

SUMMARY OF COMMENTARY ON CURRENT ECONOMIC CONDITIONS
BY FEDERAL RESERVE DISTRICT

OCTOBER 1988

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SUMMARY*

Most districts report continuing growth in their regional economies. New York, Philadelphia, Cleveland, Richmond, Chicago, and San Francisco all report further expansion over the past six weeks. Four districts --Atlanta, St. Louis, Kansas City, and Dallas -- report slow or sluggish growth. Boston represents general business sentiment as cautious, and Minneapolis says business conditions have held steady.

Though conditions in agriculture vary across districts, it now appears that, in the aggregate, the drought will have a much smaller impact on farm income than was originally thought. The slump in oil prices has depressed the energy industry in the Dallas district, but the effect has been minimal elsewhere. Construction of residential dwellings, especially multifamily structures, is slow and homebuilders are preparing for further declines; nonresidential construction, though, remains healthy. The manufacturing sector continues to expand, bolstered by a growing demand for exports. The outlook calls for caution and some easing in activity, however. Retail trade remains sluggish in most parts of the country, and store operators are anticipating only modest gains in the fourth quarter. In the financial sector, demand for consumer loans remains strong, led by home equity borrowing. Business lending is holding up as well.

AGRICULTURE

Agricultural conditions vary considerably by area. In the aggregate, however, it appears that the impact on farm income of any reduction in yield

*Prepared at the Federal Reserve Bank of Philadelphia using information gathered prior to October 11, 1988.

due to the drought will be largely offset by higher crop prices in general and federal aid to affected farmers in particular. And, while livestock producers' profits are being squeezed by rising feed costs, livestock prices are heading up as well, which will allow producers to pass on some of the increased costs. Kansas City reports that some cattle ranchers are maintaining herds through the winter in anticipation of higher prices in the spring. Feedlot operators, on the other hand, are seeing profits eaten away.

MINING AND ENERGY

Dallas reports significant weakness in oil and gas drilling and indicates that the rig count in the Eleventh District has dropped by 14 percent since May. The slump has had little noticeable effect in other regions, however. While the rig count in the Atlanta District is down 7 percent from a year ago, operators of offshore installations say they would expand production if they could find qualified labor. In the San Francisco District, drillers are waiting to see if prices rebound before they change plans, and refiners and retailers are enjoying wider profit margins as a result of the drop in the wholesale price of oil.

Minneapolis reports that gold-mining operations in Montana have expanded in the last year and that the stage may be set for expansion in copper mining as well. As a result, mine employment may be headed for its highest level in that district since 1983.

CONSTRUCTION

All districts except Kansas City and Dallas report a slowing or weakening in residential construction and real estate; St. Louis and Atlanta note softening house prices as well. Overall, multifamily residential construction is weaker than single-family construction. Several districts indicate that homebuilders expect mortgage rates to head upward and are therefore bracing for

further slowing. Nonresidential construction, however, remains healthy in most areas. Chicago specifically mentions public works projects as being strong.

MANUFACTURING

Virtually every district indicates continuing strength or expansion in the industrial sector. Many cite rising exports as a primary source of demand for manufactured goods; Cleveland indicates that domestic production is displacing imports in some cases. The expansion in manufacturing spreads across a wide range of industries. Among the strongest are chemicals, paper and pulp, primary metals (specifically steel), fabricated metals, automobiles and trucks, electrical and electronic machinery, and nonelectrical machinery. Weaker industries include textiles and apparel, equipment related to oil and gas drilling, and defense-related operations.

Despite the continued growth in manufacturing and the expansion of factory employment, wage pressures do not appear to be mounting at this time. Price movements vary by region and industry, but are generally moderate.

Plans for increased capital spending by manufacturers are reported by several districts. In the New York District, major manufacturers of steel, automobiles, and electronic equipment have announced plans to establish new plants or enhance existing operations. Dallas indicates that chemical producers are straining capacity and are planning expansion. In the Philadelphia District, over 40 percent of the respondents to the monthly Business Outlook Survey say they plan to spend more on plant and equipment in the next six months.

Despite the current boom in the sector, manufacturers are becoming less optimistic about coming months. Several districts say a slight slowdown became evident in late summer and that manufacturers, foreseeing a leveling off of activity through the first half of 1989, have become very cautious. For the

second month in a row, manufacturers in the Richmond District are anticipating a drop in business activity from current levels over the next six months.

RETAIL TRADE

Although several districts report a recent pickup in sales of general merchandise, retail business can accurately be described as weak or slow in most areas. Women's apparel is mentioned by several districts as a particularly weak line. Philadelphia says a slight pickup has occurred recently in higher priced merchandise.

Despite continued sluggishness in sales, retail inventories at stores in most districts are at acceptable, lean levels thanks to strict monitoring and tight ordering policies. And, although sales remain low relative to plan, Boston, Philadelphia, and San Francisco all report difficulty in hiring qualified, in-store help and note some upward pressure on wages as a result.

Retail prices are mixed. Boston reports that prices of lower-end merchandise are fairly stable, but that prices of higher-end items are rising fairly quickly. Minneapolis says price increases have been moderate and that some retailers in that region have switched to domestic suppliers as the prices of imported goods have gone up.

Sales of cars and, especially, of trucks are reported to be strong in most districts. Cleveland reports slower sales stemming from a small inventory of 1988 leftovers and the reluctance of dealers to make price concessions to clear them out. In St. Louis, sales have leveled off after seven months of strong gains.

The outlook for retail sales can be summed up in one word: cautious. Store officials' forecasts for the fourth quarter range from "moderate" to "slightly improved." No one, however, is predicting a boom in holiday sales and most are likely to continue their policies of tight inventory management.

FINANCE

Business loan volume is growing or stable in most districts, while consumer loan demand is generally described as strong. Mortgage lending, however, has tapered off. Home equity loans, on the other hand, are reported to be strong by New York and Richmond. Philadelphia notes that some bankers are concerned about funding the growth in loans and expect to have to raise interest rates on deposits to attract funds.

FIRST DISTRICT-BOSTON

Caution characterizes business sentiment in the First District. Residential real estate sales have slowed compared with a year ago. In contrast, manufacturers' sales are well above year-earlier levels, but over one-third of those contacted have experienced softer demand since July or August. While manufacturers indicate that upward pressure on materials prices has eased, most contacts report reduced constraint on their own prices. For most First District retailers, sales fell short of expectations in September. Retailers also expressed concern with rising labor costs and selected wholesale price increases.

Retail

Sales were up slightly or flat in September according to most retail reports. One exception was building supplies; demand recovered "nicely" after a dismal period attributed to the summer's heat. Among general merchandisers, women's sportswear continues to be the weakest line. Back-to-school purchases also did not measure up to expectations. Despite disappointing sales, inventories are not out of line.

