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## SUMMARY\*

Most Federal Reserve Districts reported that economic activity continued to expand slowly to moderately in June and the first half of July. Flooding inflicted considerable damage in parts of the Chicago, St. Louis, Kansas City and Minneapolis Districts, but the effects of flooding were said to be highly concentrated and were not seen to threaten overall economic expansion in any District. Single-family home construction continued as a source of strength for many areas of the country. Retail sales grew across most Districts although the rate of increase varied widely. Auto sales rose in many areas of the country. Price pressures in the markets for materials and finished products were reported to be mixed.

### Manufacturing

Manufacturing output growth was described as generally sluggish in most Districts although conditions varied. Most Districts said that manufacturers have not increased employment and do not plan to for the remainder of the year. Several Districts noted weak sales to Europe, but strong exports to developing countries. The Cleveland District reported strong demand for steel and heavy truck components, but softening orders in several other industries. Respondents in the Chicago District cited a modest slowdown in industrial expansion, although auto and heavy truck production remained high. The Atlanta and Dallas Districts noted modest growth in overall output, but found strong growth among sectors tied

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to residential construction. Rates of expansion for manufacturing output in the Philadelphia and Richmond Districts were unchanged. Growth in Boston and Minneapolis was generally considered sluggish. The San Francisco District reported weakness in aerospace and defense-related industries, and strength in textiles and apparel and in computer-related industries located outside of Silicon Valley.

### Agriculture

Agricultural conditions were said to be generally favorable, although flooding and drought have destroyed crops in several Districts. Overall, agricultural conditions were seen as favorable in the Dallas and San Francisco Districts. Kansas City and St. Louis reported that, in areas not affected by wet weather and flooding, crops were mostly in good condition and farmers were benefitting from higher grain prices. Kansas City also noted that a large wheat crop was expected and many farmers anticipated strong earnings. In the Minneapolis District, above-normal precipitation has been a boon to cattle raisers, and pasture and range conditions in the Dakotas and Montana were said to be the best in many years.

Several Districts reported too much rain, too little rain, or both. Crop prospects are uncertain in many of these areas and will be determined by conditions between now and the frost. Atlanta, St. Louis and Richmond reported that hot dry weather has damaged crops in their Districts. High temperatures and drought have weakened rangeland and pastures in the Dallas District. Heavy rains and flooding ruined crops in portions of the Chicago, St. Louis, Minneapolis and Kansas City Districts. The Minneapolis and Kansas City Districts noted that corn and soybean crops were particularly hard hit by heavy rains and flooding. Minneapolis reported that unseasonably cool weather slowed crop development across the District. Chicago also reported that crops have been slow to develop.

The Richmond and San Francisco Districts said seafood production has declined.

### Retail Trade and Services

Retail sales were reported to have increased somewhat in most Districts, although Atlanta, Cleveland, New York, and Philadelphia reported that sales weakened slightly in July. Overall sales strengthened in the last month in Kansas City and Minneapolis, but both the Minneapolis and Chicago Districts noted slow sales in flooded areas. Apparel demand was reported to be higher in the Atlanta, Chicago, New York, and Philadelphia Districts and weak or sluggish in the Cleveland, Dallas and Kansas City Districts. Atlanta, Cleveland, Dallas and Kansas City all reported increased auto sales. Philadelphia reported that, while growth of auto sales slowed somewhat in July, sales were expected to be above last summer's rate. Retail and auto sales were said to be mixed in the San Francisco District.

In Atlanta, Richmond, San Francisco, and portions of the Minneapolis District, tourism was strong and the New York District reported minor gains in tourism.

### Real Estate and Construction

Residential construction and real estate activity remained strong in most Districts. Minneapolis reported that residential and commercial construction was perhaps the strongest component in the region's economy. Housing activity continued to increase in the Chicago District, but growth was thought to have slowed somewhat. San Francisco reported strong housing markets for most of the District, although southern California and western Washington were exceptions.

Commercial real estate activity remained sluggish or weak in most areas of the Atlanta, Dallas and Richmond Districts.

### Natural Resources

The Dallas, Kansas City and Atlanta Districts reported that higher natural gas prices have led to increased drilling, and a rise in activity for related service companies. Although

drilling is generally expected to continue its upturn, Dallas respondents said that lower oil prices have clouded the drilling outlook for the second half of the year. In the San Francisco District, recent Alaskan oil discoveries were said to have improved the prospects for economic activity.

Mineral mining activity was mixed. The San Francisco District noted weaker mining activity in Utah, Idaho and Alaska, while iron output increased slightly in Minneapolis. Timber and logging activity was also cited as weakening in the San Francisco District.

### Banking

Many Districts reported that business loan demand was unchanged, and that demand for mortgage refinancing was strong. According to respondents in the New York District, commercial and industrial loan demand continued to rise. Bankers in the Philadelphia District indicated that lending was generally unchanged although borrowing increased slightly among middle market companies. The Atlanta and St. Louis Districts noted recent strength in auto loans. The Cleveland District reported that business loans had softened and that consumer loans had leveled off, after a surge last spring. In the Kansas City District, consumer loans have increased, while business loans were flat to slightly up. Dallas said that overall loan demand had declined. Respondents in the San Francisco District said that banking conditions in California continued to improve.

### Prices

District reports suggested that price pressures were mixed. The San Francisco and Richmond Districts saw some increased prices for building materials and other raw materials. New York and Minneapolis Districts reported that lumber prices have declined. Manufacturing input prices were stable to slightly higher in Kansas City. Chicago mentioned higher prices for auto parts. Boston reported that auto parts suppliers are under much pressure to freeze or

reduce prices, and that they will try to offset higher material prices with productivity gains. Retail prices were reported to be very competitive in New York. Chicago, Cleveland, and Dallas mentioned that several retailers have lowered their prices. Kansas City District retailers said they were holding prices steady. The Richmond District reported that retail prices were rising. Atlanta and Minneapolis noted stable price levels.

Higher prices were reported for natural gas, but lower prices for oil. Several Districts reported higher agricultural prices, particularly in areas affected by flooding.

## FIRST DISTRICT - BOSTON

Economic activity in the First District continues to expand slowly, and inflation remains low. Retail contacts indicate that consumers are spending cautiously. Manufacturers report sluggish growth overall, but strength in automotive sales. The New England housing market has improved only modestly since last year.

Retail

Retail sales performance among First District contacts varies from flat to sizable increases over year-ago levels. Because consumers seem hesitant to spend, those retailers with sales gains believe their positive results come at the expense of their rivals.

Prices remain generally stable. Drought in the South and floods in the Midwest have not yet affected the cost of food or construction-related items. No increases in inventory stocks are planned, except for two contacts who are altering their mix of goods to offer higher-margin products.

Capital spending plans have increased, as several retailers seek to expand the number of locations in addition to renovating existing stores. Except for hiring to staff new locations, employment levels are unchanged. Wage increases, when they occur, are modest. Because recent sales gains have been unsteady, retailers generally are reluctant to express optimism about future trends.

Manufacturing

Most manufacturing contacts report that their recent sales increased between zero and 3 percent from year-earlier levels. Some companies are benefiting from strong demand from the automotive and

biotechnology industries. Sales of a variety of consumer products are growing, but slowly. Demand for aircraft parts and general industrial machinery remains sluggish.

