

**SUMMARY OF COMMENTARY ON CURRENT ECONOMIC CONDITIONS
BY FEDERAL RESERVE DISTRICTS**

January 1990

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SUMMARY*

Economic activity is expanding slowly in most of the nation, with conditions somewhat stronger in the West than the East. Retail sales in the holiday season ranged from "disappointing" in Boston to modest in Philadelphia and Atlanta and relatively strong in Chicago, Minneapolis, and San Francisco; however, widespread discounting generally reduced store profits. Manufacturing activity is generally sluggish with production declines in some industries (autos, in particular) offsetting gains in others (such as commercial aircraft and oilfield equipment). Several Districts reported that the steel and computer industries, among others, may be "bottoming out."

Unseasonably cold weather dampened construction activity in some areas, but real estate markets generally held steady. Cold or dry weather also adversely affected citrus, vegetable, and winter wheat crops. Other agricultural and resource-related sectors did moderately well. The outlook is for slow growth in all regions in 1990; some respondents expect improvement late in the year.

Retail

Retail results for the Christmas season were mixed. Most Districts in the eastern third of the nation -- Philadelphia, Cleveland, Richmond, and Atlanta -- found sales up about 5 percent. New York

*Prepared at the Federal Reserve Bank of Boston and based on information obtained before January 13, 1990. This document summarizes comments received from business and other contacts outside the Federal Reserve and is not a commentary on the views of Federal Reserve officials.

respondents reported stronger sales and Boston somewhat weaker sales. Retailers in Districts farther west -- Chicago, St. Louis, Minneapolis, Kansas City, Dallas, and San Francisco -- had a better holiday season. Consumer durables, such as furniture and housewares, moved less briskly than apparel and other nondurables. Inventories of certain items were high in Boston, Cleveland, and Chicago, as Christmas sales ran below expectations and promotions failed to bring stocks into line. Auto sales were reported to be weak nationwide, although Chicago cited national data indicating that sales picked up at the turn of the year.

Most Districts reported widespread discounting. In some Districts, especially steep discounting by department stores adversely affected sales at discount and specialty stores.

Retailers expect flat sales or modest increases through the first six months of 1990. Results in the first weeks of January were said to be encouraging.

Manufacturing

Manufacturing activity was reported to be slow in most of the Districts. In Boston, Cleveland, Chicago, Dallas, and San Francisco, however, some industries were said to be showing signs of "bottoming out" and were posting slight gains in orders from year-ago levels. Food, apparel, lumber, commercial aircraft, and farm, oilfield, and some electric equipment all made gains. Defense, construction, and automotive products continued to face weak demand; however, respondents from Chicago and Cleveland suggested that current cutbacks in auto production may prove adequate to eliminate the industry's inventory overhang. Orders for first-quarter delivery also suggest a gradual improvement for steel.

Although a Minneapolis computer firm recently made a large layoff, Dallas and San Francisco reported signs of a pickup in that industry as well. Manufacturers in the Chicago, Dallas, and Boston Districts found that significant foreign sales are helping to offset weak domestic demand.

Manufacturing employment was reportedly flat to down compared with earlier in 1989, with firms in the New York, Chicago, St. Louis, Minneapolis, and San Francisco Districts facing major layoffs in autos, aerospace, or computers. Except for fuel, input prices were said to be steady or falling. Scattered evidence suggests that selling prices were also steady or falling, with discounting occurring in some industries.

Despite weakness in autos and parts of aerospace, New York and San Francisco reported major investment projects by firms in those industries. Boston, Cleveland, and Atlanta also indicated that several respondents plan capital spending above 1989 levels.

Most manufacturers expected slow growth in 1990, with a weak first half followed by gradual improvement. Despite widespread public concern about possible defense cutbacks, defense contractors in the Boston and St. Louis Districts expected declines in defense spending to be gradual, with limited local impact.

Agriculture and Natural Resources

December's severe cold weather adversely affected some agricultural sectors and led to large increases in fruit and vegetable prices. Richmond, St. Louis, Minneapolis, and Kansas City also noted possible or confirmed damage to winter wheat crops due to cold, dry weather.

Reports from other agricultural and resource-based sectors were

more positive. Minneapolis, Kansas City, Dallas, and San Francisco all mentioned high cattle prices and strength in the beef or dairy industries. Atlanta and St. Louis referred to sharp energy price increases, believed to be temporary and weather-related, while Atlanta, Kansas City, and San Francisco described greater oil and gas exploration or drilling activity. Mining and lumber industries were reported to be doing well in the Minneapolis and San Francisco Districts.

Banking

Regional financial conditions varied by District and by type of loan. Bankers in Atlanta, St. Louis, Kansas City, the Pacific Northwest and central California reported increased demand for business or consumer loans. By contrast, New York District banks saw a decline in demand for most types of credit. While Philadelphia lenders experienced an increase from year-earlier levels in total loans outstanding, they noted a recent decline in loan demand. Mortgage lending is down, according to New York, Atlanta and St. Louis institutions, while San Francisco mentioned that some Arizona and Alaska banks face real-estate related problems. Several Districts noted that banks have initiated credit reviews and were tightening criteria for making loans - especially for real estate purposes.

Real Estate

Most Districts discussing real estate reported steady or modestly improved conditions. Atlanta, Kansas City, and Philadelphia noted some signs of weakness, however. Expected declines in mortgage interest rates provided some reason for optimism in the real estate outlook.

Homebuilding activity was mixed. Richmond, Chicago, Minneapolis,

and San Francisco showed strength in at least some parts of their Districts, but New York, Atlanta, and Kansas City experienced slow or declining activity.

Reductions in home prices in Boston and the New York metropolitan area have boosted sales activity but have not eliminated the oversupply of homes available for resale in either region. Real estate prices were also said to be declining in St. Louis; by contrast, they were reported steady in Kansas City and up sharply in the state of Washington. Sales of expensive homes were said to be holding up well in parts of Miami, while lower-priced homes were the top performers in California and Boston.

Nonresidential property markets were generally slow. Office vacancies rose in Manhattan and Florida, and Atlanta reported slower pre-leasing of new projects in its downtown. Dallas, in contrast, found increases in office building occupancy.

FIRST DISTRICT-BOSTON

Reports on First District economic conditions were mixed in early January. Retail results were generally disappointing, but most manufacturers and realtors reported modest gains in sales. All types of contacts face intense price competition, with discounting becoming increasingly widespread. First District manufacturers indicate that international demand is stronger than domestic and that growing shares of their sales are made overseas. Most contacts expect the first half of 1990 to continue soft, with a pickup possible later in the year.

Retail

First District retailers report weak sales, slow traffic, and a heavily promotional atmosphere through the Christmas season. Discretionary items and building supplies sold especially poorly. Some firms that had expected stronger sales are now carrying excess inventories.