All contacts mentioned rising wages and difficulty hiring in-store help, but the price picture was mixed. Prices are reportedly stable at the lower end of the market but are rising noticeably for higher-end merchandise. For example, the cost of basic apparel is rising 5 percent, while high-fashion women's clothing is up 10 to 15 percent. Discounters

are finding low-cost merchandise in third-world countries whose currencies have not appreciated against the dollar.

Flat sales, price-cutting promotions, and rising costs are all cutting into profits. Nevertheless, capital spending plans remain "ambitious." For several merchants, however, this spending is aimed at increasing efficiency rather than expansion. Some contacts with idiosyncratic explanations for their recent poor showing are quite optimistic about the remainder of the year; others are less upbeat.

Manufacturing

First District manufacturers report that sales and orders are generally 10 to 25 percent above last year's levels; profits - when mentioned - have gained even more. Manufacturers say demand is well dispersed across a range of industries and customer groups. As exceptions, contacts mentioned that defense-related and consumer goods were relatively weak. In addition, some firms that had experienced several quarters of accelerating gains in sales and orders now report that the trend flattened late this summer.

Most First District manufacturers believe that materials price increases have leveled off. Although one firm mentioned rumors of an additional steel price increase in November, others suggest that steel and food prices have peaked. Contacts pointed out that new capacity will curb price rises for computer chips, paper, and chemicals, while the strong dollar reduced the price of imported inputs during the third quarter. By contrast, most firms seemed less reluctant than in previous quarters to raise their own prices. The 3 to 5 percent increases mentioned more than offset most firms' rising materials costs. In explaining their pricing actions, respondents mentioned a decline in discounting, competitors' price changes and their own capacity constraints.

Manufacturing contacts indicate that employment levels are generally rising, but in contrast to retailers, few found labor markets tight or wage pressures mounting. While inventories are considered a bit high, they are not seen as worrisome. In most cases, capital spending continues at last year's pace, with productivity increases and expansion the primary goals.

Half the respondents expect a recession or significant slowdown within the next 18 months. The others see favorable prospects for themselves and the economy. Even among the optimistic, however, caution prevails. For example, one corporate economist is concerned that economic activity may be less robust than widely believed because the prolonged fall in computer prices is distorting measured growth in "real" investment and GNP. Another respondent is "nervous" that talk of recession will prove self-fulfilling. A third who sees no evidence of recession has nevertheless counseled his management to "tread water." As one manufacturer who usually describes himself as "cautiously optimistic" put it, "Now I'm just plain cautious."

Residential Real Estate

Some residential realtors in the First District say activity has slowed recently; others, with an earlier summer sales peak, noted a slowdown in August and moderate comeback in the past few weeks. Most report that business is slower now than a year earlier. This weakness is attributable to cautious buyers, not to a lack of inventory. More expensive homes are generally selling better than less expensive ones, and houses are selling better than condominiums. Half the realtors surveyed foresee healthy activity through year-end; the rest think sales will fall.

SECOND DISTRICT--NEW YORK

The Second District economy remains generally healthy and registered some further modest expansion since the last report. The percentage of purchasing managers who reported improved business conditions increased and leasing activity in the District's office markets continued at a moderate pace. Retail sales were sluggish during August but spending picked up somewhat in September. Activity among homebuilders has generally been slow though there continue to be some areas of strength. Small and medium-sized banks report strong demand for home equity loans.

Consumer Spending

District retail sales remained sluggish in August when a prolonged heat wave continued in many areas. Spending picked up somewhat in September though the extent of the improvement varied. Thus far, the sales results for the new fall fashions in women's apparel have been mixed. Items cited as in stronger demand were children's back-to-school clothes, athletic apparel, electronics and toys.

During August sales at District retailers whom we contact declined from a year earlier by from 0.5 percent to 5.5 percent, results which were definitely below plan. With the unusual heat, the main items in strong demand were air conditioners and fans. September brought a general improvement in sales with over-the-year changes ranging from -2.0 percent to +10.0 percent. For the most part, sales remained somewhat below plan but retailers are hopeful that year-to-year gains will increase as the holiday season nears. Despite lower-than-expected sales, inventories are generally at satisfactory levels and actually below plan at some retail chains as a result of strict monitoring.

Business Activity

Some further expansion in the District's business activity occurred in recent weeks. During September the percentage of purchasing managers in both

Rochester and Buffalo who reported improved conditions increased--in Rochester to the highest level since March. Rochester, New York's leading manufacturing export center, is benefitting greatly from the dollar's relative weakness with its average factory workweek climbing to a record 45.4 hours at one point this year. Major exporters there include Eastman Kodak, Xerox and Bausch & Lomb.

Plans for several new projects in the District were recently announced. Port Chester, N.Y. officials signed an agreement for a \$200 million harbor redevelopment which will include condominium homes, a yacht club, boat slips, a restaurant and commercial-retail space. In another attempt to reclaim a waterfront, Buffalo officials approved a \$63 million plan which will include shops, offices, a hotel and a lakefront park. Since one of the developers of this plan was involved in the restoration of the Boston, Baltimore, and New York City waterfronts, Buffalo is hopeful that its project will also prove to be a popular tourist attraction. In the manufacturing sector, Bethlehem Steel unveiled plans to spend some \$45 million over the next few years to enhance its three remaining operations in the Buffalo area. This follows announcements made earlier that General Motors will invest \$80 million to build a new series of hi-tech engines beginning this fall and that Motorola will build a new plant in that area as well.

Residential Construction and Real Estate

Activity among District homebuilders has generally been slow in recent weeks though there continues to be some strength in upstate New York. Sluggishness in the resale market was cited as a major deterrent. Potential new homebuyers have reportedly not reduced asking prices sufficiently to sell their current dwellings, and a substantial inventory of existing homes for sale has developed. Higher mortgage rates and the satisfaction of pent-up demand during the past few years were also mentioned as contributing to the current slowdown in residential construction. Few observers anticipate improvement in the near future.

Leasing activity in the District's office market continued at a moderate pace in recent weeks. Additional leases were signed for extensive space in several

of the commercial buildings under construction on the developing west side of Manhattan and some renewed activity took place in lower Manhattan as well. Long Island continues to have one of the lowest office vacancy rates in the suburban U.S., due in part to temporary moratoriums placed by some communities on new buildings in recent years. Realtors report a turnaround in Westchester County's office market with increased demand and virtually no new supply resulting in lower vacancy rates and increased rentals.