Manufacturers report that the U.S. and U.K. economies are in a slow growth mode, but that other European markets are still in recession and the recent fiscal stimulus in Japan is having only limited effects. Some contacts report strongly rising demand from developing countries in Asia or Latin America.

First District manufacturers have experienced little inflation. Small cost increases are reported for some specialty chemicals and metal products, but plastics prices have fallen. One contact anticipates a 3 percent increase in the cost of paper. Consumer goods manufacturers have increased selling prices by up to a few percentage points, but industrial goods manufacturers have not raised prices at all. Auto companies in particular are pressuring their suppliers in the First District to freeze or reduce prices, often requiring them to offset higher materials costs by productivity gains. Computer prices continue to trend downward.

Most manufacturing contacts report that employment is flat or down several percentage points from a year earlier. However, two relatively small companies have increased their head count by double-digit rates. Manufacturers generally expect a continuation of recent economic trends; therefore, they indicate that employment will remain approximately steady in coming months. Some companies will continue to allow employment levels to drift downward. Others anticipate meeting bulges in demand through temporary help and greater overtime. Employers

with prospects for steady growth are considering only selective hiring. A majority of manufacturing contacts indicate that they intend to invest in labor-saving machinery and equipment.

#### Residential Real Estate

The market for residential real estate in the First District changed little during the last quarter. Contacts point to slight year-to-date sales increases in Maine and New Hampshire as a positive sign, given the strong increases in sales from 1991 to 1992. The real estate recovery in Connecticut and Rhode Island continues to lag behind the rest of the region, although prices are no longer reported to be falling. Despite data showing decreased sales in April and May, increased transactions in the higher-priced trade-up market suggest that the housing market in Massachusetts may be stronger than in the rest of the region. All contacts point to low interest rates and prices as having brought additional buyers into the housing market; many expressed concern about the effects of a rise in interest rates, should one occur.

#### Nonbank Financial Services

Insurance companies report strong sales of annuities, mutual funds, and life insurance in the second quarter. Several respondents are experiencing a slowdown in health insurance sales, which they attribute to customers' uncertainty over the shape of the coming health care reform. For some contacts, low credit ratings hamper pension sales. Approximately half of the respondents have kept their employment steady, while the rest reduced employment in the second quarter.

## SECOND DISTRICT -- NEW YORK

Most sectors of the economy of the Second District made headway during June but there are a few preliminary indications of some retrenchment in July. June retail sales were reported "good" to "very good" with gains averaging 4 to 13 percent above year ago levels. Home builders reported generally fair-to-good housing starts although there was considerable variation within the region. Office leasing activity gained in most areas throughout the district and vacancy rates inched lower. The unemployment rate in New Jersey fell to 6.9 percent in June, from 7.4 percent in May, while in New York the unemployment rate rose from 7.5 percent to 7.8 percent. Early reports of economic activity in July, however, suggest some softening of the economy with a retreat in retail sales and housing.

### Consumer Spending

Retailers were generally upbeat, reporting good-to-strong gains in all merchandise categories during June. For many merchants, calendar shifts pushed extra spending into June because the timing of Memorial Day and July 4th meant that sales on those days would be counted in the June figures. Sales gains generally ranged from 3.8 percent to double digit growth. Demand was strong across all categories including apparel, electronic goods, fashion and furniture. Inventories were largely in good shape, the result of close control throughout the year. Several retailers mentioned that there is no pricing power, however. In contrast, early July sales were characterized as very disappointing or poor. Because of the erratic trend in the month-to-month retail figures and the sharp retrenchment in July sales, retailers have lowered their expectations and now expect generally modest gains in the coming months, below the rates of increase in the first half of the year.

### Residential Construction and Real Estate

Residential construction activity was mixed with the market tone improving with the distance from the New York City metropolitan area. Most builders report that banks will lend construction money only if the builder has a signed sales contract in hand. There is no lending for construction on speculation. Thus current building activity represents the strength in April-May sales. Since then, floor traffic has faded in many areas and fewer contracts were signed in the June-July period, suggesting some slowdown will develop in August-September construction. Even as lumber prices continued to move lower, some builders reported a cost-efficient trend of substituting steel for lumber in certain applications.

Higher loan-to-value ratios with downpayments as low as 10-15 percent were a boost to New Jersey home sales but credit remained a difficult issue for many builders. The scarcity of acquisition and development loans is driving many builders out of the market; those who can borrow cite private lenders and pension funds as their sources, not banks. In addition, restructured projects from the Resolution Trust Corporation are viewed as a potential threat by many builders who feel that they cannot compete financially, and the potentially larger supply of RTC projects is viewed as particularly worrisome.

Commercial vacancy rates drifted lower in most areas throughout the region including Fairfield County, Northern New Jersey and Westchester, but the trends in Manhattan were mixed. Because employment growth remains negligible in most areas, the absorption rate for office space is slow. In addition, declining vacancy rates for primary space were also frequently associated with rising vacancy rates for secondary space.

### Other Business Activity

Signs of strength were evident in state tax collections. Following two months of declines, personal income tax collections, a proxy for personal income, rose 3.8 percent in June from a

year earlier in New York State, while tax collections for retail sales posted a 4 percent gain for the April-June quarter. Tourism sustained minor gains, despite the bombing of the World Trade Center and the subsequent revelation of additional terrorist plots -- no significant cancellations of tours or conventions were reported. Base closings in or near the Second District over the next five years are estimated to cost the region a net 7400 military and civilian jobs, representing less than 0.1 percent of the combined job base in New York and New Jersey. The monthly reading of the unemployment rate remained erratic with New York rising to 7.8 percent in June, while New Jersey declined to 6.9 percent. However, the overall trend remains definitively down; the unemployment rate a year ago for both states was close to 9 percent. A major regional retailer, Jamesway Corporation, filed for protection under Chapter 11 of the U.S. Bankruptcy Code and retail analysts expect several stores to be closed in the coming months. Merck & Co., a New Jersey based pharmaceutical manufacturer, announced plans to eliminate 2100 jobs through an early retirement program. The reduction will be diffused throughout their worldwide operations which employ approximately 38,000 people.

#### Financial Developments

Almost all senior loan officers surveyed at small and midsized banks in the Second District indicated that their willingness to lend was unchanged relative to two months ago. The few bankers who cited an increased willingness to make loans attributed it to a sharp increase in demand deposits. However, this increase in deposits was not widespread, as a majority of officers instead noted a decline or a lack of growth in certificates of deposit and money market accounts. Passbook savings accounts grew slightly. Overall demand for loans stabilized, although demand for commercial and industrial loans continued to improve. Interest rates on loans were steady or lower. Delinquency rates for all types of loans were unchanged or improved slightly during the preceding two months.

## THIRD DISTRICT - PHILADELPHIA

Economic activity in the Third District appeared to be steady in July, based on reports from business contacts. Manufacturers indicated that shipments were running at a level pace but new orders were falling. Retailers generally reported steady or improving sales although the gains appeared to be easing. Most bankers said loan demand remained flat while a few reported increased lending to middle market companies.

