

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

December 1990

TABLE OF CONTENTS

SUMMARY . . . . . i

First District - Boston . . . . . I-1

Second District - New York . . . . . II-1

Third District - Philadelphia . . . . . III-1

Fourth District - Cleveland . . . . . IV-1

Fifth District - Richmond . . . . . V-1

Sixth District - Atlanta . . . . . VI-1

Seventh District - Chicago . . . . . VII-1

Eighth District - St. Louis . . . . . VIII-1

Ninth District - Minneapolis . . . . . IX-1

Tenth District - Kansas City . . . . . X-1

Eleventh District - Dallas . . . . . XI-1

Twelfth District - San Francisco . . . . . XII-1

**SUMMARY\***

Business conditions are somewhat mixed in different parts of the country but on balance display a weaker pattern. In many of the Federal Reserve districts, economic activity appears to have declined recently while it has remained sluggish or grown slowly in the rest. Several districts report a decline in consumer and business confidence and many refer to expectations of continued diminution in economic activity. Retail sales, adjusted for inflation, appear to have declined below their year-ago levels in almost all districts. Manufacturing conditions have weakened in most districts. However, soft domestic demand has been partially offset by strong export orders. Most districts report continued weakness in construction. Several districts report a decline in business loan demand as well as some tightening of loan standards by banks. In contrast, agriculture is reported to have been doing very well. Crop yields have been good and livestock prices have been high.

**Consumer Spending**

Retail sales apparently have weakened in almost all the districts. The dollar volume of retail sales in October was lower than a year ago in most of the districts. At best, only slight increases are reported in the rest of the districts. Thus, real retail sales appear to have fallen from their year-ago levels. The Chicago, Atlanta, and St. Louis districts cite sharply lower consumer confidence as a key factor in the retail sales slowdown. Several

---

\*Prepared at the Federal Reserve Bank of Minneapolis and based on information collected before November 26, 1990. This document summarizes comments received from businesses and other contacts outside the Federal Reserve and is not a commentary on the views of Federal Reserve officials.

districts report that sales of durable goods were particularly hard hit. Automobile sales in particular are reported to have weakened, except in Dallas. Inventories are generally reported to have been at satisfactory levels.

Most districts report that retailers were pessimistic about sales prospects for the Christmas season as well as for 1991. However, the Richmond district reports unexpectedly strong sales in metropolitan areas immediately following Thanksgiving, and the Kansas City district reports that retailers expect sales to be steady to moderately improved throughout the Christmas season.

### Manufacturing

The Cleveland, Chicago, and St. Louis districts note particular weakness in the automobile industry. Weak domestic demand for manufactured goods was partially offset by strong export orders. An aircraft manufacturer reports that 90 percent of orders were from overseas compared to an average of 60 percent of orders during the previous two years. The Richmond and Atlanta districts also report strong export shipments. Manufacturing inventories have been described as under control.

Manufacturers have expressed concern about business prospects for the coming months. The majority of manufacturers contacted in the Boston district expect a national recession lasting two to four quarters. Business leaders contacted in the San Francisco district expect continued deterioration in the national economy. Manufacturers in the Philadelphia district, however, expect modest increases in orders and shipments over the next six months, and manufacturers in the Richmond district were less pessimistic about prospects than they had been a month ago.

### Construction and Real Estate

Most districts report continued sluggishness in construction activity. Residential construction continued to be weak, with several districts citing a glut of houses for resale. Atlanta, St. Louis, and Minneapolis report a decline in sales of existing homes. Nonresidential construction is also reported to be generally weak. New York and San Francisco point to an abundant supply of office and commercial space as big factors in the slowdown. However, there are a few bright spots. New York reports a recent pickup in office leasing activity in downtown Manhattan. Chicago reports that construction slowdowns are not universal and that development continues in communities outside major metropolitan areas in the district. Minneapolis reports a recent rebound in construction activity.

### Wages and Prices

None of the districts report significant wage pressures. Minneapolis reports that medical insurance costs have continued to rise sharply. Atlanta reports some easing of medical worker shortages. Dallas reports strong demand for service workers.

Reports of price increases for goods are mixed. San Francisco reports price increases in the 3 to 5 percent range, but Boston reports that materials prices for oil-based products have increased as much as 8 percent. Richmond reports steady finished good prices, even for products using oil-based inputs. Several districts report expectations of discounting by retailers this Christmas season in the face of weak demand.

**Finance and Credit**

Activity in the financial sector has been generally softer. Several districts report a decline in consumer and business loan demand. Almost all districts also report some tightening by banks of business loan terms, particularly for construction and land development. Reports of banks' willingness to lend are mixed, with New York reporting that banks are somewhat less willing to lend but with St. Louis reporting no change.

**Agriculture and Resource Related Industries**

The agricultural sector is reported to have been strong across the country. Crop yields are generally reported to have been fairly good. Partly as a result of these high yields, crop prices have fallen recently and reports are mixed on farmers' incomes. However, Minneapolis reports that farmers' balance sheets are in excellent shape. Several districts note that livestock producers have had an outstanding year.

Oil and gas extraction reports show little change in Dallas or San Francisco and a modest pickup in Kansas City and Minneapolis.

## FIRST DISTRICT-BOSTON

First District contacts in both retailing and manufacturing report that economic activity in the District was generally below year-earlier levels in October and November. For most retail contacts, sales are running from slightly above to modestly below 1989 figures, but sales of some durable or discretionary items have declined more than 10 percent. Sales of First District manufacturers remain mixed, but most report that orders are flat to down from year-ago levels. Fearing a national recession, most manufacturing respondents are keeping inventories lean, reducing employment and cutting capital spending plans. Retailers, too, have been cautious in preparing for the Christmas season.

**Retail**

For the most part, this month's panel of retailers reported sales results ranging from slight increases from last year's figures to single-digit declines. Sales of pharmaceutical products have increased more than most goods, however, while sales of home building supplies and some non-essential items have declined at double-digit rates. Results from northern New England tend to be stronger than those from the southern states in the region. Because of continuing regional economic weakness, increases in oil and gasoline prices, and anxiety about the Middle East, retailers are being cautious in adding stocks and employees for the Christmas season.

Most prices are reported to be fairly stable because weak retail demand requires a promotional stance. However, prices for some metal and plastic hardware products are up as much as 8 percent from last year.

Retail contacts are continuing to pursue cost-control measures. Some are reducing interest expenses by repaying loans. Sellers of durable goods seem especially focused on reducing inventory and employment costs.

The consensus projection for 1991 calls for fairly flat sales combined with continued pressures on earnings.

### Manufacturing

First District manufacturers contacted in mid-November report mixed sales results; however, a clear majority indicates that orders are flat to down compared with year-ago figures. Declines in orders range from 5 to 25 percent from 1989 levels. One-third of the respondents noted a sharp drop in demand 6 to 8 weeks ago. With the exception of Germany, demand from overseas has reportedly softened and is no longer stronger than domestic activity. In the United States, the auto and construction industries, retailing, and the government sector all represent relatively weak markets. Stronger sectors include commercial aircraft, telecommunications, electronics, and packaging. Inventory levels are widely described as satisfactory.