Financial Developments

Based on a survey of small and medium-sized banks in the Second District, demand for home equity loans remains strong. Some officers stated that demand for home equity loans has never been greater, though others reported that demand is not quite as high as during the introductory period. Most expected demand will rise through early 1989 and especially during the upcoming holiday season. Approximately half of the banks in the survey indicated that they were aggressively marketing home equity loans at the present time. Because most home equity loans have adjustable interest rates, a popular marketing feature is a low cap on potential interest rate increases. Even at those banks without a promotion campaign, home equity loans comprise a large and growing share of total consumer lending. Home equity credit is most commonly used to defray expenses related to home improvement and college costs, as well as for debt consolidation. A number of bankers noted that borrowers using home equity credit for debt consolidation usually did so for the tax advantage, not because they felt pressed to reschedule overwhelming debt. However, few banks actually inquire about the purpose of the loan in the credit screening process. The officers believed that prudence by borrowers and strict credit standards have thus far resulted in very low delinquency rates for home equity loans. Many commented that home equity loans have by far the lowest delinquency rates of any consumer loan in their bank's portfolio.

THIRD DISTRICT - PHILADELPHIA

Moderate expansion in the Third District economy is continuing in October, according to indications from the manufacturing and finance sectors, and there are some signs that the consumer sector is regaining momentum. Manufacturers report ongoing improvement in business is boosting both current shipments and order backlogs. Retailers saw a slight pickup in sales during September that has continued into October. Bankers note strength in business loan demand carrying over from the summer. They also say personal loan growth is accelerating modestly as credit card outstandings are beginning to rise, adding to already healthy demand for other types of personal loans.

Views of the future for the Third District economy are mostly positive. Manufacturers generally foresee further gains, although at a somewhat more modest pace than in recent months. Confidence among retailers is rising slightly in response to the current improvement in sales and they are raising their forecasts for the fourth quarter. Bankers expect more growth in business and consumer lending through the fourth quarter but they anticipate further moderation in the rate at which real estate lending is increasing.

MANUFACTURING

Area manufacturers are reporting the ninth consecutive month of rising output in October, according to the Business Outlook Survey. Nearly 32 percent of the firms participating in the survey say business has picked up from September levels while only 5 percent note a drop. Both the durable and nondurable goods sectors are sharing in this moderate growth.

Nearly all measures of industrial activity are showing some improvement in October. New orders and shipments are up at over 40 percent of the plants in this month's survey, and order backlogs are higher at one-fourth of the firms. While delivery times remain unchanged for most local companies, 15 percent note longer lags on orders in October versus September. Employment also shows continuing strength: 26 percent of the industrial establishments covered by the October survey are adding workers, and 19 percent have extended working hours.

Price increases remain a feature of the area's industrial expansion. Over half of the survey respondents are paying more for inputs in October than they did in September, and nearly one-fourth have raised the prices of their own products. While expectations of further price increases predominate among survey respondents, the percentage anticipating further hikes has moderated somewhat from surveys taken during the summer.

In their overall assessment of the near future, survey participants foresee modest growth; 30 percent expect further increases in business over the next six months while 19 percent anticipate a slowdown. On balance, responses to the survey indicate moderate advances in new orders and shipments over the winter, and marginal gains in employment. With 41 percent of the companies polled in October planning to boost outlays for plant and equipment, capital spending should pick up as well.

RETAIL

Reports from Third District retailers in early October indicate that consumer buying has picked up slightly in recent weeks, and more stores are making year-over-year gains than was the case during the summer. While this growth in sales is noted in most product lines, there are indications that upscale stores are doing somewhat better than discount and mid-market retailers.

Store officials continue to note that labor shortages are hindering staffing efforts and forcing them to bid up wages.

Merchants are raising their sights a bit for fall and winter sales. While most store officials expect real sales for the fourth quarter to just match or slightly exceed results in the same period last year, this forecast represents a modest increase in confidence compared to earlier expectations. However, retailers do expect promotion efforts and discounting to accelerate as the Christmas shopping season approaches.

FINANCE

Total loan volume at major Third District banks in late September was about 13 percent above the year-ago level, and bankers contacted in early October said this rate of increase was being maintained. Commercial and industrial loan demand was healthy, according to bank lending officers; they report stepped-up borrowing by regular customers for working capital needs and for investment in plant and equipment.

Consumer lending, which accelerated during the summer, is still moving up, according to bankers. Demand for personal installment and auto loans continues to grow, and several large banks indicate that credit card outstandings are increasing after holding steady for the past two or three quarters.

The pace of growth in real estate lending, while still healthy, continues to taper off. Bankers note a decrease in loan requests from developers engaged in speculative projects.

Third District bankers expect loan demand to continue to grow at around its current pace at least through the end of the year. Some express concern about funding this growth in assets; while most contacts are satisfied with deposit growth at this time, several expect they will have to increase interest rates on deposits soon in order to attract retail funds to match growing loan demand.

FOURTH DISTRICT - CLEVELAND

Summary

Fourth District economic conditions have changed very little since the last report. Manufacturing output continues to expand at capacity rates, especially in durable goods sectors. New orders are strong and inventories are relatively low. Unemployment rates in many parts of the District are at or below the national level, while factory workers earnings are stable. Retail and auto sales remain slow. Banks report moderate loan demand.

Retail Sales

Major retailers in the District report that sales on average are 5 percent higher than a year ago. Since retail price increases have ranged from 3 to 5 percent over last year, the slight increase in sales represents very little gain in real volume. Inventories are reported to be lean, and ordering for winter and spring has been very cautious. Most respondents have encountered no noticeable capacity constraints at their suppliers, but one major firm has noticed longer delivery times for sewn and woven goods.

Auto dealers report sluggish sales compared to a year ago, reportedly because inventories of 1988 model cars are low and manufacturers and dealers are not making large price concessions to clear them out. Initial dealer experience with sales of the 1989 models ranges from slow to very good. Those reporting slow sales blame the rather large price increase on various new models.

Labor Markets

Fourth District labor markets have shown signs of healthy expansion without much accompanying wage pressure. For the last three months, the Ohio and Pennsylvania unemployment rates (currently 5.6% and 4.5%, respectively) have both been at or below the national rate. This has been accomplished partly because the annual rate of job creation in Pennsylvania and Ohio has exceeded the national rate during the past year. In contrast, the unemployment rate in Kentucky has risen partly because of loss of agricultural jobs from the summer drought.

Hiring projections by employers in the District suggest that employment growth will continue to be strong in the fourth quarter. Substantial increases in employment are expected by employers in 19 of the 25 District cities covered in a recent survey of hiring expectations. Hiring is expected to be brisk in the four largest cities in the District: Pittsburgh, Cleveland, Columbus, and Cincinnati. Some smaller cities, such as Akron, are expecting even larger employment gains.

Across the district, new job opportunities are expected in wholesale and retail trade, manufacturing, services, and finance, insurance, and real estate. For example, two large automobile manufacturers have announced major expansions in Northern Ohio, which will directly add over 2,000 new jobs.

