

SUMMARY OF COMMENTARY ON CURRENT ECONOMIC CONDITIONS
BY FEDERAL RESERVE DISTRICTS

MAY 1988

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SUMMARY*

Continued moderate growth of the nation's economy is again confirmed by reports from the Federal Reserve Districts. Manufacturing sector activity remains strong, with export growth a major contributor. Recent retail sales growth generally has been modest. Housing activity in most Districts has shown some recent improvement, but remains below that of a year earlier. Nonresidential construction activity is mixed. Conditions appear to be improving in resource industries, including energy where there is some pickup in oil drilling activity. Farm sector conditions are also continuing to improve. Generally stronger loan demand is reported at banks in a number of Districts.

Consumer Spending

Recent improvement in retail sales is best described as generally modest, with this year's early Easter affecting comparisons with a year earlier. Several individual District reports use words like sluggish, slow, and modest in describing recent sales growth (New York, Philadelphia, Cleveland, Atlanta, and Minneapolis). Somewhat greater strength is suggested by reports from Richmond, St. Louis, and Boston. Where specific lines of goods are mentioned, apparel sales are generally described as weak, while strength in sales of appliances and home furnishings varies from region to region. General merchandise and department store sales appear to be faring better than sales at specialty stores. Retail inventories are being closely monitored, with aggressive markdowns reported in several Districts in order to keep inventories under control. Several Districts note strong sales for

*Prepared at the Federal Reserve Bank of Kansas City based on information gathered before April 26, 1988.

domestically produced new cars, including light trucks and minivans. Inventories of new cars were generally described as satisfactory to tight.

Manufacturing

Manufacturing sector activity remains strong. The strength appears to be generally broad-based, with export growth often cited as a major contributor. Boston, Philadelphia, and Richmond note general strength in both shipments and orders. Chicago remarks on the reopening of export markets for heavy trucks. Atlanta reports apparel exports are growing and textile mills are running at or near capacity. St. Louis and Dallas, however, note some slowing in textile and apparel production. Chicago and Cleveland report continuing strength in heavy industries such as steel and machine tools. Chicago reports strength in steel mill orders into the third quarter. Steel fabricators have orders backlogged into the third quarter, and service center business is also strong. Prices are up for most types of steel, with some types in short supply. Manufacturers' purchasing agents in both the Chicago and Kansas City Districts are seeing longer delays in deliveries of goods ordered. Respondents are also concerned about higher materials prices, especially for steel, paper, plastics, and aluminum.

Construction

Housing sector activity in most Districts has shown some recent improvement, but remains below levels of a year earlier. Nonresidential building activity is mixed. According to the Atlanta Bank, the decline in nonresidential construction activity in the southeast is slowing. Chicago reports modestly higher nonresidential building activity and expects a higher level of industrial construction this year. The pace of office leasing has improved in the New York District and considerable hotel construction is scheduled or underway in New York City. Overall construction activity in the

Dallas District continues to decline with little evidence of recovery in the near future.

Resource Industries

Conditions appear to be improving in resource industries, including the energy sector. San Francisco, Minneapolis, and Kansas City all report some pickup in oil drilling activity, but Kansas City notes further improvement may be limited by uncertainty about oil supplies and prices. Dallas notes a sharp rebound in oil drilling, concentrated in Texas where the rig count increased for the first time in six months; further gains are expected. Forest products companies and copper mining in the San Francisco District are benefiting from strong prices and improved cost structures. Minneapolis reports its important forest products industry is currently running at capacity.

Agriculture

Conditions in the farm sector generally continue to improve. Farm incomes are expected to be relatively high again this year but not as high as in 1987, due primarily to smaller government payments and smaller returns to the livestock sector. Farmland values are generally rising in most areas and farm financial conditions appear to be strengthening. Dallas reports the number of farmers and ranchers leaving agriculture is slowing considerably. Cotton acreage planted is expected to increase substantially in the Atlanta and St. Louis Districts. Dry conditions are of some concern in several states, with water shortages of increasing concern in the San Francisco District where livestock producers are already suffering and crop irrigation may be reduced this summer.

Banking

A number of Districts report stronger loan demand. Relatively strong loan demand in the Cleveland District is concentrated in business lending,

with smaller gains in consumer installment lending. Consumer lending growth is mentioned by several Districts, with Richmond and Philadelphia noting some strength in the demand for home equity loans. San Francisco, however, reports overall loan demand appears about unchanged. Also, Dallas says loans in that District are generally still in a slide, with business loans declining most. Dallas also notes, though, that the rates of decline in loans at large banks slowed markedly in the first quarter compared with the last half of 1987.

FIRST DISTRICT - BOSTON

Most of the First District manufacturing and retail firms contacted are satisfied with their recent performance. Sales are generally up, inventories are satisfactory, and price increases have been modest. Most retailers report sales in March and April ahead of a year earlier and in line with plans. Planned spending on warehousing, new stores, and store remodeling is higher this year than last. Manufacturers sum up the first quarter of 1988 with a relieved "so far so good." With some exceptions, new orders and shipments have risen by double-digit percentages. While optimistic, manufacturers are watching carefully for any signs of deterioration later in the year.

Retail

First District retailers generally reported rising sales in recent weeks, but their experiences were quite varied. While one upscale merchant enjoyed a 20 percent sales increase in March, another reported a slight decline in revenues during the first quarter of 1988. Two chains -- both with locations concentrated in rural and suburban areas -- reported a steady 10 percent advance over year-ago levels. But a third serving the same market saw its sales momentum decline as year-to-year increases fell from double digits in January to barely positive in March. Meanwhile, prices were stable to 3 percent above year-earlier levels.

Most retailers are pleased with their profit picture despite rising costs. A shortage of retail clerk and warehouse labor has resulted in higher compensation and turnover as well as suboptimal staffing levels. Rent, insurance, and other overhead costs are also rising. Gross profits generally expanded in line with sales, however, and net income grew.

A movement toward increased quality characterizes local retail markets. Both upscale merchants and discounters described changes intended to upgrade their merchandise mix, especially apparel.

Retailers are optimistic about future growth and are confidently proceeding with various capital spending initiatives. All are adding outlets, some are expanding or remodeling, and some are investing in more warehouse space and associated material handling and computerized inventory control equipment.

Manufacturing

Factory contacts report that shipments are 10 to 14 percent above year-ago levels in real terms, while new orders are running flat to plus 10 to 12 percent. Producers with customers in financial services, housing and the government sense some softening in those sectors and newspaper accounts suggest that computer sales are slower than expected. By contrast, retailers' purchases, which had been weak early in the year, were strong in March. Other areas of strength included commercial instruments, electrical cables and electronic components, particularly for the automotive market.