Most respondents report wholesale prices rising at the same rate as earlier in 1989 -- flat to up 7 percent, depending on the line of business. Prices at retail rose less than at wholesale, as large retail establishments reduced gross margins in response to stiff competitive pressures. Smaller establishments, which seem less subject to price competition, either maintained or increased their gross margins.

Retailers surveyed said that the cost of doing business continues to increase. Commercial rents are reportedly still rising, even though vacancies are up. Total labor compensation is growing at an annual rate of about 10 percent, with benefit costs rising much faster than wages. Faced with weak sales and rising costs, several firms report work force

reductions; all report increased labor availability.

A majority of retailers foresee weak sales through the first half of 1990, with possible improvement late in year. Most have no plans for expansion, and are using available funds to pay down debt.

Manufacturing

Conversations with First District manufacturers generally had a positive tone. A majority report modest growth in sales and orders - with gains ranging from slight to 10 percent above year-ago levels. International markets remain stronger than domestic, with contacts benefitting from a mini-boom in European capital spending and a few reporting gains in the Japanese market. Several respondents now obtain close to half of their sales revenue from overseas (through subsidiaries as well as exports). While some firms have seen a pickup in demand for automotive, commercial aerospace, and computer- and construction-related products, others see no such trend. Paper and defense products are said to be weakening.

All manufacturers are making concerted efforts to remain "lean." Most report that inventories are at satisfactory levels, although one-third describe them as undesirably high. Employment levels remain largely unchanged.

Most First District manufacturers report that materials prices are flat or falling. They cite plastic resin, steel, paper, DRAMs, and printing costs. Faced with intense worldwide competition, most manufacturers have passed some of these cost savings on to their customers. While two contacts have raised prices 5 percent, almost half mentioned discounting within their industry. Among firms discussing margins and profits, reports were mixed; however, two contacts expect a big improvement in profits this year.

The majority of First District manufacturers contacted this month expect to increase capital spending from 1989 levels. Budgeted increases range from 8 to 40 percent. Capital spending plans target replacement, consolidation, productivity improvements and, in a few cases, modest capacity expansion; however, little construction is planned.

A majority of First District contacts characterize their outlook as "guarded," although two expect 1990 to be an exceptionally strong year. Most anticipate U.S. GNP growth of less than 2 percent, with a weak first half followed by a modest pickup later in the year - "a soft landing and a soft take-off," as one respondent described it. Several expressed concern about the financial viability of their customers in the retail industry. Almost all contacts view the 1990s with optimism. Many firms feel well positioned in foreign markets where they expect rapid growth. Although concern has been expressed about defense cutbacks, the defense contractors contacted anticipate very gradual declines in real defense spending in the first half of the decade.

Real Estate

First District realtors expressed renewed optimism as the volume of home sales increased through the start of the new year. This improvement was attributed to lower asking prices and recent declines in mortgage interest rates. Properties continue to remain on the market longer than a year ago. The nascent pickup in residential real estate transactions has been driven largely by lower-priced (below \$150,000) single-family homes. Commercial property sales remain quite sluggish. All the realtors contacted expect sales to increase in future months, provided present market conditions prevail.

SECOND DISTRICT--NEW YORK

The Second District economy has continued to show little change from the mixed patterns described in other recent reports. Sales results at department stores were uneven in what retailers described as an unusually competitive environment, and homebuilding activity was seasonally slow. Unemployment rates in New York and New Jersey moved in opposite directions and office vacancy rates also varied. Most officers of small to medium-sized banks reported an over-the-year decline in demand for many types of bank credit.

Consumer Spending

Sales results at District department stores were mixed in recent weeks with some meeting or surpassing planned levels and others falling below. All respondents commented on the unusually competitive environment this holiday season which manifested itself in a high level of price-cutting throughout the period and resulted in below-targeted profit margins. Over-the-year sales gains during November ranged between 1.5 percent and 9.7 percent while the December range was from 3 to 12.2 percent. A survey conducted by the Retail Council of New York State covering some 100 stores across the state found sales during the five-week pre-Christmas period to be 7 to 10 percent above a year earlier.

In general, women's apparel remained the strongest selling item. However, with the arrival of unusually cold temperatures in November, retailers also experienced strong demand for outerwear, leather goods, sweaters and down comforters. Some contacts mentioned a pickup in sales of furniture and home furnishings following earlier softness. Due in large part to the heavy promotional activity in recent weeks, inventories are generally at desired levels with the major exception of the reportedly understocked Campeau-owned chains which some manufacturers are reluctant to supply.

Construction and Real Estate

Homebuilding activity is seasonally slow throughout the District but the underlying demand for new homes remains mixed. A glut of homes for resale continues to plague much of the New York metropolitan area whereas some upstate New York communities report that buyer interest in their areas is still strong. Home prices have declined somewhat in the New York metropolitan area, due largely to reductions by hardpressed sellers. Regarding the outlook, homebuilders in the downstate area are not optimistic, anticipating that, despite lower mortgage rates, "1990 will be another tough year".

While office leasing activity in Manhattan was reported brisk in recent weeks, substantial amounts of additional space were placed on the market by consolidating and restructuring firms. As a result, vacancy rates for primary space in both midtown and downtown Manhattan rose and some observers anticipate further increases as buildings now under construction are completed. Office vacancy rates remain high in some of the District's suburban areas but, for the most part, have stabilized or declined recently due to a slowdown in new construction.

Other Business Activity

District unemployment rates moved in opposite directions during December. New Jersey's rate fell to 3.6 percent from 5.1 percent in November while New York's rate rose to 5.6 percent from 5.1 percent. Rates in both states varied erratically and over an unusually wide range in 1989. More recently, as part of the nationwide cutback in auto production, several thousand workers have been on temporary layoff at District auto plants, and close to 1000 workers have been permanently laid off due to the closing of the Lockheed Electronics plant in Plainfield, New Jersey.

The percentage of Buffalo purchasing managers reporting improved new orders rose sharply in December but continued to be surpassed by firms reporting a decline. The number of firms reporting greater production increased slightly but was also surpassed by those with declining output.

Among recent developments in the District, Ford Motor Co. announced a \$200 million modernization plan for its Buffalo stamping plant and the Newark Housing Authority unveiled plans for a \$400 million riverfront project to be built in the downtown area with construction to begin this year. On a less positive note, tax revenues throughout the District are falling short of expectations and both New York City and New York State face sizable budget deficits in their current fiscal years.