Employment is below year-ago levels at almost all manufacturers contacted. Declines range from slight to as much as 10 percent. Respondents plan no additional lay-offs at this time.

Materials prices are generally reported to be increasing--from gradually to as much as 8 percent for oil-based products. Contacts mentioned price increases for chemical feedstocks, steel, imported inputs, and "shop supplies," such as safety equipment. Most contacts are trying to

pass these input price increases on to their customers, but one-third are meeting resistance. Almost half have raised their selling prices by 3 to 5 percent on selected items.

Among firms discussing 1990 capital spending, most describe current expenditures as below-budget. Almost half the firms contacted plan to spend just enough to cover depreciation in 1991. A few firms expect to upgrade their equipment; only one is building a new facility.

First District manufacturers describe themselves as very cautious. The majority expect a national recession lasting two to four quarters. A few respondents report making contingency plans in case the downturn turns out to be longer or deeper than currently anticipated. Several contacts expressed concerns about the implications of current debt levels for the economy.

### Outlook

The New England Economic Project (NEEP), a nonprofit organization comprising businesses, government agencies and educational institutions, held its semi-annual outlook conference at the end of November. Based on a national forecast that now includes a recession, the NEEP forecast calls for nonagricultural employment in New England to continue declining through the end of next year. Jobs in the region are expected to grow at a very modest pace in 1992 and remain below 1990 levels even in 1993. Unemployment in New England is projected to exceed 7.5 percent in the second quarter of 1991. Incomes are expected to grow more slowly in the region than the nation through the end of 1993.

## SECOND DISTRICT--NEW YORK

Recent reports on District developments have been soft to mixed. Most retail contacts had disappointing sales results in October with year-to-year declines for the third consecutive month. Homebuilding activity remains sluggish and unemployment rates rose further to just below the national average. Although a majority of firms in the Buffalo and Rochester purchasing managers' surveys continue to report improvement or no change in business conditions, there has been a sizable increase in the percentage citing worsened conditions. On the positive side, a pickup in office leasing resulted in a decline in Manhattan's primary vacancy rates. Demand for consumer, business and home equity loans at small and medium-size banks fell over the last three months.

Consumer Spending

Most District retail contacts reported disappointing sales results in October though year-over-year declines were generally smaller than in September. One respondent stated that October sales were on target and represented a decided improvement compared with the preceding two months.

Over-the-year sales results in October ranged from -18% to no change from a year earlier. Big ticket items such as furniture, rugs and other home furnishings continued to be hard hit as they have for several months. Among items in strong demand were cosmetics, higher priced women's apparel and shoes, and men's shirts and ties. Inventories were generally described as on target which in some cases meant well below last year's level. Only one contact reported overstocked shelves.

Respondents tended to be rather pessimistic about the outlook for the upcoming holiday season based on consumer reluctance to spend in recent months. Expressing optimism about the longer term, Barneys New York

announced plans to open a huge specialty clothing store in midtown Manhattan in 1992.

#### Residential Construction and Real Estate

Homebuilding activity remained sluggish in the Second District during recent weeks. While a shortage of credit for acquisition and construction loans is part of the problem, a continuing glut of houses for resale is also a major deterrent to new construction. In addition, some developers have been downsizing projects already underway citing slow demand for new middle-income homes and condominiums which they attributed to growing consumer cautiousness about the economic outlook.

A pickup in office leasing activity in downtown Manhattan and moderate activity in midtown resulted in a decline in Manhattan's primary vacancy rates recently. Vacancy rates remain at relatively high levels, however, and the continuing addition of older space to the market due to consolidations and restructurings by various firms has caused vacancy rates in the secondary market to climb further. With the large overhang of vacant office space in the region, much controversy still exists concerning the wisdom of proceeding at this time with the construction of several new office towers as part of a Times Square redevelopment project.

#### Other Business Activity

Both the Buffalo and Rochester surveys of purchasing managers reported a sizable increase in the percentage of firms with worsened business conditions in October. However, a majority of firms in both surveys still reported either improved conditions or no change from September.

Unemployment rates rose further in the District during October and are now only slightly below the national average. New York's rate moved up to 5.6 percent from 5.5 percent in September while New Jersey's rate increased to 5.5 percent from 5.2 percent. Further dampening the District's labor markets were recent statements by the governors of both states that

substantial employment cutbacks may be necessary to close large budget gaps in the current and next fiscal years. New York City is also facing the possibility of sizable layoffs because of a substantial revenue shortfall. In addition, some financial services firms are still downsizing in Manhattan, and Blue Cross and Blue Shield of New Jersey plans to lay off 600 workers in the near future.

#### Financial Developments

Based on a survey of small and medium-size banks in the Second District, demand for consumer, business and home equity loans has fallen over the last three months. Business loan demand appears to have fallen the most, as nearly all respondents reported a decrease in that category. Although home-equity loan demand has slowed from three months earlier, it appears to have leveled off over in recent weeks. Delinquencies have risen for all three categories and bankers reported a general lengthening of repayment schedules. When asked to forecast the demand three months from now, a majority of bankers expected demand for each type of loan--consumer, business and home equity--to stay the same. Among the remaining bankers, there was roughly an equal number predicting increasing and decreasing demand for each type.

No banker reported that his institution was more willing to lend today than three months ago. Roughly equal numbers reported less and unchanged willingness to lend. The decreased willingness took various forms: some banks had increased interest rates on loans; others had raised their qualifying standards by increasing collateral requirements; a few had tightened some loan covenants. No banker reported a lowering of the maximum amount available for a loan, however, or higher fees on business loan commitments. Bankers reporting unchanged willingness to make loans generally had not altered their standards for at least two years.

## THIRD DISTRICT - PHILADELPHIA

Economic activity in the Third District continued to ease in November, according to indications from business contacts. Although more industrial firms reported improving business in November than in earlier months this fall, overall manufacturing activity remained on a downward trend. Retail sales in October and November, including Thanksgiving weekend, were below sales in the same months of last year for most stores, and auto sales were continuing to drop. Bankers indicated that lending has been flat in recent weeks, with modest growth in mortgage lending offset by slower business and consumer lending.

While there is some optimism among manufacturers, in general the outlook in the Third District business community is dim. Slightly more manufacturing executives expect business to pick up between now and next spring than anticipate continued slowing, but manufacturing employment generally is expected to continue falling. Retailers expect sales for the holiday period to be below last year's results and they are concerned that sales will remain soft in 1991. Auto dealers expect sales to continue dropping. Bankers predict continued softness in lending, due to weakening loan demand and further lending restraint prompted by the need to bolster capital.

MANUFACTURING

Industrial activity in the Third District continued to decline in November, but the severity of the downturn appeared to be diminishing a bit. Four out of ten manufacturers contacted for this report indicated that business was slipping, but this represented a slight improvement since early fall, when over half reported declining activity. Also, some firms indicated that business was improving in November, in contrast to early fall when there were virtually no manufacturers experiencing improvement. Nevertheless, the region's goods-

producing sector remained on the downward trend that began a year and a half ago.

