

**SUMMARY OF COMMENTARY ON CURRENT ECONOMIC CONDITIONS**

**JANUARY 1994**

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## SUMMARY\*

Economic activity continued to expand with signs of acceleration in some sectors, according to most Federal Reserve District reports. Consumer spending, especially on household-related items, was strong during the holidays in most districts. Manufacturing activity strengthened, and the manufacturing employment picture improved somewhat. Residential real estate sales and construction grew robustly in almost all districts. Commercial real estate leasing and construction improved in some districts but remained generally sluggish. Loan demand increased somewhat in many districts. Several districts reported weather-related stress to agricultural crops, but crop prices rose and crop income prospects improved. Little upward pressure on wages and prices was indicated by almost all districts; however, reports of lumber price increases were widespread, and scattered labor shortages were reported. Weak economic conditions continued in southern California.

### CONSUMER SPENDING

Retailers in most districts enjoyed strong sales that met or exceeded expectations during the holiday season, although the Boston District's retailers were disappointed with their modest gains. In the Atlanta, Dallas, and New York Districts, stores offered earlier-than-normal holiday price discounts and in the Chicago, St. Louis, and New York Districts, retailers indicated they advertised more than normal. Retailers in the Boston, Kansas City,

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Philadelphia, Richmond, and St. Louis Districts expected continued economic growth to boost retail sales moderately this spring.

Most districts reported robust sales of electronics and other home-related durables during December. Retailers in the Dallas, Minneapolis, St. Louis, and San Francisco Districts indicated that automobile sales were strong, and those in the Kansas City and St. Louis Districts expressed optimism about prospects for sales of new cars and trucks in 1994. In contrast, the Atlanta, Chicago, Cleveland, Dallas, New York, and San Francisco Districts reported that apparel sales were weak; Kansas City, however, reported generally strong apparel sales.

## **MANUFACTURING**

Most districts reported that manufacturing activity strengthened. Reports from Cleveland and Minneapolis indicated that some factories were operating near capacity, and several districts reported signs of stronger demand for manufactured products. The Atlanta, Boston, Dallas, and Minneapolis Districts noted increased demand for construction-related products, while stronger demand for automotive products was cited in the Boston, Chicago, and Cleveland reports. Personal computer orders strengthened in the Boston and San Francisco Districts, while capital equipment orders rose in the Cleveland District. The Atlanta District reported continued strength in textile orders arising from residential home sales and refurbishing. Defense-related manufacturing, however, continued to be sluggish in the Boston, Atlanta, and San Francisco Districts, and apparel manufacturing apparently was lackluster in the Atlanta and Dallas Districts. Looking forward, manufacturers in several

districts expected continued economic expansion in early 1994 and looked for continued improvement in business conditions.

Most reports of manufacturing employment indicated improvement. Producers in several districts increased employment a little and those in some districts planned to add workers if economic growth continues. Manufacturers in the Boston and Richmond Districts expected stable employment levels in 1994. Defense-related cutbacks in employment, however, were reported in the Atlanta, Cleveland, St. Louis, and San Francisco Districts, and apparel manufacturers in the Atlanta District reported further cutbacks in employment and a shortening of the factory workweek. In the New York District, several major manufacturers announced layoffs.

## **REAL ESTATE**

Reports from most districts indicated substantial improvement in residential real estate sales and construction. Home sales increased in the Boston, Richmond, Atlanta, St. Louis, and Kansas City Districts. Homebuilding also increased in these districts and in the New York, Minneapolis, and Dallas Districts, where residential construction activity exhibited unusually strong growth. San Francisco contrasted continued weakness in residential sales and construction in southern California with robust housing activity in Idaho.

Commercial real estate activity was mixed. Office vacancy rates fell in the Richmond and Atlanta Districts. New York reported some reduction in Manhattan vacancy rates, but that market was still considered weak. Commercial construction increased in the Richmond, Dallas, and Minneapolis Districts. Commercial real estate in California remained weak according to the San Francisco report.

The New York, Richmond, Atlanta, Kansas City, Dallas, and San Francisco Districts reported tight markets for building materials and/or construction labor. In several districts, short supplies of these inputs delayed some construction projects; in some districts, the tightness in supplies of inputs led to higher construction costs, which placed upward pressure on housing prices.