Inventories are generally termed satisfactory. While two respondents reported improvements over the fourth quarter, two others indicated that inventories are a bit too high.

Most First District manufacturers reported small increases in materials prices. Items singled out included paper, steel and imported woods. Postage costs were also mentioned as were shortages of DRAMs. Manufacturers' own prices were flat to up 4 percent, except for computer makers and government contractors whose prices are falling.

The employment picture is mixed. One firm mentioned employment gains of 10 percent. Another, active in government work, reported a significant decline. Elsewhere employment was flat to down slightly. Two recurring themes were the tight labor market in Massachusetts and Rhode Island and the impact of increased labor productivity in reducing employment needs.

A majority of First District respondents plan to increase capital spending from modestly to significantly above last year's level. In general these expenditures reflect replacement needs and a continuing emphasis on installing more efficient equipment. A couple of the firms plan some expansion - in the Southwest, Canada and abroad. Among those planning to reduce capital spending were some high tech firms; excess capacity was the reason given.

Most First District manufacturers are encouraged by the year's performance so far. They expect a "reasonable" year with revenues up 10 to 15 percent and earnings up even more, thanks to continuing efforts to cut costs. However, several contacts also mentioned that they will be watching very carefully for any signs of weakening later in the year.

SECOND DISTRICT-NEW YORK

Developments in the Second District economy varied among sectors in recent weeks. General business conditions improved moderately and commercial leasing in much of the District expanded. Residential construction has been somewhat sluggish, however, and retail sales have generally been below plan. Small and medium-sized banks also report that demand for home mortgages has been weak.

Consumer Spending

Sales at District retail stores have been rather sluggish since the last report. This was particularly true in February when all respondents experienced disappointing results. Sales improved in March, but generally remained somewhat below expectations. While one retailer attributed the recent slowdown to continuing resistance to the current styles in women's apparel, others noted a more widespread sluggishness which they were unable to explain.

For February, year-to-year changes in District retail sales ranged from -6.7 percent to +2.0 percent, results which ran from slightly below to "way behind" plan. Aided by this year's early Easter, over-the-year gains of from 3 percent to 11 percent were registered in March--results which ranged from somewhat below to slightly above plan. Despite the lackluster sales, inventories are generally reported at relatively comfortable levels as a result of close monitoring and some aggressive markdowns.

Business Activity

The Second District's economy expanded moderately in recent weeks. The percentage of purchasing managers reporting improved business

conditions in the Rochester survey jumped from 38 percent in February to 53 percent in March. The Buffalo survey registered a smaller rise. A much larger percentage of surveyed Buffalo firms also reported lower inventories in March than in February.

Recent developments point to some further strength in the District's economy. In Syracuse, General Electric has begun working on its almost \$1 billion submarine combat system contract which the company was awarded by the Navy late last year. In the Buffalo area, Sierra Research just received a \$100 million award from the Air Force for the production of computerized flight inspection systems with the possibility of additional support work later on as well. Plans have been announced for the construction of several large co-generation plants that manufacturing firms hope will reduce energy costs. A recent negative announcement was that Grumman Corporation will reduce its workforce on Long Island by 2300 employees as a result of losing a Navy aircraft bid. With Long Island's February unemployment rate at 3.3 percent, observers anticipate that these workers can be absorbed without much difficulty.

Residential Construction and Real Estate

Activity in the District's residential construction market has been somewhat sluggish due in part to the unusually cold weather this spring season. Homebuilders report some recent improvement and anticipate much more traffic and interest in the months ahead. However, few expect the 1988 pace to match that in recent years. Less pent-up demand, a growing shortage of suitable land in some areas, and the high level at which home prices seem to have stabilized are cited as factors which are expected to contribute to some slowing this year.

The pace of office leasing generally has improved within the District. Demand for office space in midtown Manhattan picked up substantially in recent weeks, but downtown Manhattan leasing remains slow. Elsewhere in the metropolitan area demand is reported strong. Some Fairfield County spokesmen state that a real upturn is occurring. The relatively few new office projects currently planned there and in Westchester County are generating some optimism that the high vacancy rates may soon decline. Hotel construction is one category in which considerable building is either planned or underway--most noticeably in Manhattan where four hotels are currently being built and four more are scheduled. Higher rentals, relatively high occupancy rates, and a record number of visitors are spurring this development.

Financial Developments

According to loan officers of small to medium-sized banks in the Second District, demand for home mortgages is rather weak. Though the number of loan applications has recently begun to rise, most bankers attributed this to seasonal factors. Some officers, especially those in the New York metropolitan area, believe that the stock market unrest has made some potential homebuyers wary. Given the relatively low mortgage rates, buyers currently prefer fixed-rate loans. However, most bankers expect that interest rates will rise by the end of the summer and demand will shift back to adjustable rate mortgages with their typically lower introductory rates. Demand for home equity loans is still strong, but considerably below last year's level when they were heavily promoted. Nearly all respondents believe the high cost of housing has resulted in a significant drop in the percentage of first-time homebuyers. This trend seems to have become more pronounced in the last two years. Increasingly, those in the real estate market are either trading up to a better home or buying vacation homes.

THIRD DISTRICT - PHILADELPHIA

The Third District economy is growing at a moderate pace in April. Manufacturing activity has picked up somewhat during the month and factory payrolls have grown. Retail sales have advanced modestly for department and general merchandise stores, but remain weak at specialty stores. Bank lending to businesses has improved and consumer lending has increased slightly. Deposit growth has fallen below banks' expectations.

Businesses contacted in April have altered the forecasts they made earlier this year, but generally foresee a continuation of current trends. Area manufacturers are optimistic about the next six months -- a turnabout from opinions expressed in the last two months -- but still see only slow growth ahead. Department store officials have lowered their sales forecasts for the year, but still predict gains, while specialty merchants see no improvement in the near future. Bankers expect continued growth in business lending, slight expansion in consumer credit, and a possible slowdown in the growth of real estate lending by year-end.

MANUFACTURING

Manufacturing activity in the region is accelerating, according to the April Business Outlook Survey. Overall, survey respondents stepped up operations a little more briskly during the month than they did in the first quarter. More than one-third of the firms polled in April said business was improving while only one-tenth indicated slower business compared to March. Conditions are similar in the nondurables and durables sectors, although durable goods makers reported a relatively greater increase in shipments for the month.

Most measures of industrial activity reflect improvement. Shipments are increasing, allowing area plants to work down inventories; but the current rate of shipments is also keeping pace with new orders at local firms, so order backlogs are only steady. The employment situation remains positive: more firms reported hiring workers than reported cutting back payrolls in April, marking a year of continuous growth in jobs at surveyed companies.