Ohio manufacturing wages have fallen slightly, primarily due to a shorter workweek.

Manufacturing

Conditions in manufacturing remain very much the same as last month. The manufacturing sector is continuing its strong performance: production is up, exports are growing, and domestic production is displacing imports. Sentiment among District manufacturer's remains optimistic.

Preliminary estimates of manufacturing output in Ohio show a 4.3 percent annual increase, after adjusting for unusual weather conditions. Most of the increase comes from the durable-goods sectors. Primary metals and fabricated metals showed particularly strong growth. For example, raw steel production in Ohio rose 9.0 percent during the last three months over the same three-month period a year ago.

Output growth is expected to continue as District purchasing managers report increases in new orders and declines in finished goods inventories. However, some purchasing managers report that vendors are still having trouble meeting the demands of producers as firms continue to build up their inventories of raw materials.

Manufacturers report that production continues at capacity rates in chemicals, plastics, glass, ceramics, specialty steel, and container industries. A wide variety of commodities, particularly bearings, electric motors, and a number of chemical, steel, and aluminum products, remain in short supply leading in some cases to price increases. For example, steel prices are reported to be up 6 to 7 percent from a year ago, and zinc prices have risen 50 percent since January.

Banking

District loan demand has been moderate. Total loans outstanding at large banks grew at an annual rate of 6 percent from mid-August to mid-September. Most of the loan growth was in business and consumer lending. Commercial and industrial loans rose at an annual pace of 3 percent and consumer installment loans increased at an annual pace of 13 percent. In contrast, real estate lending has been flat, which may be attributed in part to higher mortgage rates.

FIFTH DISTRICT-RICHMOND

Overview

Economic growth apparently slowed further in the District in September, although manufacturing seemed to regain some of the strength that it had lost in August. Our September survey indicates that retail sales were flat. Slower rates of increase in prices and wages were reported in retailing as well as in manufacturing. Sales of new homes declined, as did homebuilding activity. The levels of shipments in and out of our District ports were largely unchanged.

Reports from other District sectors were mixed. Depository institutions indicated little change in commercial loan demand but continued strength in home equity loans. Farmers gave uneven reports on the fall harvest and were uncertain as to how disaster payments will be made. Resort and hotel representatives said this summer's tourist activity was above last summer's, but that fall bookings were about the same as at this time a year ago.

Participants in our surveys were also asked about their expectations for the next six months. Among producers, optimism declined for the second month in a row, but most still expect business conditions to remain the same or improve in the months ahead. Among retailers, optimism about the economic outlook remained at last month's high level. Most of the bankers contacted expect interest rates to rise, but most homebuilders expect mortgage rates to decline. District farmers who escaped the worst of the drought expect their incomes this year to be above those of a year ago, and they look for further income gains next year.

Consumer Spending and Tourism

Responses to our regular mail survey of District retailers imply that sales were unchanged in September from August, while other indicators of retail activity were mixed. Almost equal percentages of retailers reported declines, increases, and no changes in their sales. Reports of decreases in employment outnumbered reports of increases, but over three-fourths of our retailers indicated no change in employment. Inventories were said to be higher by one-third of the respondents, and lower by one-fifth. About 40 percent said they had raised wages in September, compared to about half who said they did so in August.

Sales activity varied by type of store. Among department stores, about 40 percent reported decreases in sales, and about 20 percent reported increases. Sales of big ticket items declined in 20 percent of the department stores and rose in about 10 percent. Most car dealers reported increases in sales, while most furniture stores reported no change.

Most District resorts and hotels contacted by telephone said this summer's tourist activity was higher than last summer's. Bookings for this fall are about the same as at this time last year.

Manufacturing

Manufacturing activity continued to expand in September according to respondents to our regular mail survey. Thirty-nine percent of the respondents in the District reported increased shipments and 13 percent reported declines, compared with 34 and 21 percent, respectively, in our previous survey. New orders, employment, and the length of the workweek also increased, and the backlog of orders declined. Inventories of finished goods were unchanged in September while inventories of raw materials declined

somewhat. Sixteen percent of our respondents said they raised wages in September, compared with 20 percent who raised wages in August.

Prices of manufacturers' materials have apparently continued to rise, but the pace of increase slowed for the third consecutive month. Fifty percent of our respondents said that prices of raw materials increased in September, compared with 61 percent who reported increases in August.

For the second consecutive month, manufacturers who said they expect decreases nationally in the general level of business activity exceeded the number who expect an upturn. Twenty-eight percent anticipate a decline in the next six months, while 20 percent anticipate an increase. With regard to the outlook for their own businesses, 40 percent of the respondents believe their shipments will rise in the next six months and 31 percent anticipate declines. Producers who foresee declines in their unfilled orders, workweeks, and inventories of materials and finished goods outnumbered those who expect increases.

Port Activity

No clear trend in trade is apparent from the September reports of the three major District ports--Hampton Roads, Baltimore and Charleston. Shipments in September were up slightly over August levels at Charleston, down slightly at Hampton Roads, and unchanged at Baltimore. Import shipments remained about the same at Baltimore and Charleston, but declined slightly at Hampton Roads.

Housing

District home builders' associations surveyed by telephone indicated a softening in activity in the housing sector. Builders reported that the seasonally adjusted pace of new home sales declined more in September than in

August. In addition, the level of home building in the District apparently declined further from its pace of a year ago. While most respondents reported generally slower activity, some indicated increased sales of homes priced above \$200,000.

Financial

Our telephone survey of District financial institutions indicated little change in the demand for commercial loans in September. Two banks, however, reported declines in loans for commercial construction.

Reports of the demand for residential mortgages varied widely. About the same number of respondents reported increases as decreases. Many respondents said the demand for home equity loans remains strong despite the winding down of promotional efforts.

Agriculture

Fifth District farmers gave mixed reports on their fall harvests. In the areas of extreme drought, some crops were total losses. A farmer from central Maryland reported that corn fields were not worth picking in his area. A farmer from North Carolina, however, said his state is enjoying an above normal corn harvest. The peach harvest was reported to be very good in both Carolinas. Late soybeans in Maryland and South Carolina received adequate rain and should yield well. District cotton production is up this year, partly because more acres were planted.

Total farm income in the District probably will be higher this year than last. Farm production this year is expected to match production of last year, which was also a year of drought in the District. This year, however, farm prices--including the prices of poultry, and those of most crops--have been higher because the drought was a national phenomenon that reduced supplies.

