, unsold inventories of new tractors and combines, relative to annual sales, are now at the lowest levels since the late 1970s and early 1980s. The comparatively low inventories, coupled with expectations of at least further modest gains in sales, raise hopes that long-depressed farm equipment production in the District may begin to recover in the months ahead.

## EIGHTH DISTRICT - ST. LOUIS

Summary

The District economy continued to expand moderately, but indicators of future economic activity are mixed. Strong employment growth, for example, was spurred by gains in services and manufacturing. The construction sector, however, weakened. Consumer spending reportedly strengthened in February after a weak January, but bank lending slowed due to a sharp decline in consumer borrowing. The farm sector is in good condition for the coming crop year.

Outlook

A recent survey of 240 small District businesses revealed increasing pessimism about general business conditions over the next six months. The proportion of respondents who felt conditions would worsen was up slightly from October and was almost double the response of a year ago. In contrast, more respondents planned to make capital expenditures for plant or equipment and expand their workforces than a year ago. Furthermore, two-thirds planned no reduction in their inventories. In the recent survey, 13 percent of respondents reported an inability to fill positions for skilled workers, double the year-earlier response.

Employment

Preliminary data indicate that nonagricultural employment expanded rapidly, at a 5.0 percent rate in the three months through January compared with a 2.8 percent rate in the previous period. The major sources of job growth were services (particularly health and

business services), construction (mainly commercial projects) and manufacturing. Intermittent layoffs of auto assembly workers have continued. Most other manufacturing industries, aided by growing exports, report continued growth. Producers of fabricated metal, for example, have rapidly expanded their workforces as orders increase. Rising import prices have allowed regional producers of nonelectrical machinery and apparel to increase sales and expand their operations.

### Consumer Spending

District retail sales rose 5.3 percent in the fourth quarter from a year earlier. Rapid sales growth in Arkansas was responsible for much of the increase. Contacts report sluggish January spending, with sales of durables particularly weak. Sales improved in February, however, spurred by stronger car sales.

### Construction and Real Estate

The value of District construction contracts fell 2.0 percent in the three months through January. Growth in Kentucky and Missouri was largely responsible for a 3.5 percent advance in District residential contracts. Gains in the residential sector, however, were offset by a 8.7 percent drop in contracts for nonresidential buildings.

Home building and buying has picked up slightly from January, but is still well below year-ago levels. Refinancing of existing mortgages reportedly has increased as rates for fixed-rate mortgages dropped into single digits.

### Banking

Total loans outstanding at weekly reporting District banks rose at an 8.0 percent annual rate over the December - February period. This

figure is down sharply from the 19.6 percent rate for the same period a year ago. Both commercial and real estate lending growth changed little over the period, but consumer loans declined at an annual rate of 18.2 percent after increasing at a 25.4 percent rate over the same period last year.

### Agriculture

The District agricultural sector is in good condition after a mild winter. The winter wheat crop is rated in good-to-excellent condition. Livestock operations report only average rates of weather-related losses. Croplands, dried by the lack of rain last summer and fall, have been recharged by winter moisture and should be ready for the upcoming planting season. Crop prices will continue to be supported by government programs. Cattle prices are expected to remain strong, while poultry and pork prices should decline.

Preliminary banking data for 1987 indicate that farm loan performance at agricultural banks continued to improve. The rate of delinquent farm loans at agricultural banks fell from 7.0 percent in 1986 to 5.3 percent in 1987. The loan loss rate at agricultural banks improved, falling from 1.8 percent of all loans in 1986 to 1.2 percent in 1987. This improvement occurred in every District state except Mississippi. Commercial bank farm loans declined by 14 percent in the District in 1987; declines were noted in all District states.

## NINTH DISTRICT--MINNEAPOLIS

Despite slower consumer spending than a year ago, the Ninth District's economy held firm in the opening months of 1988. Labor market conditions remained strong. Although residential construction slowed, nonresidential building projects were under way. The district's wood products industry has been thriving, and the news for agricultural producers has been encouraging.