Industrial prices continue to rise, according to survey respondents. Among firms contacted in April, 57 percent report higher input charges compared to March, and 30 percent are raising the prices of their own products.

Looking ahead, positive views edged out negative forecasts among area manufacturers in April, reversing the pessimistic balance of opinion that characterized the previous two months. Overall, however, survey respondents remain cautious. They expect some increases in new orders and shipments over the next six months, but they do not anticipate demand improving enough to push up order backlogs. Local firms also plan to boost payrolls slightly, but they will hold capital spending to the current pace.

RETAIL

Third District retailers report mixed results. Department store executives contacted in late April said sales in March ran comfortably above the year-ago period, prompted by an early Easter this year, and some of that momentum was carrying through April. General merchandise stores in the mid- and low-priced ranges indicate similar results. Specialty stores generally report disappointing performance in sales and profits. Women's apparel sales are running below a year ago while many stores must meet higher expenses resulting from recent expansion. Sales of appliances and electronic goods are flat to down compared to last year. Retailers say increased prices for imported items in these categories have hurt sales.

Looking ahead, Third District retailers expect a continuation of current trends. Department store officials are guardedly optimistic; although they see no negative developments on the horizon, they are trimming their sales forecasts from predictions made earlier in the year. Specialty merchants foresee no turnaround in sales immediately ahead and they are focusing on cost-cutting steps to bolster profits. Overall, retailers in the region expect sales growth in 1988 to match or only slightly exceed inflation.

FINANCE

Total loan volume outstanding at major Third District banks in March was approximately 9 percent above the year-earlier amount. Bankers contacted in April reported a slight pickup in the pace of growth. Commercial and industrial lending is advancing, especially in fixed-rate loans to middle market companies. Consumer lending is described as improving, but not strong. Auto leasing and home equity lending are the best performing categories; credit card loan volume is up only slightly from last year. Real estate loan growth remains strong, continuing a trend that has been running for more than a year in the region.

Bankers expect continued improvement in business lending in the months ahead, reflecting healthy conditions in the manufacturing sector. Although some improvement in consumer loan growth is noted currently, bankers do not expect strong performance in this category. Some reservations are also being expressed about real estate lending: most bank credit officers forecast some softening in this area by the end of the year.

Bankers note a falloff in deposit growth and some banks have boosted rates on short-term certificates of deposit to gain funds; others are tapping the money markets more than they had planned. Lackluster deposit growth is prompting reevaluations of planned asset expansion at some banks.

FOURTH DISTRICT - CLEVELAND

Summary

Economic conditions in the Fourth District generally continued to be positive. Auto sales remained strong, but other retail sales continued to be sluggish. Although the unemployment rate in Ohio rose to 7.7 percent, employment levels remained above 1987 levels, and further hiring is planned at businesses throughout the District. The manufacturing sector continued to show strength, though fewer firms reported increases in orders. Bank loans outstanding rose significantly, largely from a pickup in business lending.

Retail Sales

Department store sales in this District are growing slowly, if at all, in current dollars and are constant or declining in constant dollars. Apparel sales are the weakest, while furniture and appliance sales are still increasing, albeit more slowly than in 1987:IVQ. Furniture, appliance, and apparel sales are weaker in specialty stores than in department stores. A major department store chain reports that only part of its decline in current dollar sales in the first half of April compared to a year ago is accounted for by this year's earlier-than-usual Easter shopping season. Following its disappointing first-quarter results, another major chain lowered its forecast for sales growth for 1988 from 6 percent nominal to 3 percent nominal, which is expected to mean 0 percent real growth.

Inventories rose last quarter at most department stores, and are uncomfortably high at some stores. In general, inventories are higher than desired levels at specialty stores rather than at department stores. A

representative of one major retail chain asserts that although the retail inventory/sales ratio is too high, it is nevertheless overstated because the sales reflect price discounting, while inventories do not.

The auto market is quite strong in this District. Dealers report strong new car sales, and several report that inventories are, or soon will become, inadequate. Used car sales are also robust. Dealers say that sales incentives have become much less important in closing sales than in previous months and have little effect in stimulating customer inquiries. They attribute the first-quarter decline in imported cars' market share to the improved price competitiveness, quality, and style of domestic cars. Dealers expect the trend to continue and do not think it is a result of the domestic manufacturers' sales incentives.

Labor Markets

After a year of progress in narrowing the gap between the national unemployment rate and the state rate, the seasonally adjusted unemployment rate for Ohio rose from 6.4 percent to 7.7 percent in March.

However, other indicators of labor market activity remain strongly positive. The labor force continues to grow, and employment remains above the level reported in the latter part of 1987. In addition, employment prospects for the second quarter of 1988 are up over those of a year ago in most metropolitan areas in the District. Hiring plans are particularly strong for companies in Cleveland, Dayton, Toledo, Warren-Youngstown, and Erie, Pennsylvania. Industries with the most consistent hiring plans in the District are construction, finance-insurance-real estate, services, and wholesale-retail trade. Durable and nondurable manufacturers appear to be mixed in their hiring plans.

Foreign companies have continued to open facilities in the District. For example, in March, a Brazilian windshield wiper maker announced its intention to establish a subsidiary and warehouse in Dayton. At the same time, a major Japanese electric-equipment manufacturer made public its plan to manufacture jumbo television tubes in Dayton.

Manufacturing

Area economists are continuing to predict a good year for Ohio. There is some concern about the possibility of rising inflation and interest rates, but most analysts see the lower dollar keeping area manufacturers busy, particularly those in heavy industry such as the machine tool and steel sectors.

Reports from purchasing managers indicate continued broad-based strength in manufacturing, though there are some mixed signals for the future. In the Cincinnati area, output, employment and orders continued to be strong in March, but raw materials inventories rose at a large number of firms. In Northeast Ohio, purchasing managers generally indicated that inventory levels have stabilized. One-third of the Cleveland area producers surveyed reported increases in output and orders, though this number is down from February. Seventy-one percent of respondents reported higher prices. At least one survey participant cited the increase in exports as the cause of shortages, and expects continued upward price pressures, particularly in paper and plastics, where capacity is tight.

The steel sector in the District continues to enjoy favorable economic conditions. Raw steel production climbed almost 2 percent in the Youngstown, Pittsburgh, and Cleveland regions from February to March 1988. Prices have increased in most types of steel products, particularly in stainless steel

(flat rolled and strip). Galvanized and cold-rolled steel coils are reportedly in short supply, and price increases are expected for corrugated steel.