Although there was a slight upturn in the number of firms that reported growth in shipments and orders in November, overall new orders, shipments, and order backlogs continued to shrink at area plants. Employment also remained weak, as Third District manufacturers continued to cut payrolls and working hours, on balance.

Looking ahead, the number of area manufacturers with optimistic forecasts slightly exceeds the number predicting further deterioration in business conditions. On balance, managers at area plants expect modest increases in orders and shipments over the next six months. However, with significant uncertainty still surrounding the outlook, they are planning further cutbacks in employment.

#### RETAIL

Third District retailers contacted in late November generally indicated that sales for October and November were below the level for the same period last year and continued to be sluggish over the Thanksgiving weekend. While a few upscale specialty stores were doing well, most stores of all types were experiencing weaker sales than they had anticipated. Retailers indicated that inventories were at appropriate levels; nevertheless, many expressed determination to move out all merchandise ordered for the Christmas shopping season by the end of the year.

Store executives' forecasts of final results for the holiday sales period reflect the recent slow sales pace. Most merchants expect Christmas sales this year to be below last year's, with forecasted declines ranging up to 10 percent, in dollar terms. Retailers also generally expect slow sales in 1991.

Third District auto dealers reported a continuing decline in unit sales, and they were paring orders to manufacturers and keeping inventories lean. Most expect the downtrend to continue regardless of the course of the overall economy,

and they do not expect more than slight temporary upticks in sales in response to current or future rebates or other marketing efforts.

#### FINANCE

Aggregate loan volume outstanding at major Third District banks in early November was approximately 9 percent above the year-ago level but flat compared to the prior month. Commercial and industrial loan volume was below the year-ago level, continuing on the downward trend that began during the summer; bankers surveyed in late November said the continued softening in commercial and industrial lending was partly due to easing demand and partly to continuing lending restraint by banks. Consumer lending in November was well above a year ago, but bankers said growth was slowing noticeably, and they attributed this to increasing caution among consumers in light of economic uncertainties and growing debt burdens. Real estate lending was still growing modestly, mostly due to residential mortgages; bankers described commercial real estate lending as "inactive."

The outlook among Third District bankers is for a continued pullback in lending to business, lasting into mid-1991 at least, and softness in consumer lending until economic growth picks up. They expect banks' participation in commercial real estate financing to be restrained for an indefinite period.

Several bankers expressed concern about the imposition of new minimum capital standards. Many banks expect to limit or reduce assets in anticipation of needing to meet a capital-to-assets ratio of greater than 3 percent; however, some said reducing assets through securitization is becoming less attractive. The large number of banks attempting to sell assets is resulting in lower prices and, consequently, less funds are being generated from downsizing than had been expected.

## FOURTH DISTRICT - CLEVELAND

Summary. Nearly all Fourth District respondents expect that real GNP will decline this quarter. A few anticipate, however, that growth will revive in 1991:1Q, and that the economy will avoid recession. Respondents generally believe that the District is not currently in a recession. Manufacturing has held up better here than nationally. Several retailers expect that real consumer spending will decline this quarter from last. Construction appears to be weakening more than seasonally. Funds for qualified borrowers are generally available, but District bankers have become cautious about industrial construction and consumer loans.

National Economy. U.S. economic prospects eroded further in recent weeks. All but one of a panel of 24 Fourth District Roundtable economists expect GNP to decline this quarter. Just a few weeks ago, 6 of the group expected slight growth. Still, a few expect that growth in real GNP will revive next quarter, and believe that the economy is not in a recession, even if real GNP declines this quarter. Most panelists still anticipate a temporary bulge in prices because of the oil price shock, and forecasts of inflation a year from now hover in a 4% zone.

Regional Economy. Most respondents believe that although conditions in this District have softened recently, the economy is not now in a recession. Manufacturing has been the region's strong sector, but construction activity has been weakening. Some District respondents point out that the recent flatness in employment, a rise in Ohio's unemployment rate in September and

October, and softness in retail sales all suggest an impending slowdown in the region.

Manufacturing. Fourth District respondents still believe that manufacturing here is holding up better than in the national economy, although some note signs of deterioration in both domestic and export markets.

A supplier of electronic parts reports that year-to-year increases in the firm's exports were shrinking even before the Kuwait invasion. A softening dollar has helped to sustain exports of steel mill products, but one producer notes deterioration in its overseas markets. A capital goods exporter believes that exports should be stronger this quarter than last, partly in response to the dollar's continued decline.

Some steel producers note a recent decline in orders that may prompt some layoffs next month, but another reports that its orders are holding up because customers are hedging against a possible work stoppage when a labor contract expires in January. Producers expect that output this quarter could fall 10% from last quarter.

Capital goods producers report weakened demand in some industries, but flat to rising demand in others. A welding machinery producer comments that domestic orders softened in the last few months, resulting in a cutback in overtime work. A computer industry supplier reports that orders declined recently. In contrast, a supplier to the heavy-duty truck industry is encouraged by a gradual revival in that industry from trough months earlier

this year. Auto production this quarter has been cut back to about a 6.2 million unit annual rate. The industry is tentatively planning on a production rate only slightly higher for 1991:IQ.

Consumer Spending. Retailers generally are not optimistic about sales prospects for this quarter. Most expect a decline in real consumer spending relative to last quarter. One retailer noted that spending for big-ticket goods, including home furnishings and appliances, has been weakening. He anticipates that December sales will increase about 5%, in nominal terms, from a year earlier. Another reports its October sales in this area were only 2.5% higher (in nominal dollars) than a year earlier. Still another retailer asserted that spending in this area remains better than spending in some other regions of the country.

All retailers emphasize that advertising and other costs will be cut, and that new hiring this holiday season will be less than usual. Still, one department store official indicates that consumer spending the day after Thanksgiving was better than they expected.

Construction. Residential and nonresidential construction is softening more than seasonally, according to some construction officials.

Builders of single-family homes still have access to borrowed funds, but builders of multi-family units are forced to search extensively for financing. Neither banks nor thrifts are reported to be interested in acquisition and development loans, except to highly qualified builders of single-family units.

One builder claims that although credit conditions have changed marginally since last spring, environmental regulations in some areas are now a bigger restraint on residential construction than credit availability.

Loans for commercial real estate are difficult to obtain, except for owner-occupied buildings. A construction official claims that industrial construction is being limited to environmental work and to maintenance and repair. No new speculative office building construction is underway, according to a developer.

Financial Developments. Loan activity continues to be "soft," according to District bankers. Some report continuing growth of loans outstanding, but at a slower pace in recent months. One bank comments that credit card and auto installment loans were rather strong in November, but mortgage loans have been soft. Another reports slower total loan growth in recent months because more loan applications are being rejected. Another bank is cutting back on loans to meet its year-end capital requirements. A few well-capitalized banks claim that ample credit is available for qualified borrowers, but demand is weak.