Financial Developments

Most officers of small- to medium-sized banks in the Second District reported an over-the-year decline in demand for many types of bank credit, frequently citing sluggish local economies as the cause. Commercial and industrial loan demand declined at all but one reporting bank. Bankers indicated that caution in the business community and anticipation of interest rate declines may be forestalling demand. The single officer who noted an increase in strength said his community is home to large, non-cyclical firms which are currently expanding. Most respondents reported that consumer loan demand has also fallen off. A few officers ascribed the decline to consumer uncertainty about interest rates and the future of the economy. However, most believed that as a result of incentives created by tax reform, consumer borrowing has been largely redirected into home equity financing. While all other loan demand has declined, nearly half of the officers reported increased demand for home equity loans. Most respondents said that mortgage lending has also declined. Several bankers indicated that in recent years real estate prices have been somewhat overvalued and that potential buyers are waiting for the market to complete its natural correction. Two officers noted that mortgage demand in their communities is quite strong, crediting the growth to businesses relocating into their vicinities because other areas were too expensive. Despite the fact that overall loan demand has been soft recently, bankers foresee slow to moderate loan growth in the coming year.

THIRD DISTRICT - PHILADELPHIA

Economic conditions in the Third District were mixed as the new year began. Manufacturing continued on the slackening trend that began in mid-1989. Retailers achieved modest gains in unit sales for the Christmas season although price discounting was widespread. Overall loan volume at major banks was growing fairly steadily, but commercial and personal loan demand appeared to be easing somewhat and banks were implementing more conservative credit standards.

The outlook in most sectors of the region's economy is for very modest expansion. Among manufacturers, positive views for the first half of the year barely exceed negative expectations. Retailers generally see unit sales through the winter running little better than even with the year-ago pace. Bankers expect loan growth to continue in most credit categories, but at a slower rate as economic growth slows and more restrictive credit standards are applied.

MANUFACTURING

Manufacturing activity in the Third District in early January continues to fall. In nearly all of the industries surveyed, firms reporting slower business edged out those posting gains.

Some measures of business conditions indicated improvement, but the region's goods-producing sector remained soft overall. For example, area manufacturers indicated that new orders were rising slightly as the new year began, but the order rate was lagging behind shipments, leading to a drop in order backlogs. Local firms have been reporting shrinking order books since mid-1989. Lagging demand for manufactured goods is reflected by shorter delivery times as well, according to managers at area plants. The slackness in the manufacturing sector also appears to be bringing some stability to industrial prices; two-thirds of the firms surveyed said input prices were steady from

December into January, and three-fourths said they were holding prices constant for the goods they make. As area firms adjust production to the slow growth in orders, they are generally allowing inventories to decline; and, while most are holding employment steady, some are trimming payrolls.

Looking ahead, area manufacturers have mixed views, although slightly more firms expect improvement than anticipate further slowing in the first half of the year. On balance, managers at area plants expect marginal gains in new orders. They expect to step up shipments at least as much, however, which will prevent order backlogs from growing. Plant managers also anticipate some further trimming of employment and hours.

RETAIL

Third District retailers generally met sales goals for the Christmas shopping period, which was characterized by early and widespread discounting. Year-to-year sales gains for the season as a whole ranged up to 5 percent, in real terms, for area stores. Most department stores in the region indicated they achieved the modest sales improvement they had expected, but among discount and specialty stores results were mixed. In particular, sales at clothing stores in the last half of December did not appear to be consistent with the stronger performance in earlier fall months, after taking seasonal factors into account.

Merchants contacted in early January said sales were running about even with or slightly above the year-ago pace. For the rest of the winter, most retailers expect sales to just match last year's, in real terms. None of the store executives surveyed expressed strong optimism for the coming spring season. Several mentioned concern in the industry that major national retailers who are facing cash-flow difficulties might step up price discounting. After heavy discounting this Christmas, retailers are looking to reestablish stable pricing policies before the spring selling season begins.

FINANCE

Total loan volume at major Third District banks in late December was approximately 15 percent above the same period in the prior year, although growth appeared to ease during the month. Bankers contacted in early January said a slowdown in the rate of growth was continuing. Most expect overall loan demand to move up only modestly as the national economy enters at least one or two quarters of slower growth.

As the new year began, commercial and industrial lending was being scaled back at several large banks in the district as conditions in some sectors prompted credit reviews of companies in those industries. Builders and retailers, in particular, were being reviewed and some reductions in loan commitments were being made. Many bankers in the district expect the cutback in construction financing to result in lower total real-estate-based lending. However, some foresee a pickup in residential real estate financing, in response to recent and anticipated reductions in mortgage rates, which would mitigate the extent of the decline.

Consumer lending has been growing at a steady pace since last summer, but bankers generally expect growth to diminish, at least through the first half of the year. They cite the decline in auto sales as a negative influence on consumer borrowings, and several note that, while credit-card sales are growing steadily, paydowns are on a rising trend, leaving net outstandings nearly flat.

FOURTH DISTRICT - CLEVELAND

District respondents believe that the regional and national economies are still on a growth path, even if real GNP may have shown little or no change, or perhaps declined, last quarter. Retailers expect sluggish first-half sales. Some respondents believe that the worst of the cutbacks in industrial production are about over, although softening continues in some high-tech industries. Further declines in interest rates are generally expected by spring.

The Economy. The predominant view of the Fourth District panel is that the real GNP growth rate last quarter ranged between zero and a 1 percent annual rate. They do not, however, believe that last quarter marks the beginning of a recession, and most still expect that slow growth in output this half will be followed by a revival in growth to about a 2.5 percent rate in the second half. One panelist still expects a mild recession this half.

Consumer Spending. Last quarter's apparent weakness in spending was led by a cutback in consumer spending, especially for new cars. Major retailers report that sales during the holiday season rose about 5% to 6% from a year earlier, but that the season was as promotional as 1987. They expect relatively sluggish sales in the first half of 1990, with strengthening beginning in the summer. Inventories are close to plans, but still a little

high in view of uncertain sales prospects. A national retailer is planning to reduce inventories significantly through aggressive sales promotions and cutbacks in orders from suppliers over the next few months.

The tone of comments from auto dealers is guardedly optimistic. Sales of 1990 models are reported to be about "normal" to slightly below normal for this time of the model year, although foreign makes have been selling better than domestic cars. Some domestic dealers claim that price increases of Big Three cars average about 4% for 1990 models, partly because of added safety features mandated by law, but some foreign car dealers report no price increases for their cars. Incentives are again available on a full range of domestic cars, but some foreign car producers apparently are offering dealer incentives that they expect are sufficient to close sales. Domestic car dealers report they have been cautious in orders for 1990 models in an effort to hold down floor-plan costs.

Manufacturing. Some manufacturers believe that the worst is over for cutbacks in output, although the extent of an anticipated recovery is uncertain. Orders for heavy-duty trucks in the last three months have revived from last summer's low, but the recovery is still well below the peak levels of 1988.