Banking

Loan demand has been relatively strong at District banks. Total loans outstanding at large banks grew at an annual rate of 22 percent from mid-February to the beginning of April. The loan growth was concentrated in business lending. Commercial and industrial loans outstanding rose at an annual pace of more than 40 percent. Marginal gains in consumer installment lending represented an improvement over the decline in personal expenditure loans outstanding during January. In addition, real estate lending continued to increase at a moderate pace.

FIFTH DISTRICT-RICHMOND

Overview

The District economy made modest gains in March and prices rose further. Retail sales appeared to increase at a somewhat faster pace than in previous months, although big ticket items were steady. As compared with our previous survey, a slightly smaller proportion of retailers reported increases in the prices of their purchased products and of the items they sell. Most manufacturing indicators were higher in March, but shipments were steady to lower in early April. Prices of manufactured goods and materials rose in March. Housing activity remains relatively strong. Reports of seaport activity indicated that exports grew faster than imports in March, although both rose. Tourism was strong in the winter compared to a year ago and is expected to remain robust throughout the spring and summer. The agricultural and financial sectors were little changed, although each demonstrated some signs of strength.

Consumer Spending

District retailers responding to our regular survey reported somewhat higher sales in mid-April compared to March, with half indicating higher sales and 30 percent indicating lower sales. About half said their sales of big ticket items were unchanged while the remainder was split evenly between those reporting higher sales and those reporting lower sales. The majority of respondents expect their sales to increase in the next six months.

Retailers continue to report price increases, although there was some hint of abatement in inflation in their reports for March. About one-third of our retail respondents increased their prices while 63 percent reported no change.

In the previous survey, about 40 percent had reported increases while about half indicated no change. Moreover, 43 percent indicated that the prices of items they purchased had risen, compared with over half in the previous survey. Forty-four percent of our respondents expect to raise the prices they charge sometime in the next six months. The remainder expect to make no changes.

Manufacturing

Sizeable increases in March shipments compared to February levels were indicated by respondents to our regular survey. Other manufacturing indicators rose modestly. More manufacturers reported increases than reported decreases in new orders, the backlog of orders, and material and finished goods inventories. Employment and the length of the workweek also reportedly increased slightly in March.

When respondents compared manufacturing activity in the first half of April to late March, they reported that the more recent period was not as strong. For the first half of April, more manufacturers reported decreases in shipments than reported increases. Likewise, new orders and the backlog of orders were weaker over this period than in March.

The prices of raw materials and finished products rose further in recent weeks according to respondents. Sixty-eight percent reported they paid higher prices for raw materials in March and about one-fourth said they raised the prices of their finished products over the period. Three-fourths of the respondents look for further increases in the price of raw materials over the next six months.

Most manufacturers expect their business activity to increase in the next six months. Half of the respondents believe their shipments will rise during

the spring and summer, as compared with 15 percent who expect declines. Increases are also expected in new orders. The majority of manufacturers plan to keep their inventories at current levels in the next six months.

Ports

Reports received from the three major District ports--the Port of Hampton Roads (Norfolk), the Port of Charleston, and the Port of Baltimore--noted general increases in import and export activity for the month of March. Import shipments were higher at Hampton Roads and at Charleston but were reported unchanged at Baltimore. All ports indicated an upturn in export volume in recent weeks. When compared to a year ago, recent growth in export activity was outpacing that of imports.

Tourism

A telephone survey of resorts and hotels throughout the District indicated strong tourist activity. The majority of the respondents said that the winter convention season was good in their areas, and they expect stronger activity this spring compared with previous years. Summer bookings are running well ahead of last year. Only one-fourth of respondents expect the decline in the exchange value of the dollar to boost tourism this summer.

Housing

A special survey of District builders and realtors indicated an upturn in activity in the District's housing sector. Realtors reported that sales of single-family homes rose in March and remained strong through early April. Starts of single-family homes were also up in the period. Respondents noted continued strong construction and sales activity in the homes priced in the higher end of the market. A majority of respondents expect mortgage rates to remain at current levels or to decrease slightly over the next six months.

Agriculture

Preliminary results from a recent survey of District agricultural bankers showed that farm financial conditions appeared to be strengthening somewhat but were not yet robust. Farmland prices were relatively stable in the first three months of this year, and 45 percent of the rural bankers expect farmland prices in their areas to rise over the next three months. None expect land prices to fall. Farm loan demand is higher compared to our survey three months ago, but 20 percent of the bankers still characterize demand at their institutions as below normal, while only four percent reported it as above normal. Funds are reported to be readily available at almost 90 percent of the responding institutions, and only four percent indicated that loans were refused due to shortages of funds. Interest rates were reported to be lower across all agricultural loan categories, but bankers anticipate farm loan demand will be generally weaker in the coming three months.

Financial

The reports of executives of commercial banks and thrift institutions indicated little if any change in banking activity except in consumer loans. These loans, including home equity loans, rose at a faster pace in recent weeks, although at least some of the increase may have been due to seasonal factors. On balance, the reports indicated that commercial loans and deposits were about flat to up slightly.

SIXTH DISTRICT - ATLANTA

The southeastern economy still shows moderate strength. Manufacturing of most types continues to expand. Non auto retail sales are flat when compared to last year; nevertheless, inventories are not excessive and auto sales are improving. Although commercial construction continues at a low ebb, absorption is strong in most markets. Residential building is improving in some areas. Loan demand has turned up at commercial banks. Crop acreage is up over last year because of increased planting of cotton. Petroleum and coal extraction seems to be reviving.

Employment and Industry Industrial activity remains strong in the region. Computer software and data processing firms note expanding business activity, as do health care services. Space related government contracts continue to benefit the Alabama and Mississippi economies. Pulp and paper output continues to grow with recent announcements of plans to build new mills in the southwest region of the district.

Although apparel exports are growing, imports continue to provide stiff competition for domestic firms. The outlook for apparel firms is uncertain at this time; however, price increases appear to be benefiting some domestic producers. Textile mills are operating at or near capacity, and prices are up. Carpet producers anticipate that the strong spring residential sales will further stimulate their business.

Regional appliance producers are encouraged by the recent jump in housing starts; however, they express concern over rising raw material costs for steel and plastic. Primary metals prices have generally been increasing, however a contact reports lower prices of iron and steel scrap in recent days. There has also been a strong pick up in demand for specialty metals; exports and prices are up thanks to the weaker dollar.

Consumer Spending Most retailers report sluggish or moderate sales during April following a strong March. Markdowns are prevalent as retailers try to keep inventories in line. With respectable spring sales, retailers are slightly more optimistic about summer sales; most expect real sales to equal or slightly exceed last year's levels.

Retailers are not yet experiencing widespread price increases although most expect higher prices in the near future.