On balance, company officials surveyed for this report expect only slight gains during the rest of this year. Manufacturers anticipate an increase in new orders but they expect employment and capital spending to trend down through the rest of the year. Most merchants forecast only slight improvement in the fall. Bankers generally expect sluggish loan demand to persist due to the reluctance of both businesses and individuals to take on more debt while economic conditions are uncertain and increased taxes are in prospect.

MANUFACTURING

Third District manufacturers polled in July indicated that activity remained generally flat, with some signs of softening demand for their products. While shipments were running at a steady pace, on balance, firms reporting declines in new and unfilled orders slightly outnumbered those posting gains. These conditions prevailed in most major manufacturing sectors of the region; only food processors, chemical manufacturers, and makers of stone, clay, and glass products noted some increases in orders. Employment remained weak;

although more than two-thirds of the firms contacted for this report said they were holding payrolls and hours steady, the number of companies making cuts exceeded the number adding workers or extending hours.

Despite lackluster current conditions, area manufacturers expect improvement over the next six months. Nearly half anticipate increases in new orders and shipments while only a relatively small percentage expect declines. There appears to be ample capacity for the expected increase in demand as surveyed firms forecast continuing reductions in employment and scaled back capital spending.

#### RETAIL

Third District retailers gave mixed reports for the mid-June to mid-July period; most said they were even with the year-ago pace or achieved some increases. Discount stores and apparel and appliance specialty stores posted gains while sales for department stores were mostly flat. Merchants said the excessively hot weather of late June and early July stimulated sales of air conditioners and summer clothing, but they noted that audio equipment also sold well. Most of the merchants who were making year-to-year gains said the upward trend appeared to be easing in late July.

The majority of store officials surveyed for this report expect sales to be seasonally slow until back-to-school shopping begins in late August. Retail executives are retaining their earlier forecasts of a small improvement in sales for this fall compared to last, and they continue to cite low consumer confidence as the factor inhibiting stronger gains.

Auto dealers generally said sales slipped somewhat in July from the strong pace set in the spring. Nevertheless, most expect sales to continue to run above

last summer's rate, and they expect sales for all of 1993 to meet or exceed the forecasts they made at the beginning of the year.

FINANCE

Third District bankers generally indicated that loan demand has been stagnant in most credit categories although some said they have seen increased business borrowing in response to extensive business development efforts. Most of the new borrowing has been by middle market companies. Bankers said their new customers are borrowing to finance needed capital equipment. Consumer lending has been virtually flat in recent weeks, according to bank lending officers interviewed in late July.

Bankers expect loan demand to remain soft. Most of those contacted for this report said both businesses and individuals appear reluctant to add to outstanding debt while the economic outlook is so uncertain and changes in federal taxation are under consideration.

### **Fourth District - Cleveland**

Summary. District business activity continues to expand at a moderate pace. A brisk sales pace in durable goods has more than offset sluggish sales in apparel and various seasonal items. Low financing rates and consumers' desire to replace aging automobiles have combined to prompt a recent surge in auto sales, and the seasonal pickup in house sales has boosted the demand for home furnishings, appliances, and consumer electronics. Several industrial sectors continue to report strength in orders, backlogs, and production. Manufacturers of steel and heavy truck components indicate near-capacity operations. Producers of industrial controls and machine tools have also experienced strong demand in recent months, but several respondents anticipate a slackening in orders for the balance of the year. Loan officers note a softening in business loans and a leveling off in consumer loan volume in recent weeks.

Consumer Spending. Fourth District retailers report a continued increase in overall sales through July, although the pace of improvement appears to have slowed from the gains in May and June. Sales activity was mixed among the various types of outlets. Off-brand discount stores fared the best, especially in apparel items, and department stores reported the strongest summer season in several years. However, specialty stores, particularly upscale clothing chains, indicated a disappointing sales performance.

Retailers generally characterize consumers as reluctant to spend and very selective in their purchases. Apparel sales have been particularly sluggish. According to several respondents, large general price hikes and an absence of new styles have discouraged shoppers. One retailer noted that heavy discounting and sales promotions have been necessary to generate sales gains in recent months. Several sources said that they have been negotiating for smaller price increases from their apparel wholesalers and in some instances have changed suppliers in an effort to control prices. On the other hand, durable-goods sales, particularly for furniture, appliances, and consumer electronics

equipment, continue to strengthen--the result of considerable pent-up demand that has been augmented by demand from recent home purchases.

Low-financing rates and a perceived need to replace aging vehicles have sparked a recent surge in auto sales. Several auto dealers report increases in July as high as 20 to 30 percent over a year ago, with Big Three models outselling foreign nameplates. Big Three dealers also note that inventories are lower than desired, with stocks as low as 45 days. However, they add that they are embarking on tighter inventory control and consequently more conservative ordering.

Retailers report that summer employment has been normal to slightly below normal, although some discounters are replacing traditional sales staff with technical personnel as part of a longer-run response to more automated checkout and inventory-control systems.

Manufacturing. The recent strength in industrial activity continues to be led by several durable-goods industries. Producers of flat-rolled steel products report operating at virtual capacity, and they anticipate a full order book at least through the balance of the year. Major suppliers to heavy-truck producers also cite near-capacity operations. Despite a slight letup in orders from the peak pace of the first quarter, one producer is already booking orders for early 1994 delivery. In addition, industrial machinery producers note rising output and backlogs, which they expect to result in a record sales year in 1993. Consequently, some plan to forgo the usual summer vacation shutdown in order to meet the strong demand. A machine-cutting tool concern reports a recent surge in orders, leading to further backlogs.

Some producers have seen a softening in orders and output in the past few months, however. A parts supplier to major household appliance producers reports that orders slackened in May and June, apparently because of excess finished-goods inventories. An industrial controls manufacturer indicates that orders eased in the second quarter, particularly from customers in the utility, chemical, and paper industries.

Despite peak operations in several industries, employment prospects for factory workers have not improved appreciably. Even producers facing strong demand anticipate minimal new hiring. For example, a large heavy truck producer expects to add on no more than 300 workers over the next several months, even though his firm is facing mounting backlogs.

Financial Developments. Depository institutions generally report a continued outflow of deposits. Some institutions have attempted to reverse the trend by initiating new instruments. For example, a large thrift found success in attracting deposits with higher-than-market rates on one- and two-year certificates of deposit.

Several lenders report that business loans softened in recent weeks, and one lender foresees no pickup through the balance of this year because of an increase in cash flow generated by its customers. Loan officers also note a leveling off of consumer loan demand after a flurry of activity in the spring. Declining mortgage rates have sustained a steady volume of refinancing, but low housing starts in many parts of the District have slowed the rate of new applications. For example, a large thrift indicates that the volume of new mortgage loan applications so far this summer is below a year ago, although its mortgage rates are at least 100 basis points below last year's rates and are the lowest in 20 years.

## FIFTH DISTRICT-RICHMOND

### Overview

The Fifth District economy grew, on balance, but this growth continued to be moderate and uneven across sectors. Hot, dry weather boosted tourism and electric power demand but badly damaged agriculture. Retail spending was somewhat higher, while manufacturing was flat. Moderate growth was seen in bank lending, state revenues, and residential real estate activity. Commercial real estate remained mostly sluggish. Port activity was lower, and the shellfish industry continued to face serious supply constraints.