SIXTH DISTRICT - ATLANTA

The southeastern economy continues its somewhat sluggish pace overall. Weakening growth in manufacturing, largely reflecting downturns in transportation equipment, combines with a slower pace in the retail trade sector to hold total employment gains under the year-ago level. However, some sectors are performing quite well and scarcities of skilled laborers have been reported by textile and appliance producers and in oil drilling operations, though wages are not reported to be under much upward pressure. A number of industrial contacts report rising input prices and the ability to pass them on to manufactured products because of strong demand. Inventory levels are generally lean and retailers seem especially cautious to avoid overstocking problems, similar to those experienced in last year's fourth quarter. Export trade is unusually brisk across a wide range of products and growth appears to be gathering momentum.

Employment and Industry Unemployment rates have been edging up in the region lately, despite reports of some tightness in labor markets. For example, although the region's energy sector remains at a low ebb, offshore producers report they could now double their operations if they could find enough skilled workers.

Appliance producers note selected labor shortages and increased production costs due to rising raw material costs. However, it is difficult to recoup rising costs through price increases because the slowdown in residential construction is now weakening appliance shipments. The housing slowdown is also dampening lumber markets. In contrast to appliance and lumber manufacturers, the district's tire and rubber industry is faring well. Although raw material costs are rising, tire producers are able to increase prices because demand for tires is currently outstripping supply. Apparel and textile producers expressed a mixed outlook with some firms running overtime while others report that orders are short for this time of year. Most are keeping tight control over production and inventories are being cut back as far as practically possible.

Paper mills are doing exceptionally well with both export and domestic demand expected to remain at high levels for the remainder of the year and into the next. Orders are growing and prices are firm. By contrast, local aircraft and several defense related equipment manufacturers are cutting back operations because of reduced orders.

Consumer Spending September retail sales were sluggish but up slightly over August's soft performance. Most retailers are relieved that there has not been a repeat of last year's disastrous fall season and remain optimistic that sales will revive in the fourth quarter. Southeastern markets are intensely competitive. Heavy promotions and discounts accompanied by increased advertising are key ingredients of most retailers' sales strategy. In this environment, retailers are not ordering very far in advance and are keeping inventories well below those prevailing last fall. Car dealers generally were satisfied with September's strong sales performance that left them with a relatively low inventory of unsold 1988 cars.

Construction Year-to-date nonresidential construction growth in the District is running slightly ahead of the national level, but its strength varies widely across the District. Retail construction is strongest in the District's most prosperous states - Florida, Georgia, and Tennessee - and sluggish elsewhere. A significant amount of activity involves renovation of older shopping centers rather than building new space in a market where overbuilding, especially in strip centers, has led to vacancy rates well over 10 percent.

The housing industry is bracing for a further slowing of activity. The District states are just beginning to feel the impact of rising interest rates on home sales. Home prices in Atlanta dropped in August to their lowest level in over a year, and contacts report that September prices were low as well. In Florida, areas of the state such as Miami, Orlando and Tampa reported slowing sales in the third quarter as rising interest rates began to impact the market.

Financial Services Officers of small and midsized banks in the Sixth District report strong demand for consumer loans. The majority of bankers said that demand is

the same or greater than a year ago. Higher interest rates have not dampened installment loan demand at the surveyed banks and several bankers expect demand to continue brisk throughout the year.

Bank failures in District states have declined from a year ago. Sources in Louisiana, the most troubled state, report a downward trend in the number of bank closures there and prospects continue to brighten because of recent reductions in loan delinquencies and improvement in the local economy.

Tourism September tourism in the Southeast continues to show slight gains over last year in most areas. Central Florida is still undergoing a mini boom in hotel construction due to continued high occupancy rates. Builders are confident the number of tourists will continue to increase to fill these new rooms due to expanding attractions in the area.

Port Activity Port activity continues to boom, with export gains reaching double digits. In Miami, there has been marked improvement in exports of a variety of commodities including chemicals, steel, textile and carpet products, fruits and vegetables, and electric and electronic equipment, to Latin America. Clay products, forest products and chemicals are the leading sources of export growth in Savannah. Exports were also up in Tampa, largely due to a healthy increase in shipments of phosphate chemicals.

Agriculture and Mining Thanks to late-season rainfall, yields of most southeastern crops will be down only slightly or will show improvement from the previous season. However, the drought delayed development of the soybean and cotton crops increasing their vulnerability to early frosts and freezing weather. The Florida Citrus Industry expects another good year with increasing output from maturing new groves and strong prices thanks to bright prospects for new export markets.

Despite continued sluggishness, the oil industry has experienced a burst of new offshore activity in the Gulf waters off the coast of Louisiana, Alabama, and Mississippi. Oil production, however, remains down considerably over last year and the number of active rigs in the District has slipped 7 percent since the previous year.

SEVENTH DISTRICT--CHICAGO

Summary. Business activity continues to rise in the District, paced by the strengthening in capital goods and exports, and supported by the high level of motor vehicle sales. Some contacts, however, note a less rapid rate of growth in activity at their companies or in their industries. Employment in District states has risen further in the second half of 1988 though at a slower rate than in the first half. Chicago purchasing managers report continued widespread gains in output and orders, and an uptrend in inventory building, accompanied by rising prices. Vigorous demand for steel from motor vehicle, equipment, and construction markets is maintaining output near effective capacity. Construction activity appears to be holding up fairly well, but some sectors have slowed and further slowing appears likely. Sales at retailers sampled in the District were slow in August and mixed in September. The fall harvest has progressed at a normal pace, but part of the crop is of poor quality or contaminated as a result of the drought.

Steel. Mills are largely booked through year-end. Production slowed less than usual last summer as producers used vacation and maintenance shutdowns at customers' plants to reduce order backlogs. Some maintenance work at steel mills has been deferred in order to meet strong demand. Among major markets, demand for construction steel is strong, particularly for industrial projects. Orders also continue strong from makers of construction equipment and other machinery, are at a good pace from auto companies, and have risen (from a low level) from makers of railcars. However, orders for oil country tubular goods have dropped as buyers, facing lower oil prices, have tried to cut inventories. In addition, delays in pipeline construction have curtailed orders for steel from that sector.

Motor Vehicles. Car sales continue strong and truck sales appear headed for a record this year. Second shifts are being added at two truck assembly plants in Michigan. Regular production was started last month at a new auto assembly plant in Illinois which is owned jointly by a Japanese and a U.S. firm. A Japanese-owned plant which began production in Michigan a year ago plans to shift some car assemblies to that plant next year from Japan to counter the high yen.

Other Manufacturers. Demand is either rising or at a high level for most manufacturers, but some reports suggest a slowing in the pace of expansion. A large diversified producer indicates that gains in sales, though still strong, have been less rapid in the second half of 1988 than earlier in the year. A maker of corrugated shipping containers has seen some slippage in the second half from the record-setting pace of the previous two years. In contrast, a producer of capital goods reported strong gains in orders, and did not note indications of slowing growth. A maker of diesel engines is operating at capacity, with strength both in motor vehicles and nonautomotive markets. Construction machinery sales are reported up strongly. Major appliance sales, though at a high level, have trailed 1987 and are expected to slow further.