Unexpected strength in this year's car sales continued through early April, surpassing both year ago District and current national sales growth. Car sales were soft in early April, but domestic vehicles were selling at a better-than-expected clip. Sales of lower-priced imported vehicles in the region continue to boom despite rising prices and intense promotional activity from rivals.

Construction The region's housing market, reacting to lower mortgage rates, has picked up a bit in sales, but construction fell by almost 8 percent from January to February. Downtown residential construction has become popular in several cities in the District.

Following a weak January, nonresidential construction has slowed its descent around the U.S. and the southeast region, down only 6 and 5 percent, respectively, from last year's pace. New Orleans and Jackson still report high office vacancy rates; other District cities report strong absorption that has helped lower vacancy rates. Developers have displayed a resiliency that continues to resist a cyclical correction and are finding selected opportunities in overbuilt office markets where significant levels of preleasing - 50 percent in some cases - must be secured before financing.

Financial Services Total loans at large commercial banks throughout the Sixth District continued to increase steadily through March of 1988. Lenders in Georgia and Mississippi note renewed emphasis on providing a wide range of services for small business clients. Contacts in Louisiana note, however, that the availability of capital is a problem for small businesses and entrepreneurs, especially those outside of New Orleans.

Across all states except Louisiana, lenders report significant increases in automobile installment loans. Banks are also expecting a last effort surge in demand for home mortgage loans before an expected rate increase in the next few months.

Tourism Early indications point to the possibility that tourism is off slightly from last year in Florida. Both Orlando and Tampa had hotel occupancy rates that were

lower during the first few months of 1988 compared to a year ago. Certain segments of the tourism industry like business travel, conventions, and cruises, however, continue to outpace 1987 levels.

Agriculture, Forestry, and Mining Acreage planted to major crops in the District will increase slightly in 1988 if farmers follow through on planting intentions. A substantial rise in expected cotton plantings offsets declines in corn, soybeans, and sorghum acreage. Recent rainfall has reduced earlier concerns about inadequate soil moisture in some areas, especially Georgia.

Crude oil production in the District continues its slow decline, falling one percent since the beginning of the year and down 2 percent relative to a year ago. The number of drilling rigs currently in operation, however, has fallen 15 percent since the beginning of the year, although it remains far above the low levels of early 1987. Even so, Louisiana Gulf Coast refineries have been operating at a much higher capacity, 91 percent recently compared with 83 percent a year ago. There is rising interest in oil and gas exploration in the Gulf of Mexico. A sale of tract leases by the U.S. at the end of March achieved a new record in bidding activity. While coal production in March fell modestly, the region's coal industry ended first quarter with a five percent production increase over the same period in 1987.

SEVENTH DISTRICT--CHICAGO

Summary. Business activity has continued to expand in the District. Employment growth in the year through February was about even with the nation, apart from sizable cuts at Michigan auto and parts plants and in related manufacturing industries. Chicago purchasing managers reported further increases in output and orders through March, accompanied by longer delays in deliveries of goods ordered and widespread price increases. However, a large diversified manufacturer reported that increases in prices paid for its inputs recently have been less widespread. Contacts see strength in orders, production, and shipments across a range of manufacturing industries. Firms in the District continue to gain from the fall in the dollar since early 1985, both in competition with imports and in export markets. Although some companies in this region face loss of business due to military spending cuts, defense procurement is more heavily concentrated in other regions. Employment cuts aimed at increasing efficiency continue to be reported. Farmland values in the District rose further in the first quarter.

Motor Vehicles. With auto inventories back in line with sales, following production cuts and a sales upturn in the first quarter, domestic car manufacturers plan to boost second and third quarter production above a year earlier. Truck sales continue robust, and second shifts are being added at two pickup truck assembly plants in the District. A maker of medium and heavy trucks has raised its sales forecast for the year. Export markets for heavy trucks are reopening. Auto makers are predicting total motor vehicle sales this year only slightly below the 1987 pace.

Steel. Order books at steel mills in the District are full for the second quarter, and the third quarter is being booked. Small steel users report an inability to get firm price quotes and delivery dates. The stronger-than-

expected auto market has improved the outlook for shipments of steel this year to motor vehicle manufacturers. Demand for structural steel is very strong, reflecting in part the upturn in construction work on factories. Japanese auto and parts plants under construction in the U.S. are reported being pushed toward rapid completion. Investments in paper plants, heavy users of steel, are increasing. Steel fabricators are backlogged into the third quarter and in rare instances the fourth quarter. Buying of steel by equipment makers has strengthened further. Steel service center business continues strong. Inventories are thought to have been rebuilt to desired levels at some service center customers whose stocks were low.

Machinery. Demand has strengthened for numerous types of machinery. A supplier of components to equipment manufacturers reports stronger demand across a range of industries. Capital spending is described as "booming." Export orders continue strong. A large machine tool maker reports very favorable sales prospects, helped by the lower dollar which has contributed to reduced import penetration. Orders for construction equipment have risen substantially. Buying of food industry machinery is said to be doing well, and special industry machinery is up moderately. Sales of farm equipment this year have been sharply above the depressed year-earlier pace.

Construction. Residential construction contracts (in square feet) and shipments of building materials--concrete, cement, and gypsum board--in the first two months of 1988 were well below a year earlier in the five District states. More normal weather and resulting construction delays, after last year's exceptionally mild winter, may have accounted for a large portion of the decline. However, the decline may also be a result of many desired purchases of new or upgraded homes having been completed in recent years; the small number of listings of existing homes with Chicago-area real estate brokers is

viewed as evidence of this. Mortgage interest rates have been relatively favorable; fixed-rate 30-year loans were offered in the first quarter at interest rates as low as 9.5 percent (plus 3 points), though they have since generally risen to 10 percent or higher. First-year interest rates on adjustable-rate loans are also edging up in the Chicago area, from around 7 percent to 7.25 percent. Nonresidential building contracts in the District states were modestly higher in total reflecting increases in Indiana and Wisconsin. Industrial construction will be higher this year, including work on steel mills in Indiana, paper plants in Wisconsin, and warehouse facilities around Chicago. Public works projects, large and small, are also expected to be strong. Prices of some construction materials have fallen reflecting slower markets, overall, and ample capacity.

Consumer Spending. Retailers in the District reported mixed results for February and March, attributed to weather and the early Easter. A survey of 243 stores in Illinois and northern Indiana showed sales in February 2 percent below a year earlier. However, sales in February 1987 were strong, reflecting the warm weather. Retail inventories are viewed as in good shape. Credit delinquencies have been falling.