Labor Markets

As 1988 began, district labor markets held firm, with only normal seasonal employment declines, mainly in the construction and retail sectors. These declines brought down unadjusted employment figures in the district. Even so, Minnesota's unemployment rate in January was still a bit less than the nation's, and the Minneapolis-St. Paul metro area's unemployment rate was fully 1.6 percentage points below the nation's. Another sign of continuing labor demand in Minnesota was evident from the decline of initial unemployment claims, down 3.8 percent in January from its January 1987 level. Also, the most recent seasonally adjusted data show Ninth District employment rising in December 1987, accompanied by a drop in the district's unemployment rate.

Scattered labor-management disputes were reported recently. The largest is between flight attendants and management of the district's major airline.

Consumer Spending

Retail spending on general merchandise does not appear to have been strong in recent months. One large retail chain reports that stores it has owned for at least a year had slightly lower sales results this February than last, although year-ago sales were particularly high. Still, the sales dearth

has left the stores with above-average inventories. A second retail chain corroborates these findings. However, another chain reports that favorable weather helped it attain double-digit sales increases in February.

Sales of motor vehicles appear to be surprisingly strong, especially when last year's good performance is considered. In particular, one domestic manufacturer's truck sales were 19 percent higher through February than they were in 1987. That manufacturer's car sales were up a more modest 7 percent through February 1988.

Housing activity slowed considerably early in the year, but it may have picked up a bit in February. In Minneapolis and St. Paul, home sales were 35 percent lower this January than last, well off the record pace of March 1987. In the Twin Cities metro area, housing permits were way down in December 1987, dropping over 42 percent below year-earlier levels. And residential construction contracts in Minnesota were down 19 percent over the same period. One Bank director says that this slowing can be partly accounted for by the October 19 plunge in stock prices, which he believes has led to decreased sales of high-priced homes. But a leading Twin Cities realtor notes that the pace of sales accelerated somewhat in February.

Reports on tourist spending have been mixed. In Montana warm, dry weather has hurt some ski resorts. Adopting a novel approach to controlling state government costs, Montana plans to use state prison inmates to field out-of-state tourist inquiries. In the Upper Peninsula of Michigan, all indications point to a record year.

#### Nonresidential Construction

In contrast to residential construction, nonresidential construction for infrastructure has not fallen off in some parts of the district. While down somewhat in Minnesota during December, nonresidential building contracts

in January were three times higher than in January 1987. Most of the growth was in public infrastructure projects for highways, bridges, and sewer and water systems. A newspaper editor notes much interest in civic projects in the Fargo-Moorhead area on the border of North Dakota and Minnesota--projects including an expansion of its civic center, a new performing arts center, and a small indoor stadium. A director of this Bank's branch in Helena, Montana, mentions \$25 million in defense construction for this year at the air force base in Great Falls.

#### Wood Products

The wood products industry, one of the district's largest manufacturing industries, is currently thriving, with products ranging from lumber to chopsticks. In Minnesota alone, over \$1 billion in new capacity has been committed since 1979; the latest project, announced in February, is an expansion of capacity to make a plywood substitute. In Montana, a pulp and paper mill reports that business is very good, with prices at all-time highs. A major lumber producer notes the healthy state of the industry, with most producers operating in the black. Among producers, the pine beetle remains a continuing cause for concern.

#### Agriculture

More good news cropped up in the agriculture sector recently. The Minnesota farm price index rose in February, with increases reported both for livestock and for major crops. In addition, the federal government's Farmers Home Administration (FmHA) announced a plan to forgive as much as \$7 billion in bad farm debt. This was welcome news to over 2,000 Minnesota farmers with seriously delinquent loans at the FmHA.

## TENTH DISTRICT - KANSAS CITY

Overview. The economy of the Tenth District shows a mixed performance, but slight improvement overall. Retailers report flat to slightly increasing sales compared with a year earlier, and auto sales show some recent improvement. Farm incomes are up considerably. Home mortgage demand and housing activity are relatively weak, however, and improvement in the district's energy industry has been slowed by weaker oil prices. Loan demand and deposits at commercial banks are off slightly.