Auto production may be slashed to an annual rate of 4.5 million to 5.0 million units in January, probably the low for the year, because of excess stocks and an uncertain sales outlook. Production is expected to climb to about a 6 million annual rate in February and March, if sales respond to broadened incentives.

Steel production, which had been at virtual capacity until last summer, has been cut to about 80% of capacity. A major producer reports that orders are beginning to pick up across-the-board for first-quarter delivery, and another expects that production will hold at about the level of last quarter through 1990. Lower steel consumption, led by weakness in auto output, rising imports, and inventory liquidation that will carry at least through the next few quarters, are expected to cause shipments to fall several percent from last year. Lower volume and further declines in steel prices will reduce profitability from last year. Capital spending, however, is expected to increase again because of the need for more efficient equipment. A smaller steel producer has cut back operations to about 70% of capacity because of reduced auto schedules and inventory correction.

Orders for small electric motors and equipment last month and for the fourth quarter were stronger than expected by some producers, and orders in January continue better-than-expected from a variety of markets. Weakness is centered in automotive and nonferrous industries. A larger increase in capital spending this year than last is being planned because of the need for additional capacity to accommodate the next peak.

Ball bearing orders have eased from the peak in 1989:IIIQ when the industry was confronted with long lead times, capacity shortages, and double orders. High inventories are now being liquidated, but the recent order level is still higher than a year earlier. Plans call for a larger increase in capital spending in 1990 than in 1989 for cost and quality improvement.

Some high-tech producers expect further cutbacks in orders and output this year from last. Communication equipment is expected to soften further this quarter before reviving next quarter. Softness in computer machinery, automotive and defense industries has slowed growth of semiconductor demand, although orders in December spurted.

Financial Developments. The recent reduction in the prime rate to 10% is expected to be followed by another one-half point reduction, possibly by spring, according to some bank economists. The latest reduction in interest rates, however, is not expected to stimulate much demand for loans, which have been sluggish for the past several months. Fixed-rate mortgages on 30-year loans are common at rates of about 9.5%, and realtors and lenders are cautiously optimistic over the near-term outlook for housing.

FIFTH DISTRICT-RICHMOND

Overview

District economic activity was mixed in December and early January after a sluggish November. Retail sales before and after Christmas were generally good. The slowdown in manufacturing, however, became more pronounced. Activity at District ports was again mixed. Housing activity rose in December despite the inclement weather, and business was strong at ski resorts. In agriculture, winter wheat suffered some weather-related stress.

Consumer Spending

Our telephone survey of retail associations indicated that merchandise sales during the Christmas season were above those of a year ago. Two of the District states and Washington, D.C., reported sales were up by five percent or more, while the remaining three states reported increases of less than five percent. The associations noted that markdowns on merchandise between Thanksgiving and Christmas were greater than last year. In the two weeks after Christmas, merchandise sales were generally strong, but sales of big ticket items apparently slowed in the Washington area.

Manufacturing

District manufacturers responding to our regular mail survey in early January reported that activity declined in recent weeks. Reports of declines in shipments, new orders, unfilled orders, employment, and the length of the workweek outnumbered reports of increases. Shipments apparently declined the most: 50 percent of the January respondents reported declines while only 9 percent reported increases. These percentages indicated broader weakness than was apparent in our November survey, when 30 percent reported declines in

shipments and 20 percent reported increases. New orders for exports were down slightly. Prices for raw materials rose somewhat faster than the moderate pace reported in November. Inventories of materials and finished goods were largely unchanged.

District manufacturers were more optimistic in January than in November about prospects for growth in their businesses, and they remained optimistic about growth in the nation during the next six months. Respondents who expect increases in shipments, new orders, employment, and the length of the workweek outnumbered those who expect decreases. Most producers continued to project slow-to-moderate economic growth over the next 18 months.

Ports

Mixed reports were received from the three major District ports--Hampton Roads (Norfolk), Charleston, and Baltimore. Imports and exports were higher in December at Hampton Roads, but lower at Charleston and Baltimore. Respondents from Charleston and Baltimore attributed the recent decline in shipments to the temporary closing of the Panama canal. In the next six months, export volume is expected to be higher at Charleston, lower at Baltimore, and about the same at Hampton Roads.

Tourism

A telephone survey of hotels, motels, and resorts throughout the District indicated tourist activity was, on balance, little changed from a year ago. The ski business was especially strong in West Virginia where some resorts reported that activity was up by as much as 25 percent over last year. Most respondents expect increases in tourist activity in their areas in the coming months, and none expect declines.

Residential Real Estate

According to our telephone survey, District housing activity improved in

December and early January. Despite unusually severe December weather, nearly half of the builders who were surveyed said that they had started as many or more houses in that month as in November. Of those who started fewer, two-thirds attributed the decline to normal seasonal factors and not to bad weather or a change in underlying economic conditions. Similarly, almost 50 percent of the surveyed realtors sold as many or more homes in December as in November, and most of those whose sales were off claimed the decline was seasonal. Also, most mortgage lenders who were surveyed reported only the usual seasonal decline in activity, while one-third indicated that the demand for mortgage loans remained constant or increased in December.

Agriculture

Inclement weather apparently impacted some crops while leaving others unharmed. Despite severe cold and heavy snows, the harvest of soybeans progressed at a normal pace in December and was almost complete by the first week of January. Weather-related damage to winter wheat was reported in some areas.

SIXTH DISTRICT - ATLANTA

Overview: Contacts in the Southeast indicate that economic activity continues to expand sluggishly. Reports of weakness for industries producing goods related to residential and commercial construction and autos were widespread. Makers of industrial machinery and construction equipment have reported scaled-down capital spending plans. At the same time, chemical, paper, apparel, and natural gas producers report some increase in capital spending, much of it going to upgrade equipment. Retailers noted modest gains in the dollar value of holiday sales over last year, although they indicated that price-discounting and heavy advertising had reduced profit margins. Commercial lending continues to slow; consumers are said to be more cautious in taking on new debt. Skilled workers are still in short supply in a few locations. Wage increases are reported as being in line with expectations while input prices were said to be soft with the exception of fuels.

Prices, Wages and Employment: Most employers continue to report that wage increases are about the same as earlier in 1989. Few labor shortages were noted, although there is scattered tightness in the supply of skilled workers. Contacts in transportation and utilities said that they are still having some trouble attracting mechanics and skilled craft workers. However, a Florida contractor pointed out that the slowdown in construction there had eased markets for unskilled and skilled workers. Manufacturers of tires and auto components have recently announced that they will be laying off workers because of falling auto production.