Agriculture. Our latest survey of agricultural banks shows that farmland values rose further in the first quarter. District land values, on average, were 3.5 percent higher at the end of March than at the end of 1987, and 11.5 percent above a year earlier. The largest increase was in Iowa, where farmland values averaged 19 percent higher than in March 1987. Little or no increase was reported for Michigan and Wisconsin land values over the past year. Farmers in the District plan to increase planted acreage this year by 3 percent for corn and 2 percent for soybeans. Spring field work in most areas of the District is behind the accelerated pace of the past two years, but ahead of normal.

EIGHTH DISTRICT - ST. LOUIS

Summary

The Eighth District economy has continued to grow moderately. Widespread employment growth has resulted in a steady reduction in the region's unemployment rates, and exports continue to stimulate manufacturing activity and employment. Consumer spending has accelerated in recent months. Construction activity has picked up, but remains weaker than a year earlier. Bank lending has been relatively weak. The outlook for the farm sector is optimistic.

Employment

District nonagricultural employment rose at a strong 7.6 percent annual rate in the three months ending February, outpacing the nation's 4.1 percent rate. All major divisions of the regional economy, except for mining, generated new jobs. The wholesale and retail trade and the construction sectors grew most rapidly. Both residential and nonresidential construction activity increased slightly in recent months. Residential building, however, remains below its year-ago level: the value of residential construction contracts issued in the three months ending February was down 10.2 percent from a year earlier. Construction of a \$1.2 billion-dollar breakfast-cereal plant in Memphis is expected to boost area construction employment by 2,500 over the next three years.

Regional manufacturing employment grew at a 4.9 percent rate in the November-February period, despite a slight decline in Tennessee.

Much of the growth was concentrated in the production of electrical equipment, fabricated metals and transportation equipment. Growing export demand is responsible for the increased production of electric motors, appliances, consumer power tools and fabricated metals, with some plants running at full capacity. In the production of transportation equipment, growth stems from increased auto parts production in Arkansas and Kentucky and the expansion of auto assembly, which is due to better-than-expected car sales.

Exports of processed food products, including processed poultry and canned goods, have contributed to job growth in Arkansas. Meanwhile, after steady expansion last year, textile and apparel production is slowing as employment fell slightly in recent months. Some textile and apparel plants are operating at full capacity, however, and several apparel makers are expanding their productive capacity.

Consumer Spending

Reports indicate that District consumer spending has picked up in recent months. Retail sales in Arkansas grew at a 5 percent annual rate in the first quarter. Arkansas' sales were concentrated in incentive-induced auto sales while other sales, particularly those of clothing and in restaurants, continued to be quite sluggish. Sales in Kentucky and Tennessee also have accelerated, particularly for home appliances and furniture. Contacts report that the prices of some building materials, including plastic pipe and wiring, have increased rapidly in Louisville.

Banking

Total loans at weekly reporting District banks grew at a 5.9 percent annual rate for the first quarter, down from 13.2 percent for the same period last year. Commercial loans grew at a 15.5 percent rate, similar to their growth in the first quarter of 1987. Both consumer and real estate lending were considerably weaker than a year earlier. On April 19, two of the largest banking companies in the District announced a plan to merge, which would create the largest banking company in the Eighth District with assets of \$11.6 billion.

Agriculture

The outlook for the District's farm sector is cautiously optimistic. The price of soybeans, the District's leading crop in total sales, is at its highest level in many years. Because of the high prices, local sources have reported some imports of soybean products from South America. Despite higher prices, little expansion of soybean acreage is planned because farmers are reluctant to remove acres from the government's corn program. Cotton and rice acreage, however, is expected to increase by over 15 percent because of higher prices.

Farmland values in 1987 rose in all District states except Kentucky where they fell by 1 percent. Farmers have made early progress in planting because of favorable weather; farmers in Kentucky and Tennessee, however, are worried about possible drought. The District's wheat crop is in good-to-excellent condition after a relatively mild winter. Cattle producers continue to earn profits while pork and poultry producers are experiencing lower prices.

NINTH DISTRICT - MINNEAPOLIS

The Ninth District's economy seemed to strengthen a bit in the first quarter of 1988. Labor market conditions remained favorable, and several components of consumer spending grew. The recent stability in agriculture was reaffirmed by many observers. And some positive developments occurred in the district's major resource-based industries.

Labor Markets

In the first quarter, labor market performance strengthened. Minnesota's unemployment rate dropped 1.3 percentage points between January and March, falling to 4.8 percent. In addition, Minnesota's initial unemployment claims declined during both January and February, and the Minneapolis-St. Paul help-wanted advertising index rose in those months. The favorable employment conditions extended beyond Minnesota. In North and South Dakota, unemployment rates dropped significantly between last February and this February. And preliminary estimates from Montana and Michigan's Upper Peninsula also indicate falling unemployment. In Montana, employment will be helped by job growth at Malmstrom Air Force Base, where 650 more military personnel and their families are expected to arrive by year's end.

Consumer Spending

Sales of general merchandise appeared to grow modestly. Two major chains operating in the district report reasonable year-over-year sales growth in March, although these reports reflect last April's Easter sales. Another smaller chain reports slack sales in the first quarter and says its inventories have started to rise. However, a group of department stores, operating in many smaller cities of the district, reports good sales increases during March and April. This favorable performance was attributed in part to in-

creased optimism about the outlook for the rural economy. None of our retail sources experienced any unusual consumer credit problems.

District managers of domestically manufactured motor vehicles report that their operations again rolled up sizable sales gains. One manager notes that his year-to-date sales were up 10 percent for cars and 20 percent for trucks. Another manager reports year-to-date sales increases of 7 percent for cars and 13 percent for trucks. Inventories were no higher than normal.

In the first quarter, home sales appeared to fall off from their rapid pace of a year ago, but year-ago sales were unusually brisk. In the Minneapolis-St. Paul metro area, home sales were off 33 percent. The most recently available figures show that residential building contracts in Minnesota were off during February. A director of this Bank's branch in Helena, Montana, notes that housing starts in Billings were negligible, but another director notes that housing prices had stabilized in Miles City, Montana.

Bank directors also say the outlook for tourist spending is favorable. According to a director from South Dakota, advance bookings for summer visits were coming in at a good clip. Another director reports that tribal gambling operations in Michigan's Upper Peninsula were doing well. And a representative of this Bank's Advisory Council on Small Business, Labor, and Agriculture reports that its members expect a 15 percent increase in Michigan's tourist activity, and an 8 percent increase in South Dakota's.

Agriculture

The district's agriculture sector continued to stabilize. Although the Minnesota farm price index showed a 1 percent decline in crop prices between February and March, this still left prices 12 percent higher than a year earlier. Beef-cattle prices reached their highest level on record and, as a director from South Dakota notes, sheep prices were good, too. Of the

rural bankers responding to this Bank's quarterly survey of agricultural credit conditions, 61 percent believe that first-quarter farm profits were higher than a year earlier. More bankers also believe that farmers purchased more farm equipment. And the surveyed bankers placed fewer farmers at their debt limits than they did a year earlier. But some North Dakota bankers mention that a shortage of boxcars has made grain shipment difficult. And several observers report excessively dry conditions in parts of Montana and the Dakotas.