### Consumer Spending

Our mail survey of retailers indicated rising sales, wages, and prices but declining shopper traffic and employment in late June/early July. Retailers expected shopper traffic and sales to increase in the next six months but anticipated little change in employment.

### Manufacturing

District manufacturers surveyed saw little change in most indicators, except for higher raw materials prices. Weak product demand was cited as the most important industry problem. Respondents expected higher shipments, new orders, and raw materials prices in the next six months but lower employment.

### Ports

Representatives at District ports--Baltimore, Charleston, and Hampton Roads (Norfolk)--indicated lower imports and exports in June, compared with May and with a year ago. All three ports expected exports to increase faster than imports during the next six months.

### Tourism

Since early June, activity at District hotels, motels, and resorts was higher than in May or a year ago; good weather and package deals were cited as

causes. Most respondents were booked to capacity over the Fourth of July weekend and expected activity to improve in the next six months.

### Finance

District financial institutions contacted by telephone indicated that credit conditions improved slightly during the last six weeks. Commercial, consumer, and residential mortgage loan demands were reported marginally higher. Refinancing activity rose while mortgage originations were steady. Commercial, consumer, and residential mortgage loan rates all fell slightly.

### State Revenues

State tax analysts reported that revenue growth seemed to imply real economic growth rates of 2.5 to 3.5 percent in Virginia and North Carolina, 2 percent in West Virginia and Maryland, and 1 percent in South Carolina. Collections implied continued weakness in the District of Columbia economy, with sales and property taxes remaining sluggish.

### Electric Power

Hot weather caused especially high District electric power demand, according to power company analysts. Residential demand was up significantly, while commercial and industrial demands were steady. With only one exception, electric utilities had sufficient capacity to meet demand, though most were purchasing power from cheaper sources. The increased demand was expected to be temporary.

### Residential Real Estate

Real estate analysts and homebuilders surveyed by telephone reported that the residential market strengthened modestly in most areas during the past six weeks, though activity decreased slightly in Virginia and the District of Columbia. In Charleston, South Carolina, the lower-end market

weakened substantially due to the scheduled closing of the naval base, but home sales remained strong in the area's resort/retirement market. Home prices and starts remained mostly steady during the past six weeks.

#### Commercial Real Estate

Commercial real estate activity remained sluggish in most areas of the District during the past six weeks but continued to improve in the Charlotte and Raleigh areas. Many analysts throughout the Fifth District reported a rapidly shrinking supply of large blocks of office space. Much anchored shopping center construction was underway, though some landlords were having difficulty leasing existing space. Leasing activity was relatively flat in the industrial market in most areas.

#### Fisheries

Fishery analysts contacted by telephone indicated that District activity continued to decline. Seafood demand remained strong, but supply shortages were forcing District wholesalers to buy elsewhere. The crab harvest remained steady in Maryland in 1993 but was expected to drop about 30 percent in Virginia. The 1993 shrimp harvest in North Carolina was expected to be two-thirds of last year's total. Supply constraints had also afflicted scallop markets; scallop prices nearly doubled in the past year. Clam harvests remained steady, and the striped bass industry continued to recover.

#### Agriculture

Agricultural analysts and bankers reported drought and near-drought conditions and above-normal temperatures in most of the District. Corn, sorghum, tobacco, and soybean crops were mostly rated in poor condition, and yields were expected to be low. Bankers in some areas warned that their farm customers might face financial difficulties this fall because of bad harvests.

## SIXTH DISTRICT - ATLANTA

Overview: According to Sixth District contacts, the Southeast economy grew at a modest pace in June and early July. Consumer spending gains were again reported by most retailers, but momentum has slowed. Realtors and residential builders reported healthy sales and building activity, although multifamily and commercial real estate markets remain sluggish. Manufacturers generally experienced increased production and orders in June, with lumber, furniture, and home textile producers noting increases because of strong residential construction. However, their expectations about future production are less optimistic than they were earlier this year. According to bankers, commercial loan demand remains flat, but consumer lending, especially for automobiles and home refinancing, has increased in most areas. There were no reports of increasing wage or price pressures.

Consumer Spending: Retailers throughout the District reported that an upward sales trend continues; however, consumer spending growth has slowed in recent weeks. Smaller retail stores consistently had weaker sales than major retailers. Sales gains were most prominent in apparel, home improvement products, big ticket consumer durables, and autos. Auto sales did particularly well in June and mid-July, and the majority of dealers expect the recent trend to continue through the end of the summer. Most contacts in the hospitality industry expect further improvement in already strong tourism and business travel through the summer as air passenger traffic and convention attendance continue to outpace year-ago levels.

Manufacturing: Manufacturing activity expanded modestly in June and early July according to industry contacts. Most firms reported current increases in production and new orders; although few reported new hiring. Expectations for the near-term future have become less positive. Uncertainty and concern over taxes and health care have contributed most to declining expectations about future activity, according to many contacts. Most manufacturers stated they are not planning to add workers in the near term. Increasing backlogs of orders for home textiles were reported, as well as a pickup in orders for

sportswear, but production of other types of apparel has slowed because of declining retail sales growth. Strengthening residential construction is stimulating new orders at lumber and furniture companies, but commercial construction suppliers remain in the doldrums. Increased natural gas prices have boosted oil and gas production as well as business for related service companies. Energy companies are also planning capital expansion projects to meet environmental requirements. Defense-related job cuts continue for military contractors in the region, and cuts in both military and civilian aircraft orders have resulted in layoffs. Some industries, such as auto parts, noted slowing exports to Europe.

Construction: Real estate agents from across the District reported that home sales had leveled off in June and early July, though they remained above last year's levels. Starter and mid-priced homes continue to sell well, but luxury home sales are still fairly flat. Despite healthy single-family building, a lack of new home inventories has increased demand for resale homes in some areas. Most realtors and builders remain optimistic about the rest of the year, although a few contacts expressed concern that uncertainty about government fiscal policy was keeping potential buyers in their current homes. Increased rental rates have encouraged some multifamily building activity. Several contacts reported older multifamily properties were being purchased and refurbished at a much lower cost than new construction.

Commercial real estate markets remain slow. Several contacts have seen modest improvement in leasing activity and occupancy rates, but effective rental rates remain too low to encourage any new speculative building. Retail construction and build-to-suit projects are providing almost all of the new commercial projects in the District.

Financial Services: Bankers' reports indicate that loan demand was mixed in June and early July. Weak demand was noted in Mississippi and Louisiana, while the rest of the District experienced a modest increase. Contacts noted that there is a lot of competition for good commercial loans, with several banks pursuing any good deal that comes along. Many commercial borrowers are taking advantage of the low rates to refinance existing debts. Consumer lending, especially for new cars, has

picked up modestly in most of the District. Residential mortgage lending continues at a strong pace. Mortgage refinancings have begun to surge again after tailing off the latter part of June. Refinancings now make up about three-quarters of all mortgage loans.