Retail Sales. Tenth District retailers generally report flat to slightly improving sales when compared with a year ago, but slightly worsening sales over the past three months. Only modest general price increases are reported. While most respondents are satisfied with present inventory levels, nearly all report continuing tight inventory management. Sales are estimated to be flat to moderately increasing in the months ahead.

Automobile Sales. Automobile dealers generally report some recent improvement in sales. Although most dealers report steady inventories, some dealers are concerned that stocks are too large relative to sales. Overall, dealers are not very optimistic about 1988 sales.

Manufacturing. Manufacturers' input prices are reported to have risen moderately in the past year, with the exception of substantial increases for steel, plastic, and aluminum. Future increases are expected to be slight, except for a moderate further increase in aluminum prices. Respondents report that current inventories of materials inputs are too high, and they plan further trimming. Capacity utilization varies by respondent, ranging from 70 percent for a paint manufacturer to virtually full capacity for a manufacturer of small electric home appliances. Only a few respondents report any problems with availability or lead times for inputs. Firms selling abroad expect further improvement in 1988.

Energy. Weakening crude oil prices have begun to erode some of the stability established in the district's energy industry last year. The average weekly number of operating drilling rigs in the Tenth District decreased from 363 in December to 307 in January. In February, the rig count fell further to 271, still about 21 percent above the February 1987 average. Soft prices and continuing uncertainty about OPEC's resolve to rein in production could postpone further improvement in the district's energy sector.

Housing Activity and Finance. Activity in the housing sector shows slight improvement across the district. Homebuilders report that housing starts are up compared with last month but down substantially from a year earlier. Single-family construction has improved while multi-family construction continues to be weak. Most respondents express optimism for single-family construction in the spring. Delivery times and availability of construction materials remain about normal.

Most responding savings institutions report that savings deposit inflows are up compared with a year ago, with some tapering off since the beginning of this year. Overall, little or no change in inflows is expected in the near future. Mortgage demand has been weak in most areas, but most respondents expect a pick-up in the spring. Mortgage rates are stable to declining, but several respondents expect some increase in the second half of the year.

Banking. District commercial bankers report slightly lower total loan demand last month. Demand for commercial and industrial loans, consumer loans, and commercial real estate loans was down slightly. Demand for agricultural loans was unchanged and demand for residential real estate loans was up slightly. The prime rate fell 25 basis points on average, and consumer lending rates also fell slightly. No further change is expected in the next month in either the prime rate or consumer loan rates. Total deposits fell

slightly because of decreases in demand deposits, conventional NOWs and large CDs. These decreases were partially offset by slight increases in MMDAs, IRAs, and small time deposits. Super NOWs and passbook savings accounts were unchanged on average.

Agriculture. Tenth District farm incomes were higher in 1987 as earnings were up substantially for livestock producers, and crop farmers generally had an exceptional year as well. While gross farm incomes were up considerably, improvement in after tax incomes may be less dramatic.

Government farm programs will be popular again in 1988. Higher crop prices are not discouraging program sign up, and a majority of farmers in the district are opting for the basic 20 percent required set aside. There is less enthusiasm for the additional 10 percent voluntary set aside, and very little interest in the 0/92 program--a program which pays 92 percent of eligible deficiency payments in exchange for idling all acres. The Conservation Reserve Program (CRP), however, has been quite attractive. Bankers report that in many areas most of the eligible acreage has already entered the program, and sign up is tapering off. In other areas, the relatively complicated requirements for program compliance have made the CRP less popular.

Agricultural loan demand appears flat for 1988, with both lenders and borrowers maintaining a conservative approach to agricultural credit decisions. A few bankers anticipate a limited increase in loan demand for livestock expansion. Some renewed activity in the farm implements market may also provide a limited source of increased loan demand.