Resource-Related Industries

Some positive developments occurred in the district's resource sector. Drilling in the oil patch of western North Dakota appears to be picking up, though it is not nearly as active as during the better years of 1983-85. In Montana, interest in new mining ventures is running high: four new gold mines and a silver and copper mine have been proposed. New processing technology is expected to help a big iron-ore mine in Michigan's Upper Peninsula. And this area's slightly bigger forest products industry is currently running at capacity.

TENTH DISTRICT - KANSAS CITY

Overview. The economy of the Tenth District continues to show slight improvement. Retail sales are generally above year-ago levels, and unchanged to slightly improved in recent months. New car sales have also improved recently. While still weaker than a year ago, housing activity is increasing slightly as is home mortgage demand. While manufacturers' input prices are generally rising only moderately, the prices of some materials are increasing more rapidly. Lead times for some materials have increased. Both manufacturers and retailers report some trimming of inventories. Loan demand and deposit growth at commercial banks are both somewhat stronger. Farm incomes will likely be below those earned last year.

Retail Sales. Tenth District retailers generally report sales above year-ago levels, and unchanged or slightly improved sales over the past three months. Overall, retailers report few price increases. Although respondents are generally satisfied with present inventory levels, nearly all have been trimming inventories and may trim further. In general, retailers expect slightly improved sales over the next several months and anticipate few price increases.

Automobile Sales. Auto dealers generally report some recent improvement in sales. Adequate financing is available for both dealer inventories and customer purchases. Dealers are cautiously optimistic about 1988 auto sales. Reports on inventory changes are mixed.

Manufacturing. Most input prices have risen only moderately in the past year, but increases for steel, plastic, aluminum, and paper products are reported to have been more substantial. Materials are generally available, but lead times have increased. Respondents report continuing efforts to reduce inventory levels, now considered somewhat high. Capacity utilization rates vary widely, ranging between 70 and 90 percent.

Energy. Crude oil prices have firmed significantly in recent weeks due to potential cooperation between OPEC and non-OPEC producers and the tension in the Persian Gulf. Nonetheless, uncertainty about supplies and prices will probably limit further improvements in the district's energy industry. The average weekly number of operating drilling rigs in the Tenth District increased slightly from 273 in February to 279 in March, about 14 percent above the average recorded in March 1987.

Housing Activity and Finance. Activity in the housing market has improved recently, but continues to be weaker than last year. Housing starts are reported slightly above last month's levels, but down substantially from a year earlier. The recent increase in activity is generally the result of single-family construction. Multi-family construction remains weak across most of the district. Most respondents report improved sales of new homes. Homebuilders report no problems with materials availability or delivery times.

Nearly all respondents report that savings deposit inflows are slightly higher than a year ago and have been steady over the last month. Inflows are expected to remain steady. Recent mortgage demand has generally increased, due mostly to seasonal factors. However, most respondents report that demand is not as strong as last year at this time. Mortgage rates are reported trending higher and are expected to stabilize or rise slightly further.

Banking. District commercial bankers report generally stronger loan demand over the past month. Demand for commercial and industrial loans, agricultural loans, and commercial real estate loans have shown the most strength, while demand for consumer loans and residential real estate loans have, on balance, shown little change. Virtually all of the respondents report no change in the prime rate over the past month, but nearly half expect some movement in the near term. Consumer lending rates have been stable and

are expected to remain so. Total deposits are reported up somewhat over a month ago. Conventional NOW accounts, Super-NOW accounts, MMDA's, and IRA's/Keough's have shown some strength, while demand deposits and large CD's have shown some weakness. Passbook savings accounts and small time deposits are, on balance, little changed.

Agriculture. Agriculture's strong income performance in 1987 is apparent in spring credit reviews at district agricultural banks. Bankers report that most borrowers had positive incomes last year, with livestock producers' incomes exceptionally strong. However, smaller government payments and smaller livestock returns will likely push incomes modestly below those earned last year. Very few farm borrowers were denied credit at district agricultural banks this spring. District bankers also report that competition from the Farm Credit System (FCS) has intensified, especially since the enactment of the Agricultural Credit Act of 1987. Interest rates offered on loans by FCS units are 50 to 100 basis points below local bank lending rates in some markets.

Crop growing conditions vary widely across the Tenth District. Soil moisture is plentiful in some areas, but inadequate soil moisture is threatening crop yield prospects in others parts of the district. Much of the progress many farmers have made toward financial recovery could be reversed by drought-shortened crop yields. Moreover, cattle feeding margins are being squeezed by continued high feeder-cattle prices and developing weakness in fed-cattle prices. With current profit margins low and a market outlook that suggests fed-cattle prices may move lower, many feedlots in the district are now operating at below capacity.

ELEVENTH DISTRICT--DALLAS

The Eleventh District economy is recovering modestly. Manufacturing continues to expand overall, but weaknesses in some industries are partially offsetting strengths in others. Despite recent increases in retail sales due to the Easter season, retailers remain pessimistic that these gains are sustainable. Auto dealers, on the other hand, are quite confident that sales will continue to be strong. Construction continues to be a drag on the region's economy. Although District farmers and ranchers anticipate relatively high incomes for 1988, they expect a slight decline from the levels of 1987. Deposits at District banks remain below year-earlier levels, while thrift deposits are expanding.

Most District manufacturers are optimistic that sales will continue to grow during 1988. Notable exceptions are in the construction-related and apparel industries. Respondents in these categories report that inventories are higher than desired and that sales are down. Manufacturers of oil field machinery and equipment portray their sales as above a year earlier, but still not strong. Petroleum refiners and chemical manufacturers say that they expect sales to continue to grow moderately while steel producers foresee increasing demand. Electrical and electronic equipment producers report rising orders. Orders for food and kindred products are expanding slightly and producers expect only small improvements in 1988.

Drilling rebounded sharply in the District states in March, renewing the strong year-over-year gains achieved in the last half of 1987.

The March gain was concentrated in Texas, where the rig count increased for the first time in six months. Recent increases in oil prices are said to portend further gains in the rig count, thereby maintaining the yearly growth in this indicator. The seismic crew count, a leading indicator of drilling, showed renewed strength in early 1988, confirming the prospects for sustained modest growth in energy industry activity.