Prices of raw materials are said to be soft with the exception of fuel. A plastics producer says he expects the prices of bulk chemicals and resins to continue falling. Metal prices are reported to be stable or, in the case of aluminum, falling slowly. A builder reports that the prices of construction materials are generally softer than last year. Airlines, trucking firms and energy producers have noted sharply higher fuel

prices, although some felt that the increases were the result of the recent cold snap and therefore, temporary.

Retail Sales: Most retailers reported that nominal sales in December showed modest gains over last year. Widespread price-cutting across the District reportedly increased the volume of sales but also cut into profits. Sales of furniture and home appliances were reported weaker than a year ago, while sales of women's apparel were notably stronger. Most retailers said that inventories after the holidays were at planned levels.

Southeastern auto dealers continue to report that unit sales are down between 10 and 50 percent compared to last year. Several noted that the greater use of five year loans to finance cars in recent years has cut into current demand, especially for smaller models. They believe that lengthened maturity of these loans has not allowed car owners to build up enough equity to trade in for a new model. Other dealers pointed out that consumers have become accustomed to rebates and are much more price conscious than in the past.

Construction and Capital Spending: Reports on residential construction indicate the general weakness in this sector in the region continues. In parts of Miami, however, the demand for expensive homes is holding up as second and third time buyers cash in on past appreciation to purchase larger homes. Several contacts are now reporting increasing office vacancy rates in Florida. Warehouse construction shows some strength in Miami, although some contacts indicate this market may soon be overbuilt. Pre-leasing rates for a number of new projects that have recently gotten underway in downtown Atlanta are lower than was usual in the past.

Industrial construction along the Gulf coast continues to expand. Several large natural gas processing plants are reportedly planned for the Mobile area; and several others are expanding capacity. Several contacts noted an increase in the number of active drilling rigs in the Gulf, and they believe that the increase is permanent.

Some manufacturers of apparel, paper, and heating equipment report that they are installing computerized inventory control systems, which they expect to smooth production runs and control costs. New or expanded health care facilities have been announced in northern Florida and in Birmingham, Alabama. Several producers of heavy machinery and construction equipment report that they scaled back capital spending in 1989 and have planned no capital expansion for 1990.

Financial Services: Bankers noted an increase in business loans in December after several months of decline. They point out, however, that much of the lending has been to finance inventories and refinance older loans rather than to finance plant or capacity expansion.

Many lenders reported slower mortgage growth than at this time a year ago. Single family mortgage delinquencies are also increasing according to several bankers. In spite of lower mortgage rates, they do not expect much rebound in extensions in the next several months.

Commercial real estate loans were also down across the District. Contacts reported lenders' pre-lease requirements for new office projects have increased during the year.

SEVENTH DISTRICT--CHICAGO

Summary. Manufacturing activity in the Seventh District is showing signs of an auto-related slowdown, while other sectors of the District's economy continue to make slight improvements. Retailers report a high volume of sales in December, particularly in the final week. Auto sales improved nationally throughout December and into early January, as renewed promotional activity finally began to influence buyer decisions. Steel producers cited a stretching out of orders from the auto industry, but most other markets remain firm. Several reports from equipment producers cite a slowdown in shipments, with growth expected to remain positive. Although unseasonably cold weather slowed construction activity in December, backlogs remain relatively strong in the District. A consensus outlook of 24 business economists shows steady improvement in the economy this year, after a weak fourth quarter last year.

Consumer Spending. General merchandise sales in the District grew slightly faster than the national average during December, according to several reports. Sales among discount chains were hampered by heavy discounting at conventional department stores during the last few weeks of the Christmas shopping season. However, sales at discount chains rebounded sharply in the week after Christmas. Sales volume at one discount chain was reported to be better than expected, up slightly from 1988's growth pace. Sales growth was concentrated in urban areas of the District. Earlier concerns of excess inventories going into 1990 have been eased by strong sales last month, but inventories are high in some areas, notably apparel and household goods. Better-than-expected sales overall in early January, along with order reductions in problem areas, are expected to be sufficient to ease inventory problems early in the first quarter, according to one industry contact.

Motor Vehicles. Total auto sales nationally hit a 10 million unit annual rate in the last ten days of December, according to an industry economist, as sales promotions finally began to boost dealership traffic. Early reports for the first ten days of January suggest a continuation of sales at near a 10 million unit pace. If this sales pace continues through January, one industry economist expects that production cutbacks already announced should be sufficient to eliminate

the industry's inventory overhang. The effects of worker layoffs in January will have a sizable impact on District employment, with over half of an expected 115,000 layoffs concentrated in the District. In addition, a Michigan utility reports that during December electrical power consumption by industrial customers, led by auto producers, dropped sharply.

Steel. The steel industry shipped 20 million tons of steel in the fourth quarter of last year, according to an industry economist, pushing shipments for the year about 1 percent above 1988. However, shipments were sliding throughout the fourth quarter, reflecting primarily a slowing of shipments to the auto industry. Orders for the first quarter of this year indicate a reversal of this pattern, with shipments starting weak and gradually improving. According to one respondent, the auto industry has not cut orders, but has spread existing orders over January and February. Demand for steel from other markets, including machinery, construction, and steel service centers, is reported to be doing well.

Equipment. Producers of business equipment generally reported continued slowing in activity, with some segments showing signs of bottoming out last month. A producer of heavy equipment reports that sales of construction equipment continue to weaken and sales of mining equipment have started to slow, with the notable exception of coal mining equipment. Strength in exports is helping to offset a slowing in domestic demand for some types of heavy equipment. A producer of communications equipment reports that orders at the end of 1989 indicate a turnaround from the steadily slowing growth of shipments occurring in first quarter of 1990. Recovery to trend growth rates is expected to take most of this year, reaching trend growth by early 1991. A maker of electrical controls and supplies sold to other producers of industrial equipment, however, reports steady growth in sales to its industrial markets and expects demand for its products to continue to be strong in 1990.

Construction. Several reports indicate that on average construction activity in the District continues to be stronger than the nation. While demand for concrete in the Chicago area slumped in December due to unseasonably cold weather, backlogs were up substantially from year ago levels, according to one supplier. Gypsum board shipments to District states have been

rising at twice the national pace, although Michigan continues to lag other District states. A supplier to the residential construction market reports that contract awards in the year-to-date through November of last year increased 5 percent in the District states, compared to a 3 percent decline nationally.

Consensus Outlook. A group of 24 business economists from the Midwest met at the Bank in mid-December to discuss the economic outlook for 1990. After an expected flat fourth quarter in 1989, their median forecast shows real GNP rising 1.7 percent in 1990, on a year-over-year basis. Their industrial production forecast shows a 1.2 percent decline for the fourth quarter of 1989 and only 1.1 percent growth in 1990. However, both forecasted series show marked improvement over the course of the year, led by consumer spending. In line with the consensus outlook, the December survey of Chicago purchasing agents showed expanding activity. Finally, the median forecast for the GNP implicit price deflator indicated an easing in inflationary pressures, dropping from 4.2 percent in 1989 to 3.9 percent in 1990.