Construction. Reports on construction activity in the region have been mixed. Advance indicators such as residential and nonresidential building contracts have trailed 1987. But employment in construction has risen in the District states. Total shipments of gypsum board to the five states have been about even with last year, and shipments of cement have been rising. Strong sectors include industrial construction and public works, particularly streets and highways. Weakness has persisted in apartments, and contractors are reported less active on single-family housing construction.

Consumer Spending. A survey of Illinois retailers showed sales in August trailed the year-earlier level. Weakness was attributed to the summer heat wave. Large retailers in the District reported mixed sales performance in September.

Agriculture. Crop prices, although still high, have trended somewhat lower in recent weeks as the fall harvest has progressed at a normal pace over most of the District. Elevators have been reluctant to accept some early-harvest deliveries because of poor seed quality and the presence of aflatoxin, a highly toxic substance to humans and animals, in some corn. Testing procedures for aflatoxin are complicated and, as yet, the extent of the contamination is unknown. But concerns were eased earlier this week when the FDA reissued guidelines that will permit elevators to blend contaminated corn with clean corn to achieve tolerance levels acceptable for interstate shipments.

Recent figures confirm that farm equipment sales turned sluggish again this summer as farmers became apprehensive about the drought. However, industry analysts are looking for a modest upturn to resume by early next year. Despite the drought, the demand for farm equipment is likely to be sustained by high cash farm earnings and by a sizable increase in crop plantings next year.

EIGHTH DISTRICT - ST. LOUIS

Summary

Economic conditions in the Eighth District remain sluggish. Employment in most sectors has stagnated. Manufacturing employment has grown slightly, however, led by job gains in factories producing electrical equipment, machinery and chemicals. Retail sales remain flat, with little growth in vehicle sales or department store sales. Nonresidential construction activity increased since the last report.

Employment

District nonfarm employment has changed little over the first eight months of the year compared with the nation's 3.6 percent rate of increase. During the three months through August, all private sectors expanded more slowly in the District than in the nation. The greatest weaknesses were observed in construction, mining and services. Manufacturing employment rose slightly, growing at a 1.5 percent annual rate in the three months through August after declining at a 1.6 percent rate in the previous three months. The upturn was due largely to strong gains in three export-oriented sectors: electrical equipment, nonelectrical machinery and chemicals. Textile and apparel makers accounted for the sharpest recent decline among major District manufacturing industries. The slowdown in domestic apparel sales contributed to the closure of several regional textile and apparel plants. In the past six months, three Missouri shoe manufacturers, employing eight hundred workers, have closed permanently or have

announced their impending closure. Employment in the region's food processing industry also has declined since March.

Despite the flatness at the District level, employment in the largest metropolitan areas in the District--St. Louis, Louisville and Memphis and Little Rock--continues to trend upward. Survey results indicate considerably weaker fourth quarter hiring plans in St. Louis than in the nation. Staff reductions are foreseen in St. Louis' retail and financial sectors.

Consumer Spending

District retail sales in the three months through July were 2.4 percent higher than a year earlier, compared with a 5.8 percent national gain. Spending was particularly weak in Missouri and Tennessee where retail sales rose less than 1 percent over the year. Weak sales continued in District general merchandise stores in August and early September according to contacts. Car and light truck sales leveled off in August and September after strong gains in the the first seven months of the year. Rising interest rates were blamed for the lack of sales growth. Because retailers anticipate sluggish sales and have ordered fall merchandise conservatively, inventories are generally at satisfactory levels.

Construction and Real Estate

The value of District construction contracts rose 11.7 percent in the three months through August, compared with the 5.5 percent national average. Most of the recent regional growth was due to a 21.7

percent rise in nonresidential construction contracts. Despite the recent gains, construction contracts remained slightly below the level of a year earlier in both the District and the nation.

The number of existing homes sold in August was well above the year-earlier level in St. Louis, but the median price fell almost 5 percent. Office vacancy rates in St. Louis and Louisville dropped in the second quarter from their year-earlier levels and remained below the national average. Despite vigorous economic growth, office vacancy rates in Memphis are well above the national average and have not declined for two years.

Agriculture

The harvest of District crops is underway with few weather-related problems. Crop yields in southern portions of the District were better than expected. Growers in Tennessee, Kentucky and Arkansas report soybean yields above last year's yields. Crop losses in northern Missouri are the largest in the District, but because prices are significantly higher than last year, farm income should be little changed. Although the average farm income level will be maintained, there are wide disparities among farmers. For example, farmers who had stored crops last year received windfall gains, whereas others suffered total crop failures due to spotty rainfall and were not protected by crop insurance. Drought-related farm failures will be few because the large crops and high livestock prices of 1986 and 1987 provided a cushion against this year's setback. Recent rains have helped improve pastures and have allowed the planting of winter wheat crops.

NINTH DISTRICT--MINNEAPOLIS

Ninth District economic conditions have remained stable at satisfactory levels. Unemployment rates have not changed much. Consumer spending has been fairly healthy while inflation rates continued to be moderate. Conditions in resource-related industries have improved, and those in agriculture have remained largely unchanged.

Labor Markets

The employment situation has been reasonably good throughout the district. Between July and August, Minnesota's unemployment rate rose only one-tenth of a percentage point, to 3.6 percent; this is substantially lower than the 5 percent rate of a year earlier. In July, the help-wanted advertising index for the Minneapolis-St. Paul area was up 9.4 percent from a year earlier. South Dakota's July unemployment rate was unchanged from its year-ago rate of 3.7 percent. However, initial claims for unemployment insurance in that state were down 30.9 percent from a year ago. The unemployment rate in North Dakota, at 4.1 percent in July, was three-tenths of a percentage point lower than a year earlier. In Montana, the need for fire fighters substantially improved employment prospects. And in the Upper Peninsula of Michigan, the unemployment rate was down to 5.7 percent in July, a full percentage point below a year earlier.

Consumer Spending

Consumer spending on general merchandise has remained strong, and the prospects are promising. One retailer notes that, in the January-August period, sales at comparable stores were 25 percent ahead of a year earlier. Another retailer notes that, after a soft year in 1987, apparel sales are coming back strongly. Inventories are at acceptable levels. Retailers are optimistic about this year's Christmas sales.

Motor vehicles have been selling well. In particular, truck and van sales are reported to be up sharply over last year. One manufacturer of a domestic line reports that, even at full capacity, demand cannot be met. New models are generally expected to sell well.

Housing activity has been mixed. The number of homes sold in August in the Twin Cities area was 12.4 percent below the banner sales of a year ago. However, new housing permits issued in the whole state of Minnesota were up 9 percent during that period.