March retail sales were substantially stronger compared to year-ago levels, but retailers attribute this to an earlier Easter season. Optimism is being tempered by preliminary reports of declines in the first half of April. Despite aggressive markdowns, inventories are said to remain above desired levels .

District automobile dealers report that first-quarter sales increased significantly from a year earlier. Domestic sales are very strong, but imports are growing more slowly than during the past few years. Prices are holding steady. Dealers are optimistic that the second quarter will show further growth, provided the District economy continues to expand overall, and they expect sales in 1988 to be much higher than in 1987.

District construction activity continued its decline with little evidence of recovery in the near future. Despite February increases in residential and nonresidential contracts, which were concentrated in Texas, total contract values declined because nonbuilding construction contracts dropped sharply. Likewise, the number of residential building permits remains low. Nevertheless, a sharp February rise in single family permits offset another decline in multifamily issuance to increase total permits. Construction employment in Texas has reached its lowest level[?] in over ten years.

District farmers and ranchers are still anticipating relatively high incomes in comparison with recent years although they do expect income in 1988 to fall below 1987 levels. Recent surveys indicate that in most areas of the District the number of farmers and ranchers leaving agriculture was down almost one-third in 1987 compared with 1986. Adjustments continue as more high-cost farms brought into production during the farm boom of the 1970's are unable to compete in the climate of the 1980's. Prices for crops and livestock are up over a year ago, but crop prices have fallen from February's levels.

Although deposits at District financial institutions fell in March from February's level, they remained above the averages for the third and fourth quarters of 1987 and were essentially unchanged from a year earlier. These overall data mask differences between deposit growth at District thrifts and at banks. Deposits at thrifts have shown growth over the last year. At District banks, however, deposit declines have been substantial, with particularly acute reductions occurring at large District banks. First quarter year-over-year declines in both the commercial bank and large District bank samples were markedly larger than for either of the two previous quarters. On the asset side, loans generally remain in a slide at the large banks, with business loans declining the most. Nevertheless, rates of decline in loans at large banks slowed markedly in the first quarter from the reductions of last year's third and fourth quarters, at the same time that growth in securities holdings has moved from positive to negative rates.

TWELFTH DISTRICT — SAN FRANCISCO

Summary

The Twelfth District economy continues to grow at a healthy pace, and this Bank's survey indicates that conditions have improved during the past two months. Consumer spending is growing slowly, but car sales have improved. Manufacturing, agriculture, forest products, and mining continue to post healthy gains. Respondents report that prices of many products have risen in recent months, but the increases do not appear to be broad-based. Where wages are increasing, in most cases the increases are less than 5 percent. Real estate activity remains mixed, with strength reported in California. Financial institutions report thin profit margins and stiff competition for high-quality borrowers.

Business Sentiment

Respondents to the Twelfth District business sentiment survey expect real GNP growth to be somewhat slower than 3 percent during the next four quarters. The proportion of respondents anticipating growth at or above three percent has grown since the last survey, due in large part to expected strengthening of business investment. As was true last time, respondents expect housing activity and consumer spending to slow somewhat, while the trade deficit is expected to improve. Sixty percent expect somewhat higher inflation, but none expects inflation to worsen seriously. Most anticipate no change in the unemployment rate, and the remainder are almost evenly divided between expecting a higher or lower unemployment rate.

Consumer Spending

The pace of consumer spending growth is reported to be stable to soft. Although some respondents noted growth rates a little slower than they were before October 19,

the March pace is reported to be stronger than it was in January and February. Some Washington state respondents report slight improvement across a broad range of products, but spending on big-ticket items such as cars, houses, and furnishings is reported to be slow in Arizona. Some southern California retailers report sluggish appliance and home decorating sales, despite booming new home sales there.

An auto dealer reports that domestic new car sales have firmed, and current inventories are satisfactory to tight. New domestic truck and minivan sales remain strong, with very lean inventories. Sales of Japanese imports, in contrast, are soft, with excessive inventories relative to sales. As a result, some manufacturers increasingly are using incentives to sell these vehicles. The used car market continues to strengthen, in terms of both activity and prices.

Manufacturing

Overall, manufacturing activity in the West continues at a healthy pace. Aluminum producers have greatly expanded their output in response to dramatic price increases. An electronics manufacturer reports order and sales improvements of about 10 percent during the first quarter of 1988.

However, cutbacks in defense spending are beginning to be felt in the West. Defense-related revenue at one large contractor fell 18 percent during 1987. While total sales for this firm are expected to set a record in 1988 due to strong demand for commercial aircraft, the pace of employment growth seems to be slowing. Job advertising patterns also suggest that aerospace employment growth is flattening out.

Agriculture and Resource Related Industries

Prices and general market conditions continue to bode well for most western farm products. However, water shortages are a source of increasing concern among western farmers, and recent rains have not been sufficient to replenish reservoirs in many areas. Livestock producers already are suffering. If irrigation is reduced this summer, some permanent plantings could be lost, and crop yields likely would fall.

Forest products companies and copper mines continue to benefit from strong prices and improved cost structures. In addition, oil drilling activity ran about 30 percent higher than its year-earlier level throughout the first quarter.

Wages and Prices

More than forty percent of respondents reported little or no increases in wages or prices. However, price increases have been dramatic for some products, including aluminum, copper, wheat, logs, wool, and steel. Finished soft goods from Europe and Japan reportedly are prohibitively priced, even for the upscale U.S. market.

Price increases for intermediate and finished products appear to have been less dramatic, although several respondents expressed concern about the possibility of substantial increases during the next six months. Consumer resistance has kept a lid on apparel price increases associated with the dollar's decline. One respondent noted that, while U.S. firms are encountering capacity constraints, substantial excess capacity abroad is likely to restrain price hikes. However, production bottlenecks in lumber and paper have shown up in increased newsprint prices.

Wages are increasing in some regions and industries, but rates of increase appear to be well under 5 percent in most cases. However, the 27 percent increase in California's minimum wage, effective July 1, could place upward pressure on wages for some California retailers, farmers, and service firms.

Construction and Real Estate

Housing activity has not recovered to the levels seen during September and early October. One large firm reports that sales activity improved slightly in March and April, but still lags far behind last year's level in most markets, except in California. Real estate development in southern California reportedly is continuing aggressively, which some attribute to anticipated growth moratoria.

Sales of new homes in Arizona are reported to be slow. The fourth quarter of 1987 was the slowest in the last ten years for southern Arizona. Commercial, industrial, and

multifamily construction in the state is reported to be at a standstill, except for some small retail projects.

Financial Sector

Overall loan demand appears to be unchanged, with respondents divided as to whether demand is strong or weak, even in similar markets. Thrift representatives report extremely thin profit margins. They are flush with funds, but competition for quality mortgage borrowers is stiff.