EIGHTH DISTRICT - ST. LOUIS

Summary

Slow economic growth continues. Total District job growth has been sluggish in recent months, with declining manufacturing employment offset by moderate gains in other sectors. District retailers report that holiday sales generally met or exceeded expectations. Record cold weather in late December drove up energy consumption and, in some areas, energy prices. Total loans at the District's largest banks grew more rapidly in the fourth quarter than in the same period a year earlier, while deposit growth slowed. Most analysts expect continued slow regional growth in 1990. Contacts do not expect potential changes in defense spending to have much local impact in the early 1990s.

Manufacturing

Layoffs and production cutbacks continue at the District's vehicle assembly plants and related firms, such as tire manufacturers. All four St. Louis area vehicle assembly plants were idle in late December and three of the four plants will be shut down a week or more in January. The auto sales slowdown will also result in flat sales in the first quarter for one major chemicals producer, who produces a plastic used in windshields and a chemical used in tires, among other products.

A large home appliance plant in Arkansas, which laid off most of its work force in November because of slow sales and production line changes, is scheduled to resume production in February. A company official anticipates unit appliance sales in 1990 will be flat or slightly lower than last year. A home appliance firm in Louisville expects strengthening

sales late in 1990 and plans to hire as many as 300 new production workers.

Construction and Real Estate

Several homebuilders in the St. Louis area anticipate steady growth in single-family homebuilding in 1990, especially in more expensive "move-up" homes; these builders suggest that relatively low interest rates will help sales. Other builders, however, anticipate continued weakening, since no backlog currently exists for new home construction and the median price of existing homes is declining. A real estate developer in northwest Arkansas expects continued strong residential construction growth in that area. A Little Rock developer anticipates some residential expansion this year, but notes that generally weak local economic conditions will limit growth.

Retail Spending

District retailers report that holiday sales generally met or exceeded expectations, with most retailers experiencing increases of 4 to 10 percent over last year. Because of the unseasonable cold snap, winter apparel sales were unusually strong, which retailers say could mean slower sales of these items in the first quarter. Toys, leather apparel and jewelry also sold well. Retailers report that the sales gains this year were achieved with about the same or less price-cutting than last year. Most are not concerned with inventories being too high and are expecting zero to moderate sales growth from the first quarter of 1989 to the first quarter of 1990. District auto dealers report that sales were down in December and first-quarter expectations are for sales to remain slow with imported models selling better than domestic.

Agriculture and Natural Resources

Low water levels and ice caused temporary suspensions of commodity movement in late December on both the Mississippi and Arkansas rivers. Warmer temperatures in early January allowed some barge movement to resume. Below-normal temperatures, in conjunction with dry soil conditions and no snow cover in parts of the District, may have damaged the winter wheat crop. The unusually cold weather also had a significant effect on District energy use and prices. Natural gas prices rose 20 percent or more between October and January in some parts of the District, while other areas experienced no price increases. In some rural areas propane prices have doubled since this summer. District gasoline and diesel fuel prices rose 6 cents to 12 cents per gallon during the last week of December. Despite record winter energy demand, electric utilities are not anticipating large price increases.

Banking

Total loans at the District's 11 largest banks grew at a more rapid pace in the fourth quarter than in the same period one year earlier. Consumer lending was up significantly at these banks from a year earlier, while real estate lending has slowed, both from its 1989 third-quarter rate and its 1988 fourth-quarter rate. Securities holdings rose sharply in the fourth quarter, with all of the increase coming from increased holdings of U.S. Treasury and agency issues. Total deposits increased in the fourth quarter at about the same rate as total loans, but that rate was down from the same period last year. Partially because of deposit outflows from thrifts, money market deposit accounts increased at almost three times the rate of a year earlier.

NINTH DISTRICT--MINNEAPOLIS

Ninth District economic conditions have been moderately good. The district employment situation has been mixed. Consumer spending on general merchandise has been strong, automobile sales have continued to show large month-to-month fluctuations, and automobile inventories have been at unusually high levels. Resource-related industries have been doing moderately well.

Employment

The district employment situation has been mixed. The unemployment rate in Minnesota in November was 3.5 percent, 0.2 percentage points lower than in October but 0.3 percentage points higher than in November 1988. In the rest of the district, unemployment rates rose from October to November and were at slightly higher levels than in November 1988. Employment levels continued to decline in the computer and electronics industries in the Minneapolis-St. Paul metropolitan area with one manufacturer of mainframe computers eliminating 2.5 percent of its metropolitan area workforce in December. The labor market situation has been brighter district-wide for entry-level workers, with employers continuing to report difficulty in filling entry-level jobs. Most employers contacted expressed concern about rapidly increasing costs for health insurance.

Consumer Spending

Consumer spending on general merchandise has continued to be strong. One retailer reports that, in the five weeks ending December 30, total sales were 15.1 percent higher than a year ago,

and 7.3 percent higher at stores that have been operating for at least a year. An appliance retailer reports that total sales in December were 21 percent higher than a year ago, and 5 percent higher at stores which were open in December 1988. The retailers contacted generally report that Christmas sales were much better than expected. Inventories were at acceptable levels.

Automobile sales have continued to show large month-to-month fluctuations. A domestic manufacturer reports that car sales in the region in December were 8 percent lower than a year ago, while truck sales were 13 percent higher. This manufacturer also reports that regional car sales for all of 1989 were 3 percent higher than in 1988. Inventories of cars and trucks have continued to be at unusually high levels, but it is anticipated that by March inventories will return to normal.

Housing activity has been largely unchanged from last year's levels. The number of new housing permits issued in Minnesota rose by 4 percent in November from last year, but the number of new housing permits issued in the Minneapolis-St. Paul metropolitan area fell by 11 percent over the same period. Housing sales in this metropolitan area in December were 7.4 percent higher than in December 1988, but sales for the entire year of 1989 were roughly unchanged from 1988 levels. Construction activity levels were also roughly unchanged from a year ago. The dollar value of contracts for future construction in November was about 5 percent higher than in November 1988.

Tourist spending has been moderately strong. Montana reports an outstanding year, with reservations at ski resorts up

anywhere from 10 to 20 percent over last year. The Upper Peninsula of Michigan also reports good snowfall and an excellent tourist season. Elsewhere in the district, snowfall has been below normal and ski resorts report a disappointing season. In Deadwood, South Dakota, gambling was recently legalized and the amounts wagered have exceeded all expectations.