## ELEVENTH DISTRICT--DALLAS

The District economy continues to grow at a mild pace. Expansion in manufacturing is widespread, although construction-related manufacturing is declining. Drilling activity has recently turned up and it remains well above a year earlier. District retailers say their sales are sluggish, while auto dealers note slight increases in demand. Construction continues to decline and remains the weakest sector of the economy. Total deposits at District financial institutions remain below a year earlier. Although District agricultural prices are up from a year earlier, agriculturalists generally expect a slight decline in overall farm income in 1988.

Most district manufacturers report continued growth in orders. Demand for the products of construction-related firms, however, is falling. Manufacturers linked to oil and gas drilling note a continuation of the mild expansion in sales that emerged in the fourth quarter and they also cite significant year-over-year sales growth. Although some chemical and refined petroleum manufacturers report recent slight declines in orders, they perceive these to be temporary and they expect a strong upward trend to reappear. A number of petrochemical firms are expanding capacity. Steel producers report high levels of demand and they expect growth to persist throughout 1988. Production of electronic equipment is expanding moderately. Although some defense-related manufacturers report falloffs in contract values due to defense cuts, respondents expect to be impacted less than in other regions because of the high-technology focus of much District production. Most manufacturers in apparel and in food and kindred products report expanding orders. No manufacturing respondents reported significant increases in unplanned inventories.

The District drilling rig count increased slightly in February after declining in each of the previous four months. The February rig count was 22.2 percent higher than in February 1987 but was 9.6 percent lower than its previous peak of September 1987. A recent increase in District well permit applications, a leading indicator of drilling activity, suggests continued slight gains in the rig count.

The value of District construction contracts continues its protracted decline in both residential and nonresidential building. Overbuilding remains a problem in the office and retail markets in a number of District cities including, most notably, Austin. Even nonbuilding activity, which had been a strong point in District construction, has shown some recent weakness. Issuance of residential permits is at about one-fifth its 1984 rate. Both single and multi-family residential building permits are down.

District retailers say that sales are sluggish, following a better than expected showing at the end of the year. At department stores, January sales were below a year earlier, after a year-over-year increase in December. Department store sales have been particularly weak in the Dallas-Ft. Worth area. Retail employment continues to fall in the District both as a result of weak sales and because recent mergers and consolidations have led to layoffs of redundant managerial staffs.

District auto dealers report slight upturns in sales in February, following a decline in January. Inventories for domestic models are said to be at desired levels, while inventories of imports are high and above planned levels. Dealers expect little expansion in sales until the second half of 1988.

Total deposits at District financial institutions remain below a year earlier, despite year-over-year expansions at thrifts and member banks. Concerns about the stability of District financial institutions, as a result of problem real estate loans, are widespread. One large District financial institution lost eight percent of its total deposits in one week. These concerns are said to explain the shifts out of large time deposits and into small time deposits that continue to be evident, particularly at thrift institutions. At large District banks, business and real estate loans remain below a year earlier, with particularly strong declines appearing in the business loans category.

District farmers and ranchers generally expect their incomes to fall slightly below 1987 levels, but they anticipate relatively high incomes compared with other recent years. Although District crop and livestock prices remain above a year earlier, the ratio of prices paid by farmers to prices received by them has also grown. The 1987 sale of a cooperative denim mill in West Texas has pumped about \$100 million into the farm economy of the region. The effects of that one-time income shock are increased land values and a firmer market for cotton equipment. Texas grapefruit production has finally rebounded from the 1983 freeze: 3.3 million boxes are expected this season, a 71 percent increase over a year ago. Texas cattle raisers are increasing their herds while herd sizes are declining nationally.