Agriculture: In contrast to the Midwest, drought conditions exist in portions of Alabama, Georgia, and Tennessee. The situation is most severe in east-central Georgia and east Tennessee. In the affected areas of Georgia, the dry land corn crop may have been entirely lost. Cotton and soybean crops are also in need of rain, but are more drought tolerant than corn. Dairy farmers have been forced to dip into winter hay reserves because the pastures have become too dry to graze. In east Tennessee, grazing pastures and tobacco are being hurt the worst. Alabama crops have been less affected, but one-third of the corn crop acreage is now rated poor or very poor. On the other hand, Florida farm land has had at least adequate soil moisture in all areas except the northeastern coast. Mississippi and Louisiana crops are in good to excellent condition for the most part.

Wages and Prices: Factory contacts did not report any increases in raw materials or finished good prices. There were no reports of increasing wage pressures.

## SEVENTH DISTRICT--CHICAGO

**Summary.** Economic expansion generally continued in the District in June and early July, although flooding significantly disrupted activity in affected areas. Reports from retailers suggest that sales growth in the District picked up further upward momentum in June and early July. Housing industry contacts indicated that sales of new and existing homes continued to increase, although residential construction growth may have slowed somewhat. Purchasing managers' surveys and reports from individual firms depicted a modest slowdown in the rate of expansion in overall industrial output, while the pace of the recovery in motor vehicle production was little changed. Flooding has inflicted considerable damage and hardship, but it is not expected to threaten expansion in the overall District economy. Agriculture has been the sector hardest hit by the flooding, and crop prospects are under considerable uncertainty.

**Retail Sales.** District retailers were generally encouraged about sales activity in June and July. A major chain reported solid growth in same-store sales, led by continuing strength in appliances and improvement in apparel. Sales gains in this company's stores in the Midwest generally continued to outpace the national average, with little impact from recent flooding evident in the company's regional sales aggregations. Another large retailer reported that sales in recent weeks have been "quite good," primarily due to the arrival of hot summer weather. This arrival was tardy, however, and while apparel sales strengthened, they did so at lower clearance-type margins, at a time when margins have been under pressure more generally. This firm characterized same-store sales gains in recent months as "kind of soft", and revised its forecast for sales in 1993 downward slightly. Another large chain reported increased sales gains during late June and into July, with results in the Midwest outpacing the national average (particularly in Michigan). This firm noted that sales strengthening was evident in household products as well as apparel. Several retailers reported improvement in sales in the Detroit area, where new store opening programs have been announced by a number of retail chains. A chain of warehouse stores stated that demand from wholesale cash-and-carry customers (primarily small businesses) is "a lot more robust now than it was two months ago."

**Housing.** Sales of new and existing homes held up well or continued to increase in recent months, according to contact reports, but a modest slowing in new home construction was also noted. One of the largest realtors in the District reported a record month for unit sales volume in June, and stated that appraisals of market conditions among the firm's salespeople continue to improve during the month of July. This contact noted that the prospect of higher personal income tax rates was one potential factor promoting sales, due to the increased value of the tax benefits of home ownership. An association of home builders in the

District characterized recent trends as "good;" the quality and interest of buyer traffic has remained relatively strong and sales have strengthened somewhat further, particularly in the lower end of the market. At the same time, however, starts have slowed modestly, and this contact stated that builders' comfort level with the overall economy may have fallen off from earlier in the year. However, a major producer of window and door hardware stated that its own production has been "going bananas" in the last three months, following an increase in orders that was largely unanticipated.

**Manufacturing.** Purchasing managers' surveys and reports from individual firms were consistent with slowing but continued growth in District production in recent months. Patterns in the production component of purchasing managers' surveys in Chicago, Detroit, Milwaukee and Western Michigan generally suggested a modest slowing in growth from earlier in the year, but continued expansion was indicated for a majority of respondents in each of these surveys through the month of June. A July survey of metalworking firms indicated renewed strengthening in momentum, following a slowdown in growth earlier in the year. The association conducting this survey reported that member firms have stepped up their apprenticeship training, after this activity "had remained dormant for some time."

Manufacturing contacts generally reported little change or moderate improvement in their own sales growth, but political and economic uncertainties were often identified as a weight on business activity more generally. An automaker confirmed its announced production schedules for the third quarter, which call for a significant increase over the same period last year. Another automaker anticipated a brisk increase in domestic sales in the 1994 model year. A large producer of auto parts reported increased aftermarket sales, with higher unit volume as well as modestly higher prices. Two electric utilities in Michigan reported further strengthening in industrial sales. A manufacturer of heavy-duty trucks reported a substantial increase in sales growth in June, and noted that industry sales reached their highest level for June since 1979. However, one heavy-duty truck producer expected industry output to flatten out (at relatively high levels) over the remainder of the year. An industry survey indicated that heavy-duty truck order backlogs remain firm, with buyers still requesting deliveries on time or ahead of schedule. A large manufacturer of business furniture systems expected a modest real gain in industry sales in 1993, but not so strong an increase as the recovery during 1992. This firm stated that the potential for sales to the financial services industry is relatively strong, following the improvement in profitability in the industry in recent years. A large chemical producer gave a mixed assessment of the prospects for earnings gains in the latter half of 1993, partly due to continued pricing

weakness. Several firms noted significant, continuing weakness in European markets, with one stating that this weakness was leading it to hold domestic capital spending "a little closer to the vest."

**Effects of Flooding.** Flooding has inflicted considerable hardship, damage and disruption to the affected areas of the District, particularly Iowa and portions of Illinois along the Mississippi. Insurance, disaster relief, voluntary assistance and other offsetting effects are anticipated to soften some of the losses. However, the full impact on the overall District economy will not be known for several months. Much retail activity has been shut down in flooded areas, but stores also reported a run-up in sales in anticipation of the floods, and retailers in neighboring areas have seen a pickup in recent weeks. One major discount retailer revised its estimate of sales in the region for 1993 substantially upward, because of the sales expected to be generated in response to the flood damage. Most manufacturers continue to operate outside of the flooded areas, although some plants in Des Moines closed (with resulting layoffs) due to power or water shortages after flooding of the Des Moines and Raccoon rivers. Automakers reported some delays in shipments for plants near the affected areas, but there were no significant production disruptions. Distribution in the area has shifted to more costly alternative routes where they are available. Hundreds of small businesses were flooded out, although many flooded warehouses were cleared before the water arrived. Agriculture has been the hardest hit sector, with water damage not restricted to areas close to the flooded rivers.

**Agriculture.** Extensive flooding and slow-to-develop crops add to the uncertainties regarding this year's harvest prospects. Across the District, crop conditions as of July 25th ranged from mostly "good" in Illinois, Indiana, and Michigan to mostly "fair-to-poor" in Iowa and Wisconsin. Assessments of the crop acreage covered by flooding continue to be adjusted as repeated, heavy rainfalls through last weekend added to the expected river cresting levels and triggered still more levee failures. Aside from extensive crop losses on the flooded acreage, yields elsewhere in the water-logged areas remain vulnerable to ponding, inadequate fertilization and weed control, and the possibility of being hit by frost before reaching maturity.

Flooding continues to cause bottlenecks in the transportation network. Fortunately, water levels on the upper Mississippi have recently retreated, even falling below flood stage for most areas north of Davenport, Iowa. Several locks on this portion of the River have reopened, permitting local barge movements of grain, coal, and fertilizer. However, the long-haul barge shipments needed to help replenish grain stocks at the critical Gulf Port terminals still await the reopening of locks around the St. Louis area. Some observers believe it will take 10 days of no rain before commercial barge traffic in that area can resume.