Resource-Related Industries

Resource-related industries have been doing moderately well. Conditions in agriculture have been fairly good in the district except for parts of North Dakota, where a continuing drought caused declines in the output of wheat. However, the barley and sugar beet crops in North Dakota were reported to be good. A director reports that in some parts of North Dakota farmers' net worth declined by about 10 percent in 1989. Livestock dealers and ranchers throughout the district report to have had a good year. The lumber industry in the district has been doing well, although concerns have continued to be expressed about the long-term outlook of the industry due to environmental restrictions. The mining industry reports an exceptionally good year, particularly in Montana, where several expansion projects of copper mines are in progress.

TENTH DISTRICT - KANSAS CITY

Overview. The Tenth District economy continues to grow modestly. Christmas sales were near expected levels at most retailers, but continued sluggishness of auto sales has resulted in an unwanted buildup of dealer inventories. With most manufacturing plants operating below capacity, inputs are generally available with shorter lead times and at only slightly higher prices. Housing starts have declined and mortgage loan demand remains weak at district thrift institutions. Continued improvement in resource industries is a bright spot for the district. Oil and gas drilling activity is increasing, and agriculture's strong financial performance is encouraging expanded farm lending activity at commercial banks.

Retail Sales. District retailers report steady to higher sales over a year earlier, but sales have been mixed over the last three months. Demand is especially strong for women's apparel, while housewares and furniture sales are somewhat weak. Christmas sales nearly met expectations and exceeded year-ago levels for most retailers. Prices are expected to stabilize in the near future, and inventory levels appear satisfactory. Automobile dealers report sluggish sales of new vehicles during the last month. Dealers are trying to trim large inventories in anticipation of slower sales over the coming months.

Manufacturing. Purchasing agents report input prices unchanged from or slightly higher than a year ago. Prices have increased on only a few items over the last three months, and no price changes are expected over the next three months. Inputs are generally available with shorter lead times. Many firms are planning to trim inventories in the months ahead. Most plants are operating below full capacity, with few reports of skilled labor shortages.

Energy. Exploration and development for oil and gas in the district

continues to improve even though the recent increase in oil prices is not expected to persist. The average number of active drilling rigs in the district increased from 326 in November to 336 in December. Six consecutive months of increase have boosted drilling activity 25 percent above the level a year ago.

Housing Activity and Finance. District housing starts have decreased slightly from a year ago and from last month. Homebuilders expect starts and sales this year to be about the same as last year. New home sales and prices have generally been steady, while inventories of unsold homes are down slightly. Builders expect no problems obtaining materials. District savings and loan institutions report flat or negative net deposit flows over the last month. In almost all cases, net deposit flows were more favorable than a year ago. Most respondents expect no net change or a slight increase in deposits in the near term. District thrift institutions report weak mortgage demand and steady to slightly lower mortgage rates. Expectations for future mortgage rates are mixed.

Banking. Most district commercial banks report unchanged loan demand over the last month although some banks note a slight increase in demand. Increased demand is most apparent for commercial and industrial loans and consumer loans. Demand for other types of loans is generally unchanged. Among responding banks, loan-to-deposit ratios are about the same as a month ago but somewhat lower than a year ago. Deposit behavior varies considerably among responding banks, with slightly more banks reporting increases in deposits than reporting decreases. Demand deposits and NOW accounts show the greatest strength.

Agriculture. Bitterly cold December temperatures and continued dry

weather have heightened concerns over the condition of the winter wheat crop across much of the Tenth District. Dry growing conditions during the fall and early winter limited root development of the wheat crop in several states and left the crop vulnerable to damage by cold temperatures and wind erosion. In Wyoming, however, wheat fields are protected by a deep snow cover. Although much of the district's wheat crop is under stress, most of the crop should develop satisfactorily if normal weather conditions return.

Despite severely cold temperatures in late December, most district cattle feeders marketed cattle on a normal schedule. Faster weight gains during unseasonably warm temperatures early in December helped compensate for the slower weight gains caused by colder temperatures later in the month. High cattle prices have boosted feeding margins and encouraged some district producers to feed cattle to heavier weights than usual.

Strong returns from both livestock and crops allowed most district farmers to pay off 1989 operating loans at a rate similar to that of a year ago. In parts of Oklahoma and Kansas, however, continued drought and an early frost cut crop yields and boosted carry-over farm debt. Nevertheless, most district banks have little unwanted carry-over debt and are actively seeking new farm loan accounts to increase loan-deposit ratios. In general, agriculture's strong financial performance in recent years has encouraged district bankers to expand farm lending activity.

ELEVENTH DISTRICT--DALLAS

Respondents report that District economic growth has accelerated since the last Beige Book survey. Demand for manufactured products is increasing, after showing some softness in November. A number of firms report that retail sales growth in the District is faster than the national average. Auto sales are weak. Service industries continue to expand. Energy activity is picking up. A modest recovery is taking place in construction. Agriculture was hard hit by December's severely cold weather.

District manufacturing has resumed its expansion according to surveyed firms. Year-over-year growth in sales of oilfield equipment accelerated during the fourth quarter, and a significant portion of this upturn was attributed to increased exports. Primary metals producers say demand and prices weakened in November and again in December and that their product inventories are undesirably high. Although a number of fabricated metals manufacturers cite rising sales, those that sell to the construction industry note that December's extreme cold wave led to a greater-than-normal falloffs in the season's normally weak demand. Reports by lumber and wood products producers vary greatly, but most firms say their sales are increasing and firms serving the Houston market are particularly positive. Fourth quarter demand for paper and board was up over the third quarter but weaker than a year earlier. Several firms noted problems of overcapacity in the industry. Stone, clay, and glass producers generally cite little recent change in their demand, although manufacturers of auto glass say their sales are declining markedly. Manufacturers of electronics and computer-related

products report that demand recently has turned up, following a period of softness, and they are cautiously optimistic for the rest of 1990. District food products respondents note year-over-year growth in sales volume. Demand for apparel is expanding somewhat. Chemicals producers say their selling prices have stopped falling and demand has leveled off, but December's severe freeze caused widespread shutdowns along the Gulf Coast. Respondents in the chemical industry continue to voice fears about what continued expansions in capacity will do to product prices. Demand for petroleum products rose markedly as a result of December's cold weather but, after adjustment for this phenomenon, sales are little changed overall.

Retail sales showed strong growth during the holiday shopping season and a number of national chains said their sales grew more rapidly in the District than nationally. Sales expansion in the Dallas/Ft. Worth and Houston areas was said to be particularly strong, with slower upturns in San Antonio and Austin and still weaker growth in west Texas. Retailers expect sales growth to slow in 1990.