Several banks report that they are now more cautious about consumer loans, and indicate that more applicants are being turned down than a few months ago. Auto dealers note a marked tightening in bank financing for new cars.

A large mortgage lender reports that the value of its construction and development loans in 1990 will nearly match its 1989 level.

FIFTH DISTRICT-RICHMOND

Overview

Reports of business and financial conditions in the District suggested that economic activity declined in early November. Retail sales were weak through the first half of the month but showed strength after Thanksgiving. Manufacturing activity fell. Loan demand softened, and a more conservative approach characterized all bank lending. Funds for new commercial construction and speculative residential building were particularly tight. Exports continued to rise faster than imports, and agricultural conditions remained generally favorable.

Consumer Spending

Responses to a pre-Thanksgiving mail survey of retailers indicated that retail activity softened in early November from October. Some retailers blamed unseasonably warm weather for the slow sales, while others pointed to reduced consumer confidence and purchasing power. Overall declines were recorded in sales of big ticket items as well as in total sales, shopper traffic, and employment. Business at department stores was especially poor and not expected to improve.

Despite the weakness in sales, inventories also apparently declined over the survey period. There was some indication that suppliers were requiring earlier payment for delivered goods. Retail and wholesale prices were reported steady to higher.

Retailers reported unexpectedly strong sales in most major District metropolitan areas during the three days following Thanksgiving. Surveys by

the local newspapers in these areas indicated that shopper traffic was very heavy and that business was brisk. Lines of shoppers were reported at some stores that had advertized discounted merchandise.

### Manufacturing

Our regular mail survey suggested that District manufacturing activity declined slightly in early November. Respondents indicated that shipments, orders, and employment declined, but that inventories of raw materials and finished goods changed little. Most manufacturers felt that poor sales were their biggest problem, and manufacturers of furniture, textiles and apparel said their industries were definitely in recessions. Some manufacturers said that customers were increasingly reluctant to order very far ahead.

Raw materials prices rose, but most manufacturers apparently held finished product prices steady. Even firms that use petroleum-based inputs like chemicals and plastics said that they had absorbed sharp increases in their raw material costs and had not increased prices of their finished goods.

Manufacturers saw weakness in current economic conditions, but they were somewhat less pessimistic than a month ago about prospects for business next year. Most respondents believed that economic activity weakened in their local areas and in the nation in early November, and about half expected further weakening in the months ahead. A significantly larger number of respondents in November than in October, however, expected activity to pick up in coming months.

### Port Activity

Officials at District ports--Baltimore, Charleston, and Hampton Roads (Norfolk)--indicated that, seasonally adjusted, exports rose in October from

September and imports were generally unchanged. Compared with a year ago, export activity was higher and import activity was mixed. All port representatives expected exports would continue to increase faster than imports during the next six months.

The declining dollar evidently gave a modest boost to some exports. West Virginia's timber industry, for example, enjoyed strong export sales, and exports of coal to overseas markets apparently rose.

### Finance

A telephone survey of financial institutions and conversations with other business people suggested that total credit volume shrank in the first three weeks of November. Decreases in loan demand and in credit availability were cited as reasons for the decline.

The volume of outstanding commercial and industrial loans evidently declined in early November. Lenders reported that the demand for new commercial loans decreased and that borrowers were reluctant to use existing lines of credit. Bankers attributed the weaker demand to the sluggish economy and to the uncertainty resulting from Mideast tensions. Some lenders also indicated that they were taking extra care to ensure that potential borrowers were creditworthy. Nearly all lenders reported no change in their loan rates.

Bankers said they were analyzing loans for new ventures and business expansions more carefully. They indicated, however, that quality customers with sound management and sufficient documentation should find adequate credit available. Even so, some small businesses and real estate developers with strong past repayment records reported that they had not been able to find adequate funds. In some metropolitan areas, loans for real estate development

were reported to have dried up and construction activity was described as deeply depressed.

### Agriculture

After falling behind earlier this autumn, harvest and planting activity progressed at a rapid pace in recent weeks due to a lack of rainfall. As of mid-November, the harvests of corn, soybeans, peanuts, and apples were at normal to above-normal levels. The planting of small grains was on schedule, and above-normal temperatures accelerated the germination and emergence of these grains.

Most livestock producers received relatively high prices and benefitted from relatively low feed prices. High production, however, held down lamb prices.

## SIXTH DISTRICT - ATLANTA

Overview: Most business contacts report that activity weakened in October and November from earlier this year, with real sales revenues even with or lower than at this time last year. Manufacturers producing for domestic consumption indicate declining orders relative to this time last year, and are cutting production and shrinking employment as a consequence. On a more positive note, orders for defense-related goods and exports are said to be increasing, thus supporting production and limiting the overall employment drop. Businesses report only limited cost pass-through of oil-related price increases and an easing of previous labor shortages for selected occupations. Retailers generally report poor sales; they are increasingly pessimistic concerning the outlook for the holiday season. Our business contacts almost universally note an erosion of consumer confidence. Reports from bankers mirror those of our manufacturing and retail contacts, indicating weaker consumer spending and more cautious borrowing behavior in October and early November than in previous months. In the construction sector, contacts report that the level of overall activity declined in October as compared to earlier this year or to last October.

Manufacturing: The consumer spending slowdown is said to be rippling through the manufacturing sector with widespread reports of declining orders and employee layoffs. As orders fall, apparel producers say they are attempting to reduce inventory risk by placing orders for fabrics only after they receive firm orders from retailers. A producer of children's clothing, who claims his sales are usually recession-proof, reports November orders are off by one-fourth compared to last year. Likewise, producers of shirts and hosiery report falling orders and continuing layoffs. A heavy equipment manufacturer reportedly will close a plant in November and more temporary shutdowns at auto assembly plants were announced this month.

Positive developments within manufacturing are noted by producers of defense products in Georgia and Alabama. An executive at a major utility reported that energy use was up 5 percent on average in October from a year earlier in the metals, paper, chemicals, and auto parts industries. Except for metals, export markets for these products are reportedly strong.

Wage and Prices: Freight costs are being affected by higher oil prices, though transportation companies say the economic environment is limiting their attempts to fully pass-through fuel cost increases. The cost of producing petroleum-derivative commodities such as styrofoam packaging materials, chemicals, and fertilizers is also up and in varying degree is being passed on to customers. Utility company executives report that prices of domestically-produced alternative fuels such as coal and natural gas are remaining stable, limiting the impact of higher-priced oil. In labor markets, scattered reports indicate both an easing of the nurse shortage because the economic slowing is causing some local labor force reentry and growth in the pool of available skilled and professional workers. The recent call-up of reserves is reported to be having no significant impact yet on labor availability.

Retail Sales: Retailers and other business contacts generally used increasingly pessimistic terms to describe consumer spending. Most expect that real sales this holiday season will be down in Florida and Georgia, and only flat or up slightly elsewhere in the region relative to last year. Uncertainties about energy prices and the future of the economy are reported to continue their impact on consumer confidence and to limit buying of cars and other durable goods. In Florida, consumer confidence, as measured by a University of Florida survey, plummeted in October to the lowest level recorded in the survey's six year history. In Atlanta, a similar poll taken in mid-November by a private organization suggests holiday spending will be down this year compared to 1989. This poll also found that consumers are increasingly reluctant to make car or major appliance purchases as compared to sentiments expressed in

August. Merchants elsewhere in the region also point to eroding consumer confidence and falling discretionary income as factors limiting consumer spending.