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### EIGHTH DISTRICT - ST. LOUIS

#### **Summary**

Despite flooding in parts of the District, contacts report that their operations have been largely unaffected. For most establishments, the biggest change has been the use of trucks rather than railroads for their transportation needs. A preliminary assessment puts a lower bound on damage from flooding in the District at \$1.5 billion to \$2 billion. This estimate is tentative at this point and subject to a relatively large forecast error.

Flooding aside, other reports from District firms are mixed, with some experiencing modestly increased sales and others having flat or declining sales. Residential construction activity is strong in most areas of the District, as are new and existing home sales. Area banks for the most part were unaffected by recent flooding. While excessive rainfall and flooding have affected northern portions of the District, hot, dry weather is the norm in the southern reaches.

#### **Manufacturing and Other Business Activity**

Most contacts in both flooded and non-flooded areas report that the flooding has had minimal effect on their operations. Delays in transporting supplies and output because of flooded rail lines are the main hardship. A switch to trucking has created little disruption and has sufficed for most establishments. One major manufacturer in St. Louis has had to close a plant because of an evacuation order. Other large manufacturers along the Missouri River, especially near Jefferson City, and along the Mississippi River have had to close temporarily because of flooding. In total, the Missouri Department of Employment Security estimates that about 10,000 workers have been shut out of their workplaces by flood waters. This number will fluctuate, of course, as the rivers continue to rise and fall.

Public utilities in the affected areas report that service has been maintained, although in some cases a great deal of overtime has been employed to stay on top of service losses. Most major terminals and substations have been unaffected by the flooding. The total extent of flood damage at the household level, though, cannot be determined until flood waters recede and people return to their homes.

Retailers in the St. Louis area report sales, especially in apparel, as relatively flat compared with the same period last year. The riverfront has seen an increase in foot traffic, but no proportionate movement in purchases. Some are concerned that misinformation reported in the media about flooding in the St. Louis area could lead to a decline in retail sales in the coming weeks because potential tourists cannot distinguish between the city's flooded and non-flooded areas. Apparently the national attention has yet to affect the city's convention business, however.

Contacts in the iron, hydraulic parts and oil-extraction equipment industries report that sales are good and growing modestly. One contact emphasized international sales as being strong, especially from developing countries, while domestic sales are almost nonexistent. Many domestic firms, the contact reports, are postponing capital equipment expenditures until 1994. A contact from the heating and cooling industry reports that industry-wide sales have fallen dramatically and that inventories are growing.

According to a recent National Federation of Independent Businesses survey of District firms, about one-half of the respondents do not believe this is a good time to expand. One-fourth of the respondents felt conditions in the coming six months would be somewhat worse; however, one-fourth will increase employment this quarter.

### **Construction and Real Estate**

Declining interest rates continue to stimulate new construction and both new and existing home sales in most parts of the District. The housing market in Little Rock remains tight, as potential buyers outnumber available properties. Contacts report rising prices for new and existing homes as well as rental properties. The St. Louis and

Memphis markets have also picked up in recent months, although homebuilders in St. Louis are still behind because of the weather. Contacts in the two cities also report improving conditions in commercial real estate markets: In St. Louis, retail vacancy rates are down and rental rates are up; in Memphis, speculative warehouse building is on the rise.

### **Banking and Finance**

Most District banks in flooded areas have faced minimal disruptions to their businesses. Several area banks are offering special loan products and low rates to flood victims. Outside the flooded areas, consumer loan demand is reported to be increasing, especially for auto loans. Mortgage refinancings at area financial institutions continue at a brisk pace. No appreciable pickup in commercial loan demand has been reported.

### **Agriculture and Transportation**

Weather conditions vary dramatically throughout the District. In the northern parts of the District, flooding has affected an estimated 1.7 million acres in Missouri, more than 750,000 acres in Illinois and roughly 35,000 acres in Kentucky. In areas that have not been affected, the corn and soybean crops are in mostly good condition, and those farmers are reaping the benefit from higher grain prices. Much drier weather has prevailed in the southern portions of the District. Contacts in Arkansas report that dry, hot weather has led many farmers to irrigate their crops. Arkansas poultry producers report thousands of chickens have died because of the heat.

According to the Army Corps of Engineers, the Port of St. Louis probably will not open until late August or early September. The closure of the upper Mississippi to barge traffic has led to only a slight increase in activity on the Ohio River, principally grain shipments. Flooding has also disrupted rail and trucking activities. A large District trucking firm reports that although shipments are off from one year ago, they are receiving some business they would not usually receive because of rail and barge disruptions.

**NINTH DISTRICT--MINNEAPOLIS**

Moderate growth continues to characterize the economy of the Ninth District in spite of adverse weather and flooding in many areas. Residential and commercial construction continues above 1992 levels and is perhaps the strongest component in the district economy. General merchandise and vehicle sales are also good except in areas where flooding has slowed retail spending. The tourist industry is generally strong in western portions of the district but somewhat slow in regions plagued by persistent rains. Price levels are stable with no indications of inflationary pressures while labor markets show modest improvements in employment levels. However crops, particularly soybeans and corn, have suffered extensive damage from heavy rains, flooding and cool weather; such losses are likely to exceed \$1.5 billion.

**Construction and Housing**

Construction continues to be one of the strongest areas in the economy. Publicly awarded construction contracts in Minnesota and the Dakotas continue to run 25 percent above 1992 levels. Residential construction is also strong throughout most areas of the district. "Home builders are seeing a steady flow of business this summer," said one Minneapolis-St. Paul builder's association spokesperson. A substantial new apartment project was announced in Fargo, N.D. Newspapers also report substantial construction of housing in the Black Hills region of western South Dakota, new or expanded tourist facilities in northeastern Minnesota and retail buildings in Grand Forks, N.D.

**Consumer Spending**

In June and July, general merchandise sales appear stronger than in April and May. Shopping mall managers in eastern South and North Dakota reported traffic up from 1992 levels. A major Minneapolis-based retailer reported June comparable-store sales up about 4 percent from 1992 levels and stated that they were encouraged with the performance of their moderate-price division. New vehicles generally continue as a strong area of consumer spending although dealers and industry spokespersons in areas affected by flooding report that sales are down for autos and particularly for pickups.

### Tourism

Tourist activity is generally good for the district as a whole. Industry sources and newspapers from Michigan's Upper Peninsula, North Dakota and Montana all report a generally good season. Bridge crossings into the Upper Peninsula are about 5 percent above year-earlier figures. There is increased bus tour traffic in both North and South Dakota. The tourist season in Montana had a strong start, but visits have slowed recently in response to wet weather. In South Dakota business appears mixed. A Tourism Department official said visits were down in spite of a 12 percent increase in inquiries while state park visits are up from 1992. And cool, wet weather has slowed tourism somewhat in Minnesota and Wisconsin according to industry and government officials.