## TWELFTH DISTRICT -- SAN FRANCISCO

Summary

Respondents in most areas of the District continue to report moderate growth, although concerns about slowing near-term growth are rising. Conditions in resource-related industries are improved generally: agricultural conditions continue to improve for most crop and livestock producers; lumber prices remain high with low inventories; and energy-related industries--although not expanding--report activity above year-earlier levels. Residential and nonresidential construction has been weakening in many parts of the District. Manufacturing activity is mixed, with gains reported in resource-processing and export-related industries, but slowdowns reported in construction and defense-related manufacturing. Lending activity remains mixed, as lower interest rates have prevented the erosion of business, but have not stimulated increases.

Business Sentiment

Nearly all respondents anticipate slowing national growth this year, but none expects a recession. Respondents generally expect below average housing starts, slight increases in the growth of business investment, slight decreases in consumer spending growth, and significant shrinkage in the trade deficit. On average, respondents expect slight increases in both inflation and unemployment rates this year.

Agriculture and Resource Related Industries

Survey responses indicate strengthening in the agriculture sector. Higher prices, caused by increased exports and government-induced production cuts, together with lower interest rates, have helped increase land prices in most areas of the District. Crop farmers have reduced their debt burdens significantly as their incomes have risen. Grain processors report record revenues, although they expect reduced storage income this year because of reduced inventories. The domestic wine industry reports strong gains from reduced import competition. A cattle rancher reports the best conditions

since 1975 and expects conditions to strengthen further over the next 2 to 3 years. Farmers and ranchers in California, however, express concern about possible income losses arising from the imposition of Proposition 65, the state's initiative to limit the use of toxic substances.

The forest products industry reports strong prices and low inventories of logs. Respondents expect a decline in demand, however, based on reduced housing starts nationally. Pulp and paper production remains at almost 100 percent of capacity, causing sharp increases in newspaper and publishing costs.

In the mining sector, conditions are improved from year-earlier. The drilling rig count is above year-earlier, although normal seasonal declines are occurring and few in the industry expect further gains this year. Recent declines in oil prices have not yet had a significant effect on exploration and development plans, which included increased investment in Alaska. Metal mining activity continues to rebound in Arizona and Utah as a result of higher prices for copper and gold, reduced wage rates, and improved extraction technology.

#### Retail Sales

Retail sales in February were up only 2.2 percent from year-earlier, but retailers are waiting for the Easter season to get a good reading on consumer spending plans. Retailers report rising prices for some imported goods, although not all of the dollar's decline has been passed along. Inventories are reported to be at or slightly below desired levels for most retailers. Used auto prices are rising, but dealers report that consumers are waiting for new incentive programs before buying new autos. Auto inventories are up, but dealers expect reduced output by major auto makers to begin to reduce those inventories.

#### Manufacturing

The outlook for manufacturing is mixed. The falling dollar has improved the competitiveness of domestic producers, but defense and construction-related

manufacturers face slowing or negative growth. Current orders should sustain aerospace employment for the next several years, but the completion of several large defense contracts may begin to reduce employment this year in many defense-related industries. Construction-related industries expect reduced sales following the drop in housing starts. Respondents report declines in heavy equipment sales for housing and commercial construction, but report some gains in sales for nonbuilding construction. Increased prices of steel and other imported raw materials are appearing in equipment costs. Computer-related firms report rising sales, with the semiconductor book-to-bill ratio indicating a growing backlog of orders. Electronic component sales to industrial consumers also are reported to be strong with inventories declining.

#### Construction

Construction has weakened overall, although urban areas of Oregon and Washington report strong housing permits. Construction was particularly weak in Alaska (a 7 year low), Utah (down 46 percent in 1987), and Idaho. Residential and commercial construction also has slowed in California, but activity remains relatively high. Some growth is reported in nonbuilding construction in many areas of the West.

#### Finance

Lower interest rates have improved the outlook of respondents in the finance sector, although loan demand has not increased significantly. The decline in rates is generally credited with preventing a drop in loan demand by increasing consumer optimism, but does not appear to have caused an increase in demand by making loans sufficiently more affordable. Several respondents expect a refinancing boom if fixed-rate mortgages drop an additional 50 to 75 basis points. Several respondents also cite problems obtaining high-quality loan applications.