Retailers are generally comfortable with inventory and employment levels that are about even with those at this time last year. Some merchants are taking advantage of contract opportunities to reduce orders, particularly for durable goods.

Financial Services: Reports from bankers and other lenders across the region mirror retailers' reports that consumer spending is slowing, with several contacts saying that consumer loan growth has weakened appreciably since summer. Lenders generally say they are even more concerned with deteriorating loan quality now than earlier this year. They indicate that weak economic growth, tighter regulatory scrutiny, and overbuilt real estate markets have caused them to apply credit standards more diligently to all types of lending.

Construction: Overall construction and absorption is reported to remain weak across the District. A contact in New Orleans says that real estate remains dormant there, and contacts in Atlanta say home sales are flat-to-down compared to last November. In Florida, a building materials producer reports that company sales in November were running 10-20 percent below expectations, and that a rebound is not expected in Florida until 1992. Florida and Georgia utility company executives note that monthly year-over-year rates of commercial and residential customer connections have been declining this year.

## SEVENTH DISTRICT--CHICAGO

Summary. Economic activity in the Seventh District slowed moderately in October and early November, although several contacts reported that some sectors were holding firm. Retailing sources indicated that personal consumption spending has begun to show the effects of a decline in consumer confidence, and it is difficult to detect previously available signs of relative strength in spending in the District. A slowdown in orders from auto dealers prompted Big Three automakers to reduce assembly plans for the fourth quarter, affecting a number of District production facilities. Overall manufacturing activity is mixed, however, with strength in shipments in several key sectors accompanied by some weakening in orders in other sectors. Large District banks generally continued to tighten lending standards, especially for commercial real estate development. While many projects continue to move ahead, a number of contacts expressed growing concern about future construction activity.

Consumer Spending. Consumer confidence fell more sharply from July to October than in any three month period in the last 44 years, including the 1973-74 oil embargo period, according to the University of Michigan's Index of Consumer Sentiment. Several contacts in the retail sector stated that this decline has begun to impact consumer spending. A national department store chain reported that the weakness in comparable-store sales that developed in October continued into early November. Results in several Midwestern markets were somewhat better than in the nation as a whole, although sales still declined (year-over-year) in October and early November. Store traffic has slowed, according to this contact, but the average expenditure per customer is holding up. A fast-growing specialty retail chain based in the District reported that sales growth in September and October dropped more sharply than in past experience. Sales in the company's big-ticket durable goods category fell sharply from a year ago. Recent weakness in durable goods sales was also reported by a large department store chain, with October appliance sales in the Chicago metropolitan area declining somewhat less than in the nation as a whole. A large national discount store chain reported that the month of October ended stronger than it began, with good momentum continuing into November. This contact had

reported declining year-over-year sales growth from June through September, a trend that reversed itself in October and early November. District sales growth lagged behind the company's national average, principally because of increased competition in the Midwestern market.

Auto Production. Auto production in the District faces a serious slowdown over the next several months. Slowing dealer orders have prompted Big Three automakers to reduce production schedules for the fourth quarter, and several auto industry analysts maintained that Big Three production cutbacks probably will be greater than those already announced. While income guarantees included in organized labor contracts may help cushion the impact on District consumer spending, one analyst noted that the employees of many regional suppliers to the industry do not enjoy such protection. Still, several automakers contended that current and expected conditions should not produce a slump in the auto sector comparable to those in previous recessionary periods. One industry spokesman argued that 1991 sales could be as high as in 1990 if the Middle East crisis is resolved soon.

Manufacturing. Overall manufacturing activity in the District is mixed. While other durable-goods sectors have weakened along with autos recently, machine tool orders in October were robust and steel production remained solid. A large District steel producer reported that October was a good month for the company's shipments. Order books for the industry are generally full for the fourth quarter. Steel orders for the first quarter of 1991 look normal, according to an industry economist, including orders from the auto industry. A major producer of capital goods in the District reported that nondefense machinery shipments in October grew slightly faster than for the year-to-date period. However, nondefense machinery orders declined in October, in contrast to relatively strong growth for the year-to-date period. The capital-goods market was characterized as showing "no widespread recessionary cratering," but concern was expressed about the near-term outlook. New weakness in orders is consistent with the results of October purchasing managers' surveys in Chicago and Indianapolis, both of which showed relatively sharp declines in the new orders component.

Slowing economies in Canada, Western Europe, and other foreign markets could affect a significant source of expected strength in the District's manufacturing sector. A large District producer of heavy equipment reported continued slowing in unit sales in October and early November in many of its important overseas markets, following the weakness that developed over the summer. Sales growth in Asia has continued at about the same pace recorded in the third quarter, however. A capital goods producer in the District reported solid increases in export sales (in current dollar amounts) in October, but noted continued weakness in some of its foreign subsidiaries' sales. Another large exporter in the District, which produces less cyclically sensitive goods, stated that unit sales volume overseas continued to expand in October and November.

Banking. The downturn in the U.S. commercial real estate market, the prospect of higher deposit insurance premiums, and bank regulatory concerns about capital adequacy have combined to tighten credit standards at large banks in the District. One bank economist stated that recent loan demand has been driven in part by greater customer concerns about the future supply of credit, which contributed to a recent surge in medium-term note issues. Several large District banks reported stricter standards on commercial and industrial loan applications by large borrowers, while a smaller number disclosed stricter standards for small and middle market firms. Approved lending generally (although not universally) bore higher spreads on loan rates over base rates, stricter covenants, decreased maximums for credit lines, and somewhat increased credit-line fees. District respondents generally reported tighter credit standards for construction and land development loans than for other types of loans. One large District lender stated that commercial mortgage loan foreclosures are "certain to exceed 1987 levels (the previous peak) in 1990."

Construction. While most construction projects that previously received financing continue to move ahead, commercial and multi-family residential construction have become generally acknowledged sources of weakness in the District economy. A large contractor in the District stated that occupancy and rental rates indicated that demand for new office building and

hotel construction would probably be "falling rather sharply." Construction of retail stores and industrial structures has been relatively strong, but this contact believed that conditions would likely deteriorate in these areas as well. A large manufacturer of construction equipment reported that sales in the District were holding up relatively well. However, equipment customers were expressing reservations about future District construction activity, if conditions in the Northeast and the West Coast spread to the Midwest. A producer of construction materials reported greater declines in shipments for October than for the year-to-date, and noted that industry shipments in the District have begun to show declines comparable to those in the nation as a whole. Still, this source stated that Midwest construction activity is "not quite so bad" as in much of the rest of the country. A District manufacturer of capital goods used in construction reported that, after four months of deterioration in contract awards, order rates were just beginning to fall off. Reports of construction slowdowns are not universal, however, and development continues in many communities outside of major metropolitan areas in the District.