District auto dealers note that sales generally remain weak, despite the usual surge during the last week of the year. Profits are said to be poor, not only because of slow sales, but because of strong discounting, and a large number of dealers are currently operating at a loss. Respondents expect some increase in unit sales in 1990, but they are more cautious in their expectations about profits.

Most service-related firms in the District report continued expansion in sales and employment, with data-processing and accounting firms noting particularly strong growth. Airlines, however, reported some

softening. Generally, service industry respondents expect slower growth in 1990 than in 1989.

December's severe cold disrupted District construction operations, but contract values continue to edge up. Nonresidential building has provided most of the gains, but nonbuilding construction contract values also have begun to rise. Apartment occupancy rates have been climbing, reaching 90 percent in Houston and Dallas, and increased multifamily construction is widely expected for 1990. Office building occupancy also is increasing, but only slight office construction growth is expected this year.

The District oil and gas drilling industry continues to expand gradually. The unusually cold weather in December pushed the average price of West Texas Intermediate crude oil up 7.3 percent to 21.24 dollars per barrel and prices temporarily jumped to more than \$23 per barrel in early January. Prices have since subsided, but respondents believe that oil prices in 1990 will remain higher than in 1989. Drilling activity has been increasing, after seasonal adjustment. Profits are said to have risen, not only because of higher oil prices but because of reduced drilling costs.

December's hard freeze caused major disruption to District agriculture. In south Texas, about 50 percent of the citrus crop was destroyed. The freeze not only destroyed unharvested citrus fruits, but it also killed or damaged unharvested vegetable crops including broccoli, celery, lettuce, cabbage, onions, peppers, tomatoes, and sugar cane. The nursery industry has also reported damage. December crop prices were 3 percent above a year earlier, but further increases in prices have already occurred since then. Livestock prices in December were up 6 percent over a year earlier.

TWELFTH DISTRICT -- SAN FRANCISCO

Summary

Economic conditions continue to be healthy in the Twelfth Federal Reserve District. Business leaders continue to expect slow growth nationally, but their outlook has not worsened. Wage pressure is moderate in most areas of the District, although sharp increases are reported in parts of Washington. Retail sales were generally strong over the holidays, but heavy discounting held down profits. Manufacturing remains steady, with strong commercial aircraft orders offsetting weak electronics orders. Gains also are reported in machinery and food processing. Resource industries are healthy, with high prices boosting agricultural earnings and oil drilling. Forest products industries are re-tooling to process smaller logs, because of rapidly escalating log prices and anticipated additional shortages of old-growth timber. Construction and real estate activity remains strong in most parts of the District. Banks report generally good conditions, except for those in areas with serious real estate-related problems.

Business Sentiment

Western business leaders' expectations about the national economy showed little change in January compared to their previous responses. Three quarters of the respondents continue to expect GNP growth to be below its historical trend over the next four quarters. More respondents expected an improvement in housing starts, consumer spending, and the trade balance, but the general tenor of the responses indicate little fundamental change in outlook.

Wages and prices

Wage and price pressures remain moderate in the District. Materials and labor costs in construction are reported to be rising, but more slowly than the CPI. Most wage increases are in the four to five percent range. A notable exception is in Seattle, where managers and

technical workers are receiving 7 to 25 percent increases. Health care costs nationally are reported to be up about 10.5 percent from a year ago.

Consumer Spending

Holiday retail sales were generally healthy in the District. Most areas reported higher nominal sales than in 1988, but heavy discounting is expected to suppress profits. Sales were near expected levels in most parts of the District, although one respondent reported record sales in parts of Oregon. Heavy discounting was attributed in part to financial problems of some national chains with large debt burdens. Specialty stores performed especially well, according to respondents in the Northwest. Sharply higher spending by Asian tourists is keeping retail sales high in Hawaii.

Auto sales are reported to be down throughout the District. One respondent in Utah reports that dealers that normally sell 300 to 400 cars in December sold only 40 to 50 cars. Other areas report auto sales off 10 to 20 percent, with margins cut even further. A respondent in Oregon reports that auto dealers are cutting advertising budgets to reduce their costs.

Manufacturing

Manufacturing continues to show little growth in the West. One respondent reports that electronic component sales in Arizona are unchanged from a year earlier, although some gains are reported for small computer firms. Equipment orders are mixed. Backlogs are reported for farm equipment, and some expansion of capacity is reported. In contrast, construction equipment is readily available, with orders flat compared to a year earlier. Apparel production continues to rise in Southern California. Food processing also remains healthy, with strong gains in production and profits reported in Oregon. Electric utilities are not investing in

significant new capacity in the Northwest, which is raising concern at aluminum plants about potential shortages.

Some labor reductions in defense industries are reported, but the commercial aircraft sector remains very strong. In addition to increasing orders for commercial aircraft, a respondent in Southern California reports a major increase in contracts to rehabilitate existing aircraft. Investment remains strong in aerospace. Boeing has announced planned cutbacks of 2,000 workers at one plant and it has delayed plans to expand production until the middle of the year, but it is expected to continue expanding and remodeling suburban plants. The engineers union has rejected a contract offer, but talks are continuing.

Agriculture and Resource-Related Industries

Agriculture remains healthy in the West, although drought is becoming a major concern in some areas. Exports continue to increase, although a shortage of grain transport vehicles is creating a bottleneck in some areas. Fruit and vegetable prices are very high because of freeze damage in Florida and Texas. Drought continues to plague California and parts of Idaho and Utah. The dairy industry reports high prices and expanding production. Beef producers report strong prices because of rising consumption and slightly lower input costs.

Respondents report increased investment in oil exploration in California, and natural gas deliveries in Utah are up 3.7 percent. Gold mining remains strong in Nevada, despite lower prices. Lumber mills are facing diminished margins because of rapidly rising log prices. Respondents report that many mills are investing in new machinery to process smaller trees in expectation of reduced supplies of old-growth timber in the future.

Construction and Real Estate

Construction remains strong in the District, with the exception of Arizona. Construction

is very strong in Hawaii, with half of the spending in office and non-hotel building. Both residential and commercial construction are increasing in Utah and Southern California. One respondent reports increased construction in Sacramento, with old buildings being torn down and replaced by larger buildings. Prices continue to rise sharply in Washington, with appreciation of 2 percent per month reported in some areas. Some weakness in home sales priced above \$300,000 is reported in parts of California, but lower priced homes continue to appreciate.

Financial Sector

Conditions remain healthy for commercial banks in most parts of the District, although banks in Arizona and Alaska continue to have real estate-related problems. Credit flows are very strong in the Pacific Northwest, led by 20 percent gains in real estate lending, and central parts of California. One respondent in Southern California reports strong loan demand and tightening criteria for making loans.