### Manufacturing and Mining

Manufacturing output appears to have grown slightly. Year-to-date industrial use of electricity continues above trend. New small manufacturing ventures were opened or announced in Williston and Westhope, N.D., Menominee, Wis., and Duluth, Minn. Most publicly-traded small and medium manufacturing firms continue to report improved earnings compared to corresponding periods in 1992. District advisory council members report that manufacturers are cautious about capital investments, but are buying new machinery or upgrading existing facilities to increase output with existing staff.

Mining employment is stable while output is rising a bit. One western South Dakota gold mine is making a major investment to reach a new ore body. And an iron mining firm with operations in the Lake Superior region reported that its production and sales were higher than 1992 levels and above the firm's own earlier projections for the 1993 season.

### Prices, wages and labor markets

There is little evidence of upward pressure on price levels. Gasoline prices are well below year-earlier levels. Lumber prices have moderated somewhat after sharp increases earlier in the year. Advisory council members and Ninth District directors report generally stable prices in their businesses or communities and note that new public and private sector compensation agreements

generally include limited increases in wages with most increases channeled into health benefits. Employees of a major airline are likely to approve an agreement that will significantly cut their compensation as the firm struggles to avoid bankruptcy.

Non-farm employment is above year-earlier levels in all Ninth District states with most of the increase in services and trade employment. Unemployment rates declined in Montana, North Dakota, South Dakota and the Upper Peninsula of Michigan. No large layoffs were reported.

### Agriculture

Excessive rain and flooding has seriously damaged crops, particularly in eastern South Dakota, southern Minnesota and west central Wisconsin where corn and soybeans predominate. As much as 10 to 15 percent of planned corn and soybean acres were never planted due to persistent adverse weather beginning in April. In a special survey agricultural bankers in these areas expected corn and soybean yields to be only about 60 percent and small grains to be 75 percent of normal. Ninety-two of 227 counties in Minnesota, Wisconsin and South Dakota have already been declared disaster areas. Although wheat-growing areas had generally favorable conditions through June, recent heavy rains and flooding in eastern North Dakota have raised concern about the harvest. Crop development is two to three weeks behind normal across virtually all of the district due to unseasonably cool weather. And rains have obstructed hay harvesting across Wisconsin, pushing hay prices to record levels and squeezing net incomes in dairying.

But above-normal precipitation has been a boon to cattle raisers, pasture and range conditions in the Dakotas and Montana are reported to be the best in many years. Irrigation reservoir levels in western areas of the district are recovering from declines in preceding drought years. Meat prices, especially for beef, continue to be generally favorable.

## TENTH DISTRICT - KANSAS CITY

Overview. The Tenth District economy continues to grow at a moderate pace. Retail sales are still increasing, housing activity remains strong, and bank loan demand is up slightly. The energy sector continues to improve, and many district farmers expect strong earnings despite wet weather and flooding. Retail prices are generally steady and manufacturers report stable to slightly higher input prices.

Retail Sales. While most district retailers report only a slight improvement in sales compared with a year ago, retail sales have strengthened in the past month. Small sales increases were reported for most categories of merchandise, with furniture sales being relatively stronger and apparel sales weaker. With consumer demand sluggish recently, retailers are holding prices steady and intend to hold prices relatively constant over the next three months as sales are expected to improve only marginally. Instead of buying leading brands, some retailers are stocking cheaper goods of comparable quality. Satisfied with current inventory levels, retailers plan no changes for the rest of the year.

Auto dealers report a strong increase in sales over the past month. Ample financing is available for both dealers and potential buyers. Most dealers are satisfied with current inventory levels and expect strong sales for the remainder of the year.

Manufacturing. Purchasing agents report stable to modestly higher input prices compared with a year ago. Input prices are expected to remain unchanged or rise slightly in the near term. While materials are readily available, lead times for some steel products have increased. Respondents are either satisfied with their current inventories or are trimming them slightly.

Although many respondents are operating near full capacity, few bottlenecks are reported. Exporting firms report that sales abroad are increasing or steady.

Energy. Drilling activity in the district continues to improve despite generally soft oil prices. The average number of operating drilling rigs in district states jumped from 203 in May to 240 in June. During the first three weeks of July, the district rig count crept up to 244. As a result, the average rig count stands about 12 percent higher than at the same time a year ago.

Housing. Builders report that housing starts were up slightly or steady in the last month, and up significantly from a year ago. Sales of new homes are also higher relative to both a month ago and a year ago. As a result, new home inventories are low. Building materials are readily available, but builders expect prices of materials, especially lumber, to rise further in the near future.

Mortgage demand remains strong because of low mortgage interest rates. While mortgage rates have continued to fall slightly in recent weeks, most respondents expect them to show little or no change over the rest of the year.

Banking. District bankers report slightly stronger loan demand last month. Consumer loan and construction loan demand were up at most banks, while commercial and industrial loan demand was constant to up. Demand for home mortgages and commercial real estate loans was mostly unchanged. Loan-deposit ratios were constant to up from the previous month and mostly up from a year ago.

No respondents changed their prime rate last month, and none expects to change that rate in the near future. Consumer lending rates were also

constant at almost all banks, with no change expected in the near term. Lending standards were generally unchanged.

Deposits were up at most responding banks during the last month. Demand deposits were mostly higher. NOWs and MMDAs were mixed, however, and large CDs and small time deposits were constant to down.

Agriculture. Wet weather and flooding have caused significant crop losses in Kansas, Missouri, and Nebraska. Some farmers were unable to plant corn and soybeans due to prolonged wet weather, and some crops were destroyed by flooding. Corn and soybean yields are expected to be below normal, but wide margins for error bracket current estimates of crop losses. Missouri, where up to a fifth of the state's corn and soybean acreage may have been lost, accounts for the lion's share of the district's crop losses.

The wet weather has also slowed the district's winter wheat harvest. A large wheat crop is expected despite the slow pace of the harvest and hail storms that have reduced wheat yields in some areas.

The net effect of the wet weather on the district farm economy will be small, although failures among marginal farm borrowers are expected to continue. Several years of solid earnings have shored up farm balance sheets across the district, enabling most farmers to ride out the rough weather. In addition, many district farmers still expect strong earnings this year. Farmers who harvest normal or near-normal crops of corn and soybeans will benefit from higher crop prices, and the large wheat crop will bolster farm incomes in much of the district. Most livestock producers in the district expect solid earnings, although higher corn and soybean prices will push up feed costs and trim profit margins.

## ELEVENTH DISTRICT--DALLAS

The District economy continued to expand slowly from early June through mid-July. Most manufacturing industries reported sluggish growth although industries tied to residential construction grew strongly. The service sector reported continued slow growth in sales and employment. Residential construction remained robust in most markets and highway construction improved. The District drilling rig count increased in response to continued strength in natural gas prices. Retail sales increased slowly throughout most of the District. Agricultural conditions improved slightly.

Most respondents in the manufacturing sector reported that orders were flat to slightly up. Respondents in the lumber and wood products, furniture and fixtures, and stone, clay and glass industries reported continued strong orders due to strength in the residential construction sector. Most manufacturing industries reported that inventories were either manageable or near desired levels and that capital spending remained weak. Respondents in the electrical and electronic equipment industry reported overall flat orders, although several respondents noted strength in orders tied to personal computer sales. Paper producers said that orders for most of their products have been flat. A producer of corrugated boxes noted a gradual rise in orders from manufacturers in Texas. One respondent noted an increase in exports of newsprint to Mexico. Oil field equipment producers reported weak demand, particularly from their international customers. Chemical producers said demand was weak from both the U.S. and European markets. Several industries that supply products to the health care sector reported declines in orders.