## EIGHTH DISTRICT - ST. LOUIS

Summary

The level of Eighth District economic activity has declined in recent weeks. Retail sales, in real terms, are down. The manufacturing and construction sectors continue to weaken, although manufactured exports are increasing. Minor credit tightening has occurred at the District's largest banks. The agricultural sector shows continued strength.

Consumer Spending

Most retailers report that the nominal value of sales is near, or slightly below that of a year ago. Thus, real retail sales have declined. Sales of appliances, furniture and other big-ticket items are particularly weak. Relatively mild weather has slowed the sales of winter apparel, while uncertainty about national economic conditions and the Persian Gulf situation have made consumers both cautious and price-conscious. Retail inventories generally are at planned levels. Most contacts expect the nominal value of holiday sales to be near or slightly below that of 1989, though several respondents, including those representing discount stores in St. Louis and Memphis, expect substantial growth. Contacts report weakening vehicle sales, especially for cars that are domestically produced or are not fuel-efficient. Small trucks are reportedly selling fairly well. Vehicle inventories are generally at desired levels. The outlook is for continued weakness.

Manufacturing

Manufacturing activity continues to weaken, with both durables and nondurables sectors affected. Several auto assembly plants had

temporary layoffs in November and some of their suppliers, such as producers of tires and accessories, also report production cutbacks. While most textile and apparel producers in the District are experiencing flat or declining orders, three factories filling Operation Desert Shield-related orders for uniforms, hats and boots and one plant producing medical uniforms are substantially expanding their operations.

#### Construction and Real Estate

Both residential and nonresidential construction continue to weaken. Permits for single-family homes in St. Louis are down by one-third from their year-ago level, while multifamily permits are down almost 75 percent. Existing home sales have also weakened in St. Louis, Little Rock and Memphis. Realtors in these cities report that economic conditions and the Persian Gulf are the primary negative factors affecting the housing market. One Louisville realtor, however, reports that home sales are up substantially from their year-ago pace; this realtor expects a record dollar volume in 1990.

#### Banking and Credit

Loan officers report that some minor credit tightening has occurred recently at the District's five largest banks. For commercial and industrial (C&I) loans that banks were willing to approve, the costs of credit lines and the spreads of loan rates over base rates had increased somewhat, according to respondents, while the maximum size of credit lines and collateralization requirements were basically unchanged. Except for residential mortgage loans, real estate loan terms have tightened during the past three months. Credit standards for construction and land development loans and loans to finance commercial office buildings have tightened somewhat more than those for nonfarm nonresidential real estate loans. Respondents indicated that, apart from

normal seasonal changes, demand for residential mortgages had remained the same or weakened somewhat compared with the first half of the year. The banks' willingness to make consumer loans, however, had not changed.

#### Agriculture and Natural Resources

The harvest of the District's crops is nearing completion. When the harvest is over, District production of soybeans will be up slightly, while cotton and tobacco production will be up substantially over 1989. Corn production will be down. Dry soil conditions led to poor pasture conditions and a short supply of hay in parts of Mississippi. Returns to cow/calf operators remain relatively strong. Southern pine lumber mill activity is running ahead of last year. District states' recent coal production has been higher than a year ago.

#### Exports

District exports of manufactured goods have increased in recent months, while agricultural export growth appears mixed. Much of the export growth of manufactured goods is among producers of auto parts, chemicals, industrial machinery and printing and packaging machinery. Exports to Mexico are growing as import restrictions have eased. Government offices assisting exporting firms report a recent upswing in the demand for their services. Exports of rice are up slightly from a year ago, due in part to large sales to Mexico and Brazil, whose rice crops were damaged by severe droughts. Several contacts believed the lower exchange value of the dollar has helped boost exports in recent months, but were unsure how important this factor was. Corn, wheat and soybean exports are reported as lower than a year ago.

## NINTH DISTRICT—MINNEAPOLIS

Ninth district economic conditions have been showing signs of weakness recently. Labor market conditions have been mixed. Growth in spending on general merchandise has slowed down lately, automobile sales have been sluggish and housing activity has declined. Conditions in construction and manufacturing have been mixed. Resource-related industries have been doing very well. Wage and price increases have remained moderate.

Employment, Wages, and Prices

Labor market conditions have been mixed in the district. Minnesota's unemployment rate was 4.5 percent in September, up slightly from 4.3 percent in August and 4.2 percent in September 1989. Unemployment rates in Montana, South Dakota, and the Upper Peninsula of Michigan were slightly higher in September than their levels a year ago. Unemployment rates in western Wisconsin and North Dakota fell slightly over the same period. The number of people employed in the district was about 1.0 percent higher in September than in September 1989. In the Minneapolis-St. Paul area, computer and electronics firms have continued to reduce the size of their workforce but demand for hospital and medical workers is reported to have been strong.

Wage increases have remained moderate. However, employers throughout the district report that medical insurance costs have continued to rise sharply. Price increases, except for fuel costs, have been moderate. A construction contractor reports that costs are expected to increase 4 to 6 percent in the first half of 1991 but does not expect to be able to pass along cost increases fully to customers.

Consumer Spending

District retailers of general merchandise report a slowdown in sales growth lately. One major retailer reports that October sales in comparable stores were

2.4 percent higher than a year ago and sales in the first 10 months of the year were up 4.7 percent over last year. A discount chain store reports that October sales were 1 percent lower than a year ago and an appliance retailer reports no change in sales over the same period. Retailers in North Dakota, Montana, northern Minnesota, and Michigan's Upper Peninsula report strong sales to Canadian shoppers. Throughout the district, inventories are reported to be at acceptable levels.

New car and truck sales have been sluggish lately. Dealers report that truck sales in early November were about 7 percent lower than a year ago. Reports of new car sales range from a 2 percent increase to a 15 percent decrease over the same period. Automobile dealers report that they expect sales in the first quarter of 1991 to be about 1 percent lower than the first quarter of this year.

Housing starts have continued to decline in Minnesota. The number of new housing permits issued in that state was 8 percent lower this September than last. This decline was concentrated in the Minneapolis-St. Paul metropolitan area where the number of new housing permits declined by 12 percent over the same period. Sales of existing houses in this metropolitan area had been holding up well earlier in the year but fell by 34 percent this October from last October. Housing activity elsewhere in the district has been moderately good.

Tourist spending has been fairly strong, especially in areas near the Canadian border. Thus far this year, Canadians have reportedly made over 700,000 trips to North Dakota—a number which exceeds the population of that state. The number of tourists visiting Mount Rushmore in South Dakota was about 4 percent higher this year than last. The city of Deadwood, South Dakota, has grown explosively ever since legalized gambling was introduced about a year ago.

Construction and Manufacturing

Conditions in the district's construction industry have rebounded recently. In the Minneapolis-St. Paul metropolitan area, the dollar volume of contracts for future construction had been substantially below 1989 levels but rose sharply in September when it was 35 percent higher than in September 1989. However, it is expected that construction activity in this area will decline in the coming months. Elsewhere in the district, construction activity has been moderately good.