Tourist spending has also continued to increase. Despite the drought, the fall colors are an attractive sight throughout the district. Most areas contacted in Minnesota indicate good resort business, as do those in the Upper Peninsula of Michigan. In Montana, however, the fire at Yellowstone has kept the number of August tourists 7 percent below a year ago. Still, one observer thinks that a sizable number of tourists have actually been attracted by the fire.

Consumer Prices

Consumer price increases have been moderate. Retailers report some price increases as they switch increasingly from foreign to domestic buying of general merchandise. However, one retailer expects to see a slight decrease in prices of imported apparel. The drought has not affected food prices very much yet. In June, the consumer price index for the Twin Cities area was 6 percent above a year earlier.

Resource-Related Industries

Conditions in the district's resource-related industries have improved. Strikes in the wood products sector of Montana have ended. Copper mining in Montana is also picking up, with one analyst suggesting that, in the

Butte area, 2,500 new jobs might be added through 1989. Approximately 2,500 new jobs have already been added in the last two years by gold mining operations in Montana. If the copper forecast is accurate, mining employment in Montana will reach 1983's high level. The timber industry in Michigan's Upper Peninsula is also reporting a good year, with a new mill due to begin operating in 1990 and other mills significantly upgrading their facilities.

Agriculture

If rainfall returns to or exceeds normal levels, the effects of the drought on the district's agriculture sector may be milder than expected. Drought aid will significantly mitigate the effects on farmers' incomes. One analyst suggests that a farmer who normally expects to gross \$139 per acre will instead receive \$137 per acre in aid if the farmer's crop was completely destroyed. Low water levels in eastern Montana, western North Dakota, and northwestern South Dakota continue to pose some problems for cattle ranchers. But the sugar beet crop in North Dakota and Minnesota is reported to be excellent in spite of heavy rains at harvest time.

TENTH DISTRICT - KANSAS CITY

Overview. The pace of economic activity in the Tenth District is relatively slow. Retailers report a slight recent improvement in sales, as do auto dealers, and most manufacturing respondents report high capacity use rates. While retail inventories are larger than desired, manufacturing materials inventories are generally satisfactory. Housing activity is fairly stable, and home mortgage demand at savings and loan institutions is relatively weak. Loan demand at district commercial banks has been nearly constant recently, while deposits have grown modestly. While some parts of the district were severely affected by drought, higher prices and near-normal crop yields have maintained farm income in other parts.

Retail Sales. Retailers generally report weak sales compared with a year ago, but some note a slight improvement from earlier this year. A number of respondents attribute the recent improvement to greater promotional efforts. Promotional efforts have also helped hold down price increases. Retailers generally have inventories that are larger than desired, and are trying to trim them. Efforts to trim inventories are expected to continue, except for seasonal increases. Most respondents expect sales increases for the rest of the year to be moderate at best.

Automobile Sales. Most automobile dealers report steady or improved sales over the past month. Inventories are expanding as dealers receive 1989 models. Dealers expect sales to be stable or up slightly during the remainder of the year.

Manufacturing. Most respondents report that materials inputs continue to be readily available, and some shortening of lead times has occurred. The pace of price increases for inputs has apparently slowed somewhat. Most respondents are satisfied with their inventory levels, after some recent

trimming. Little further change in inventories is planned. Capacity use rates are high for most respondents, but no real bottleneck problems were reported.

Housing Activity and Finance. Activity in the housing sector remains fairly stable. Homebuilders report housing starts at or above both last month's and last year's levels. Single-family construction has improved slightly, while multi-family construction continues to be weak. New home sales are stable with some increases in inventories of new homes. No problems are reported regarding materials availability or delivery times.

Most savings and loan respondents report that savings deposit inflows are near year-ago and month-ago levels. Respondents expect inflows to remain steady or increase slightly during the remainder of 1988. In general, mortgage activity has been weak, and this weakness is expected to continue through yearend. Mortgage rates have moved in a narrow range recently and are expected to remain near current levels for the rest of the year.

Banking. District bankers report little change in banking conditions during the past month. Overall loan demand remained nearly constant, although demand for residential and commercial real estate loans rose slightly. The bankers report that the recent round of lending rate increases is drawing to a close. Most respondents held their prime lending rate steady the past month and expect no change in the near future. A few bankers, however, either recently increased their prime lending rate by 25 to 50 points or expect a slight increase. Consumer lending rates were constant to slightly higher during the month. Little change in consumer rates is expected in the near term. On average, deposits grew modestly at the respondent banks. Several bankers report a shift in savings from Money Market Deposit Accounts to time and savings certificates and deposits bearing a slightly higher rate of return.

Agriculture. Crop conditions vary widely across the district as winter wheat seeding nears completion and row crop harvest continues. Rainfall slowed the harvest of row crops during the latter part of September, but the harvest is now progressing well across most of the district. Irrigated crops are generally in very good condition throughout the district, and normal yields are expected. Dryland corn and soybeans in eastern Nebraska and northern Missouri were severely affected by the drought, and yields will be well below normal. Milo yields in Nebraska are down due to a severe greenbug infestation. In other areas of the district, however, near-normal crop yields and higher prices are helping to maintain farm incomes.

On balance, district bankers report that the rate of farmer participation in the wheat price-support program is nearly unchanged from last year's rate. On one hand, a sharply higher market price for wheat has diminished the incentive for farmers to participate in the federal price support program for wheat. On the other hand, a reduction in the percentage of wheat base acres that program participants must hold out of production encourages program participation.

The new winter wheat crop received beneficial September rains that promoted development of winter wheat pastures, but additional rainfall will be required to ensure adequate grazing conditions in many areas. In the absence of adequate wheat pastures, feed stocks could be strained during a severe winter. Ranchers would then be forced to buy high-priced feed or liquidate herds. At present, most district ranchers plan to maintain herds through the winter in anticipation of higher cattle prices next spring.

ELEVENTH DISTRICT--DALLAS

The District economy is sluggish, but there are positive signs. Orders to manufacturers are growing slowly overall. Retail sales show little increase. Auto sales expansion is weak. Construction activity is turning up. Drilling is falling in the wake of oil price declines. The drought has had little effect on District farm cash incomes because rising product prices have offset diminished yields. Economic performance varies widely across the District, with relatively strong growth occurring in Houston.