High technology equipment and many disposable medical products are considered costly and respondents say that demand has been reduced in anticipation of the new health care plan.

Respondents in the **service sector** reported that employment and orders continue to grow at a slow pace. Respondents said that hiring in anticipation of growth is a thing of the past and that employment growth will only pick up after activity picks up. A respondent from the legal industry reported that a move by insurance companies to use more in-house lawyers has reduced demand at law firms. One health care respondent said that they are cutting patient costs, through procedures such as more outpatient surgery, in anticipation of health care reform.

District **construction and real estate** activity continued to increase primarily due to strength in residential and highway construction. Respondents said that office vacancy rates remained high in Dallas/Ft. Worth and Houston, and commercial construction remained weak. Office vacancy rates continued to decline in Austin. Highway construction continued to increase as a result of the 1991 transportation bill. New home demand was reported to be strong across most of Texas, but new home sales have recently weakened in Houston.

**Retail sales** increased slowly throughout most of the District. Several retailers reported that they lowered their selling prices to maintain market share and keep inventories from building up. A few respondents reported that they anticipate lowering prices because their inventories were larger than desired. Apparel sales were said to be particularly slow. Sales along the Mexican border continued to be below last year's level because Mexico

increased enforcement of a \$50 limit on goods brought back into Mexico by its residents. Auto sales were slightly above last year's level, with particularly strong sales in the San Antonio area.

The District oil and gas rig count has increased since April primarily due to continued strength in natural gas prices. Natural gas drilling in the Gulf of Mexico was reported to be strong. Oil prices fell sharply throughout the first three weeks of July. Respondents reported that a large surplus of oil on the world market and the possibility of oil sales from Iraq has driven down oil prices. The recent declines in oil prices have clouded a previously positive outlook for drilling during the second half of the year. Respondents still expect drilling to increase during the remainder of 1993 due to continued strength of natural gas prices and the availability of previously budgeted funds.

Loan demand at district financial institutions slowed in recent months. Lack of borrower capital and insufficient cash flow were the most cited reasons for rejecting loans. Home mortgage originations and refinancings remain a bright spot.

District farming and ranching conditions have improved slightly since the last survey. Most crops were in good condition and on schedule, although ranges and pastures were beginning to deteriorate from recent hot and dry conditions in most of the state. Cotton producers were optimistic about the potential for export expansion due to the smaller than anticipated yield of cotton in China. Crop prices were generally lower than last year while livestock prices were mostly higher.

TWELFTH DISTRICT -- SAN FRANCISCO

Summary

Weakness in California continues to offset economic growth in other District states. In California, economic activity remains sluggish across a broad range of sectors--including manufacturing, construction, retail, finance, and government--and new layoffs were announced in the computer industry. Cutbacks in aerospace also are restraining growth in western Washington. Outside of these regions, growth is reported in several areas, with overall conditions strongest in eastern Washington, Utah, and Idaho. Overall business sentiment remains flat after declining from early 1993, with most contacts expecting continued slow growth.

Business Sentiment

Sentiment among Twelfth District business leaders is little changed from our June report. About half of the respondents expect the real economy to expand during the next four quarters at a rate at or above trend growth. This proportion is about the same as in June, but is down from two-thirds in April and three-quarters in March. Most other respondents expect the economy to expand, but at a rate below trend. In general, contacts from Idaho, Oregon, and Utah expect their regions to perform better than the national average. Most contacts in California and Washington, however, expect their regions to underperform the national average.

Retail Trade and Services

Retail activity varies widely across the District. In California, sluggish retail sales are reported by several contacts. Soft-good sales are reported flat and sales of cars and light trucks are reported down 2 percent from a year earlier. Contacts in western Washington also report weakness in retail trade. In Arizona, durable goods sales are reported strong, especially for autos, but non-durable goods sales are lackluster. Strong sales are reported in Idaho and Utah.

Conditions in service-related industries are mixed. Tourism is reported strong in Idaho and Utah, especially in national parks. In California, the motion picture and amusement park industries are reported to have seen rapid job growth over the past year. A contact in the legal industry reports flat or declining revenues, with downward pressure on prices. The state of California reached a budget agreement that extends temporary sales taxes and shifts property tax revenues from local governments to the state. Contacts in local government, however, report that the shift in revenues threatens to cause deep cuts in government services, employment, and wages. State budget shortfalls also are reported in Oregon and Washington. A contact with a California non-profit agency reports reduced funding from both public and private sources at a time of increased need.

### Manufacturing

Manufacturing activity is mixed in the District, with weakness centered in aerospace and defense-related industries. In Washington, contacts report that declines in defense and aerospace continue to impede economic growth. Contacts in California and Arizona also report that high-tech manufacturing is contracting due to cutbacks and restructuring in defense and aerospace. Southern Arizona, however, is benefitting from a shift of aerospace production activity from California. Computer manufacturing is reported strong in Oregon. In northern California, however, layoffs due to restructuring were announced at a major computer producer, with the job losses concentrated in Silicon Valley.

A few manufacturing industries are showing signs of improvement. A contact from Arizona reports strength in the advanced technology sector, particularly semiconductors, customized integrated circuits, and embedded microchips. High-tech manufacturing is reported strong in Idaho. Construction equipment sales are reported up in Utah. In California, contacts report strength in textiles, apparel, and other nondurable industries.

### Agriculture and Resource-Related Industries

Most contacts report a generally favorable outlook for agriculture. Rain damage to crops is reported in parts of Oregon and Arizona, but improved water availability has boosted production in California and eastern Oregon. A contact in the railroad industry reports very strong exports of fruits and vegetables. In Utah and Idaho, depressed conditions are reported in timber and mining. In Alaska, a contact reports weakness in logging, mining, and seafood. Recent oil discoveries, however, have improved prospects for increased economic activity.

### Construction and Real Estate

District real estate and construction markets show widely disparate conditions, with the weakest performance reported in southern California. A contact in southern California reports that sales activity and prices continue to decline for homes valued over \$300,000. Some activity, however, is reported in starter home construction, as disposal sales of foreclosed vacant land are providing additional and better locations for low-end projects. Mixed conditions also are reported in western Washington, in part due to layoffs in aerospace. In contrast, southern Arizona is reported to be having its largest volume of home sales in years. A surge in new residential construction is reported, and commercial real estate also is reported to be moving well. Housing markets in eastern Washington, Utah, and Idaho are reported to be very strong. Higher prices for building materials are reported to be pushing up home prices and construction costs.

### Financial Institutions

Mixed conditions are reported across District financial markets. In California, contacts report conditions as generally improving, with modest growth expected for consumer lending. Business borrowing remains lackluster, however, and foreclosure rates are expected to rise in areas hit by aerospace cutbacks. A contact from Oregon reports high profits and a strong demand for credit. Conditions in Idaho and Utah are reported as excellent, in part due to strong construction lending.