Conditions in the district's manufacturing industries have been mixed lately. The computer and electronics industries have continued to be in very poor shape and suppliers to housing construction report slow sales. However, aircraft industry suppliers and the medical instruments industry have been growing rapidly. Manufacturers generally report strong export demand, especially for capital goods.

Resource-Related Industries

The district's resource-related industries appear to be fairly healthy. Agriculture appears to be in good shape. Crop yields throughout the district have been excellent. There was very little rain in the district this fall which helped farmers dry their fall harvest. However, the lack of rain has also raised concerns about a possible drought next year. Good crop yields have been offset by a fall in prices of farm products so that farmers' incomes are not much changed from last year. However, farmers' balance sheets are reported to be fairly healthy and farmland values are reported to be rising fairly rapidly. Livestock ranchers report that this year has been the best in their experience. The mining industry has also been doing well. Oil exploration has been picking up recently, especially near proven fields.

## TENTH DISTRICT - KANSAS CITY

Overview. Continued strength in farm incomes and a modest improvement in the energy sector are helping to sustain slow growth in the Tenth District economy. High cattle and hog prices are the primary sources of strength in farm incomes, and higher oil prices are spurring exploration and development activity. Retail sales, including new auto sales, however, remain soft. Slow sales are leading both retailers and manufacturers to trim inventories. Despite slight declines in mortgage rates, new home sales and housing starts are weak. Loan demand at commercial banks decreased slightly last month, with much of the decline due to lower demand for residential construction loans and commercial real estate loans.

Retail Sales. District retailers report sales flat at best over the last year and over the last three months. One retailer noted that he would be thrilled if sales end up flat for the year. Sales strength is limited to a few categories of goods such as apparel and outdoor sporting goods. Sales of appliances and other big ticket items are generally weak. Most respondents are trimming high inventory levels and becoming more cautious about buying. One retailer remarked they were not ready for a recession because they were loaded with merchandise. While most respondents expect sales to be steady to moderately improved through the Christmas season, they also expect slower sales soon thereafter.

New auto sales are flat to down in most district states. Potential buyers in some areas are having difficulty getting loans as lenders become more selective. Most dealers are trimming inventories in the expectation of weak sales, while still trying to maintain stocks of the new models.

Manufacturing. Apart from petroleum products and fuel surcharges,

purchasing agents report only slightly higher input prices over the past three months. Prices are expected to increase modestly over the next three months. Agents report no difficulty in obtaining materials, and lead times continue to shorten. Most firms are trimming inventory levels due to lower than expected sales and continue to operate below full capacity.

Energy. Sharply higher oil prices have begun to spur exploration and development activity in the district. The average number of operating drilling rigs in district states increased from 305 in September to 325 in October, a level almost 7 percent higher than one year ago. Despite this improvement, uncertainty about the eventual outcome of the Middle East situation will moderate further gains in drilling activity.

Housing Activity and Finance. Housing starts are generally unchanged from last month, despite weak new home sales across the district. Expectations for sales are mixed, but starts are not expected to increase. Several builders report higher prices for wooden shingles and asphalt roofing. Availability of materials is not a problem, however.

Reports on deposit flows from savings and loan respondents are mixed, with results often dependent on locality and business strategy. Mortgage demand is down and is expected to worsen due to seasonal factors and a weakening economy. Mortgage rates have declined slightly over the last month and are expected to fall further in the months ahead.

Banking. Commercial bankers report total loan demand decreased slightly over the last month. Much of the decrease was due to a lower demand for residential construction loans and commercial real estate loans. Demands for commercial, consumer, and agricultural loans were steady, while home mortgage demand increased slightly over the last month. Bankers report credit

standards for loan approval unchanged to somewhat tighter, with tighter standards generally due to a less favorable economic outlook and pressures on banks' capital positions. Respondents report no change in their prime rate over the last month, but several bankers expect their prime rate to fall in the near future. Although a few respondents reduced consumer loan rates recently, most did not change their consumer rates in the last month. Total bank deposits were stable to slightly lower over the last month. Demand deposits, money market deposit accounts, and small time deposits were stable to slightly down. NOW accounts and large certificates of deposit were unchanged, while IRAs and Keogh accounts showed some increase.

Agriculture. The harvest of most district crops is nearly complete, except for Oklahoma's cotton harvest. Corn, soybean, and milo yields were normal to slightly above normal in most of the district. Sugar beet, potato, and onion yields in northern Colorado were disappointing. In southwestern Oklahoma, peanut yields were excellent, and a large cotton crop is expected.

The district's winter wheat crop is generally in excellent condition. After an excessively dry planting season in much of the district, plentiful moisture and warm weather have given the new crop a boost.

Crop income prospects for district farmers have weakened in recent months, but livestock income prospects remain bright. Crop prices slumped as the fall harvest season neared completion. Higher oil prices promise to boost crop production expenses and have encouraged farmers to purchase fuel, fertilizers, and other petrochemicals earlier than normal. Crop income subsidies have been cut back in the new government farm program, and participation in the program by district farmers may decline. High cattle and hog prices, however, continue to bolster incomes for district livestock producers.

## ELEVENTH DISTRICT--DALLAS

After adjustment for seasonal patterns, respondents indicate that output in the District has remained unchanged since the last survey. The manufacturing sector continues to decline while growth in the service sector has recently increased. Auto sales are expanding. Department store sales have increased mildly. Construction activity has declined slightly. Energy extraction has remained flat. State government revenues and expenditures continue to increase. In agriculture, prices and production have been increasing.

Manufacturing orders continue to be weak. Most respondents say that orders have not changed or have declined slightly. Respondents note continued uncertainty due to the Middle East crisis. Inventories are generally at desired levels. The weakest industries are those tied to the construction sector. Lumber producers note declining demand while orders for stone, clay and glass remain at very low levels. Orders for primary metals generally have continued strong. Fabricated metal producers cite flat sales, but respondents expect sales to decline in the coming months. Chemical orders have fallen in recent months after a surge that followed the Kuwait invasion. Chemical production has remained strong, however, because producers are replenishing depleted inventories. Petroleum refiners say that demand has generally been flat and that, while margins have improved slightly, they are well below pre-invasion levels. According to apparel manufacturers, orders have declined because retailers are cautious about the holiday season. Sales continue to be weak across a wide range of electronic products. Strong foreign demand has stimulated sales growth in oil field machinery. Sales of food and kindred

products have been growing moderately. Paper production has continued to show mild year-over-year gains.

Growth in the District **service** sector has increased during the past several months. Respondents note that increased economic uncertainty has boosted demand at temporary employment agencies, with demand particularly strong from the manufacturing sector. Computer-related business consulting has slowed somewhat while other types of business consulting have increased. Some respondents note that demand for accounting services has accelerated recently. Health services continue to grow at a moderate pace. Hotels and airlines note some recent declines in demand while respondents in the advertising sector say demand has improved modestly.