Orders to District manufacturers are noticeably above a year earlier, but growth has been slower in the last few months. There are a number of exceptions to this overall tendency, however, as sales patterns vary greatly across industries. For example, chemical producers continue to cite strong sales growth and to note capacity constraints. Expansions of plant and equipment in this industry are widely reported. Sales of paper and paperboard are rising and product prices have increased substantially, but plans for capacity expansion are rare. Orders to computer manufacturers are up markedly and respondents say that their product inventories are at undesirably low levels. Electronic equipment manufacturers also note some recent increases in sales. Construction-related manufacturers, including those in fabricated metals, lumber, and stone, clay and glass, generally cite sluggish demand except in the Houston area. Most oilfield equipment firms note that sales are weak because of low levels of drilling activity. District food processors cite

little change in orders from earlier this year, but apparel producers say their sales have been growing fairly steadily.

As a result of sluggish demand, many retailers have discounted heavily to bring inventories down to desired levels. After a protracted period of weakness, apparel sales have begun to turn up in recent weeks. Retailers expect revenues in this year's Christmas season to be moderately higher than last year's and they expect seasonally adjusted growth to continue thereafter.

Auto sales vary with the economic fortunes of District communities. Houston sales have lately shown steady growth and dealers expect past patterns to continue. In Dallas, sales are about 2 percent below a year earlier, which was a weak period. Dealers there anticipate little change in sales, aside from normal seasonal variations.

District construction activity continues to show moderate gains. The total value of construction contracts in the District has now increased, on a three-month moving average basis, for four months in a row. Although earlier increases were concentrated in New Mexico and Louisiana, Texas also showed growth in August. The gains in contract values have been led by expansion in residential building, although nonresidential has shown some slight recent expansion. District construction employment continues to decline, but the pace of reduction is somewhat slower than at the beginning of the year. Nevertheless, some Houston area industrial construction firms say they are concerned about shortages of civil engineers.

Oil and gas drilling continues to slip in response to declines in oil prices and to concerns that low prices will persist. After falling for four consecutive months, the District rig count was 14 percent lower in September

than in May. Respondents expect drilling activity to remain low over the next four quarters. Recent declines in well permit applications and a drop in the price of West Texas intermediate crude oil to below \$13 per barrel offer bases for concerns about the near-term future of extraction activity in the District.

Cash income to District agriculture is anticipated to reach predrought expectations, in part, because some reduced yields have been offset by increased prices. For example, while District sorghum yields are down 25 percent from a year earlier, prices are up by 58 percent. Corn yields are down by less than 2 percent, while prices are up by 47 percent. The increasing grain prices are squeezing profit margins of livestock producers, whose product prices have risen by far less than the cost of feed. The fortunes of cotton farmers are diminished from a year ago, as prices have dropped 24 percent and yields are down by 20 percent.

TWELFTH DISTRICT -- SAN FRANCISCO

Summary

The economy of the Twelfth District continues to grow, with little sign of a change in direction. Growth remains strong in the Pacific Northwest and California, and the weaker economies in other parts of the District show few signs of further slowing. The Business Sentiment survey reveals that respondents are becoming more pessimistic about future national growth and unemployment, but they report few signs of an impending slowdown. Retail sales improved in September, although they remain generally lackluster. Construction has been strong in the Northwest, while slow in Arizona and Utah. Housing prices continue to boom in Southern California, Washington, and Oregon, although some slowing of sales is reported in Northern California. Manufacturing remains strong in aircraft, electronics, paper, aluminum, and machinery. Output in forest products industries has slowed, but remains at a high level. Agriculture remains strong in the District, while gains in refining profits have offset the negative effect of falling oil prices on production in the energy sector.

Business Sentiment

Continuing the trend reported last month, respondents have become more pessimistic about GNP growth. Over 40 percent of the respondents to the Twelfth District Sentiment Survey expect growth to slow, up from 34 percent in September. Expectations about housing starts remain low, with 83 percent anticipating further slowing, and no respondents anticipating an improvement. Concern about inflation has moderated since the last report, although concern about unemployment is increasing.

Despite a drop in expectations about overall growth, the respondents did not report any immediate signs of slowing in the regional economy. The rapidly growing Northwest is expected to continue to boom, while the slower-growing areas see no signs of further slowing.

Retail Sales

Retail sales improved in the District in September from August levels, but overall activity remains sluggish. Retailers report softer-than-expected sales in September, although one respondent in Washington reports a 14 percent rise in retail sales over last year. Classified advertising volumes continue to drop in Los Angeles and in the nation, indicating a slowdown in consumer spending and the consolidation of the industry. Upward price pressure continues to appear in imported products, but the soft retail market is making it difficult to make price increases stick at the retail level. Inventories are reported to be in line with desired levels. Retailers note some problems attracting qualified sales people, and register concern about a possible increase in the minimum wage.

Automobile dealers report price increases of 4 to 5 percent on both domestic and imported 1989 cars. A substantial number of 1988 models remain in dealer inventories, and GM has extended its rebates to eliminate the surplus. One respondent reports fairly high sales of new cars and light trucks in the Southern California area.

Manufacturing

Manufacturing activity continues to exhibit strength, particularly in the Pacific Northwest. Pulp and paper production remains strong, although some slowing in growth is being noted and some inventories are rising. Several respondents report significant increases in farm equipment purchases, with some shortages evident. Moreover, construction equipment sales are reported strong in Utah. The slowing expansion of the wood products industry is being offset by continued expansion of aerospace, aluminum, shipping, and electronic

industries in the Northwest, with Boeing near capacity and delivery times lengthening. Some concern about semiconductor demand is being voiced in the San Francisco area, and Arizona respondents remain concerned about the effect of IBM's plant closure. Food processing and canning industries are expanding in the District.

Construction

Construction and real estate activity are highly variable in the District. Construction has been strong this past summer in Washington and Oregon, and housing prices have increased sharply in Southern California. The strength of the Washington economy is now boosting prices in that region as well. Some slowing of sales has been noted in the San Francisco area. In contrast, construction in Arizona is called the slowest in 15 years, and construction, other than for road building, remains depressed in Utah.

Resource Industries

Agriculture has had a strong year in the District. Yields in most areas are average or down mildly, but the higher prices have more than compensated. Inventories of table grapes are high, the tomato crop has been damaged by heat, and almonds have been bothered by insects, but prices have been strong. Livestock producers report strong prices, although feedlot producers are losing profits to higher feed costs. The wood products industry is still strong, although production of lumber and plywood has begun to fall. Excessive fire danger and environmental restrictions are limiting access to forests, decreasing the supply of logs. The shortage of logs has boosted prices in the Northwest. In the energy sector, the recent drop in oil prices has had little negative impact so far. Drillers are waiting to see if the lower price persists before changing plans, while refiners and retailers are enjoying the highest margins in years.

Financial Sector

Strong competition among banks for quality loans continues to be reported in the District, particularly in the Northwest and California. Conditions are improving in agricultural areas, with a drop in non-performing loans and improved asset quality. Loan growth is above expectations in Washington. Several respondents cited problems competing with below-market offers by Savings and Loan institutions.