Growth in District **retail** sales has increased since the beginning of October, although real rates of growth are close to zero. Houston and West Texas are showing some improvement. Several retailers note that the District is outperforming the nation. Weak demand has held prices flat to down for many items. Some retailers say that they have shifted from foreign to domestic manufacturers due to the falling value of the dollar. Sales at discount stores continue to be stronger than sales at non-discount retailers.

Area auto sales rebounded in October after several months of weakness. On a year-over-year basis, sales increased 20 percent in Houston and 11 percent in Dallas/Ft. Worth. In the first 10 months of 1990, sales in Houston and Dallas/Ft. Worth were up about 4 percent from the same period in 1989.

District **oil and gas** extraction has shown little change. The price of West Texas Intermediate crude has increased 90 percent since Iraq's invasion of Kuwait last August. Nonetheless, natural gas prices have increased only seasonally and oil prices are expected to retreat once the crisis in the

Persian Gulf has been resolved--leaving oil and gas producers cautious about expansion. Consequently, neither drilling nor employment in the oil and gas industry have increased significantly. Although the Texas rig count increased slightly during October, the District rig count has been declining since July.

District construction activity has slipped slightly in recent months. Median home prices in Texas dropped sharply in September and October. One respondent noted that while median home prices have decreased, this is due to a relative increase in the amount of lower priced homes being sold. The respondent noted that the price for any given home has generally been rising. District residential construction has increased due to continued strength in the Texas apartment market. Nonresidential construction has increased slightly but remains below that of a year ago. District nonbuilding construction has continued to decline.

State government respondents say that nominal tax revenues in the District continue to grow slowly. Demand for social services has increased in all three District states and employment and spending has continued to grow at moderate rates.

The District harvest is nearly complete. Production has been good despite extreme weather conditions earlier in the year. District agricultural net cash income should be up slightly from last year, even though incomes have been reduced by higher than expected fuel costs. Although livestock and livestock products prices were down from September, they reached a record October high. Crop prices were 7 percent below a year ago but up 1 percent from September.

## TWELFTH DISTRICT -- SAN FRANCISCO

Summary

Economic growth in the West remains sluggish, and western business leaders' expectations about the national economy continue to deteriorate. Reports suggest that price increases may have moderated in recent weeks. Retail trade activity in the West is mixed, with wide variations by region. Activity in most manufacturing industries is reported to be flat to down from a year ago. Agriculture is one of the stronger sectors in the District, with strong prices and good yields. Lumber orders are down, while oil producers are enjoying the current high level of prices. Construction and real estate activity are down in most parts of the West, but several inland regions report continued strength. While conditions in Twelfth District financial institutions remain generally healthy, some California banks report further softening in major markets.

Business Sentiment

Western business leaders' expectations about the national economy continue to deteriorate. According to the most recent survey, 72 percent of respondents expect a recession during the next year, compared with 67 percent five weeks earlier and 4 percent at the end of July. The remainder of respondents anticipate that real GNP will grow at a pace slower than 2 1/2 to 3 percent. Weakness is anticipated in the home building, consumer spending, and business investment sectors, with more than 90 percent of respondents expecting softening in each of these sectors. In contrast, respondents are evenly split between those expecting the trade balance to improve and those expecting it to worsen.

Wages and Prices

Reports suggest that price increases may have moderated in recent weeks. While some petroleum-based products, including plastic products, have seen their prices rise during the past six weeks, users of other petroleum products, such as jet fuel, note recent declines since the sharp

run-ups immediately following the invasion of Kuwait. Reported price increases for labor and for most other products continue to cluster in the 3 to 5 percent range. However, auto dealers and department store retailers report that consumer resistance is holding their prices down. One retailer notes that wholesale prices for soft goods appear to be declining, and these reductions should eventually be passed on to the consumer. Another retailer expects prices to fall during the holiday season as stores resort to promotional pricing to attract shoppers.

#### Retail Trade and Services

According to current reports, retail trade activity in the West is mixed. Several respondents report weakness, including an auto dealer and a department store executive. Sales are stronger in the Pacific Northwest and inter-mountain areas than they are in other parts of the West. Moreover, a Sacramento respondent notes that some retailers in that area are experiencing stronger sales than they did a year ago, much to their surprise.

While one retailer reports a slight increase in inventories, another notes that inventories are in "surprisingly good shape" due to cautious ordering by retailers. No significant changes in the composition of retail orders, in terms of domestic versus imported products, were reported.

#### Manufacturing

Most respondents familiar with manufacturing industries report that activity is flat to down compared with a year ago. Inventories, however, are generally under control. One respondent reports that electronics industry orders are being placed with much shorter lead times as customers try to hold down inventory costs. While the number of commercial aircraft manufactured remains flat, orders continue to pour in and the order backlog continues to lengthen. This year, 90 percent of one aircraft manufacturer's orders were from overseas, compared to an average of 60 percent during the previous two years. A smaller aircraft manufacturer, however, reports that the overall number of orders at his company is about the

same as it was last year, and that there has been no appreciable change in the composition of domestic versus foreign orders.

#### Agriculture and Resource-Related Industries

Agriculture is one of the stronger sectors in the District, with strong prices and good yields for most products. Beef producers are enjoying high prices, and beef exports to the Pacific Rim have picked up again after slowing this summer. In California, farmers and ranchers are increasingly concerned about the possibility of a fifth drought year. This concern, along with worries about trade negotiations and the general economy, have led to increased caution among some farmers.

Lumber orders are down from a quarter ago and from a year ago. Many mills in the Northwest are cutting back production due to this lack of demand.

Oil producers are enjoying the current high level of prices. In Kern County, California, oil companies are spending money to enhance their wells, but long-term price uncertainty is keeping them from doing much exploration.

#### Construction and Real Estate

Construction activity is down in most parts of the West, particularly in the office and commercial sectors. The weakness is attributed to an abundant supply of space in most markets, coupled with resulting caution on the part of lenders. Reports suggest that construction activity in the Seattle area may be growing more slowly or declining, but a utility company continues to experience robust growth in its number of residential hookups. Some parts of the District continue to experience strong residential construction activity, including Bakersfield and Fresno in California's central valley, and parts of Idaho, Utah, and Oregon.

Real estate activity, as measured by the number of sales, property values, and rents, continues to weaken in most parts of the West. A southern California developer reports that new

leases on office space in some areas are priced 10 to 15 percent below their peak levels. This developer also reports that few commercial properties are being sold, but estimates that the values of the well-leased commercial properties that are changing hands have fallen by as much as 10 to 15 percent as well. At the same time, in California's central valley, the Pacific Northwest, and the inter-mountain states, residential property values continue to exceed their year-earlier levels. Even in markets that are generally lackluster, low-priced homes continue to sell relatively briskly.

### Financial Sector

While conditions in Twelfth District financial institutions remain generally healthy, some California banks report further softening in major markets. One California banker, for example, reports that business loan demand is flat and consumer loan demand has softened considerably during the past two to three months. At the same time, bankers in Oregon, Utah, Idaho, Hawaii, and central California report strong or improved loan demand.