#### **FINANCE**

Commercial banks in most districts reported that loan demand strengthened somewhat. Bankers in the Atlanta, Cleveland, Dallas, Kansas City, Philadelphia, Richmond, and St. Louis Districts reported moderately higher commercial loan demand. Sluggish commercial lending was reported by banks in the New York District, however, and some lenders in the San Francisco District noted that commercial loan demand had weakened slightly. Consumer loan demand was reported to be moderately higher in the Atlanta, Cleveland, Dallas, Kansas City, New York, Philadelphia, and St. Louis Districts but was unchanged in Richmond. Atlanta and Cleveland noted especially high levels of automobile lending, and Kansas City and Dallas indicated increases in residential real estate lending. Atlanta and Cleveland noted slight declines in mortgage refinancings, although activity remained high in both districts. Bankers in the New York, Philadelphia, and Richmond Districts reported sharp declines in refinancing activity.

#### **WAGES AND PRICES**

Most districts noted little general upward pressure on prices or wages, although several reported increases in the prices of lumber and building materials and scattered labor shortages. The Boston, Cleveland, Richmond, Atlanta, Minneapolis, Kansas City, and San

Francisco Districts reported that virtually all retail and manufacturing prices were little changed, and Chicago reported that the prices paid by manufacturers declined. Energy prices declined in the Minneapolis, Kansas City, and Dallas Districts. Prices of aircraft-quality aluminum were soft in the San Francisco District, but steel prices rose in the Cleveland and Chicago Districts, and copper prices were somewhat higher in the Minneapolis District. Increases in the cost of lumber were indicated by the New York, Richmond, Kansas City, and Dallas reports. The Richmond, Dallas, and Atlanta reports also indicated higher building materials prices. In the Atlanta and Dallas Districts, housing prices were moving up somewhat, and the New York report indicated that higher materials prices could soon lead to upward pressure on housing prices.

Some districts reported tight labor markets for specific workers. Atlanta, Kansas City, and San Francisco indicated a shortage of skilled construction workers, and Chicago observed that finding skilled production workers and tradespeople was increasingly difficult. Dallas reported a short supply of temporary workers and a rise in their wages, but indicated that competition was keeping wages stable in other business services.

#### **AGRICULTURE**

Several districts indicated that worse-than-normal December weather and the lingering effects of abnormal summer and fall weather disrupted agricultural activity, but farm income levels remained steady. Snow and cold weather delayed winter small grain planting in the western part of the Richmond District, and cold weather delayed tillage in parts of Minnesota and North Dakota. Dry weather in the Dallas District damaged pastures, winter wheat, and the hay crop. Richmond and Dallas contacts expressed concern over the adequacy of hay

stocks. San Francisco reported that potato production was down in Idaho but up strongly in Washington and Oregon. The Chicago, St. Louis, Minneapolis, Kansas City, and Dallas Districts noted higher crop prices. Several districts indicated that higher grain prices would support crop receipts, but Chicago and Kansas City also noted that higher grain prices would also push up feed costs and reduce profit margins for livestock producers. Chicago and St. Louis indicated declines in livestock production.

## FIRST DISTRICT - BOSTON

First District businesses continue to report small gains.

Although recent results are mixed in all categories, retailers are generally less pleased than manufacturers or residential real estate professionals. Nonetheless, all three groups are moderately optimistic about 1994. Insurance companies are less upbeat.

Retail

Although First District retail contacts were cautious in their holiday sales forecasts, most express some disappointment at sales increases of 1 to 4 percent from the year-earlier period. Two exceptions, large firms catering to specific markets, enjoyed double-digit growth in December sales.

Retail contacts noted some unusual holiday shopping patterns this year. Durables were a big seller, particularly electric appliances, whereas apparel, especially women's clothing, did poorly. Sales fluctuated from one day to the next without obvious explanations. Early promotions generated a busier-than-usual week after Thanksgiving, but continued promotions failed to produce a hoped-for surge the week before Christmas. Retailers observed fewer impulse purchases by shoppers.

Despite the ups and downs of December sales, retailers say they are optimistic about 1994, sensing increased consumer confidence. Department and specialty stores anticipate modest sales growth of 1 to 5 percent; the merchants with strong December results expect sales to grow by as much as 10 percent. All contacts plan to open new stores in 1994 and to raise employment levels accordingly.

Manufacturing

First District manufacturing contacts report solid sales increases from a year ago in the domestic automotive, consumer electronics, and construction markets. Demand for other products is more mixed. A supplier to the furniture industry has experienced a sharp turnaround from last year's slow sales pace, but a furniture manufacturer reports a small decline. Medical suppliers indicate slightly higher revenues than a year ago from small equipment and spare parts, but declines of 20 to 30 percent for major equipment. Contacts in the aircraft industry indicate higher demand from some foreign markets, particularly developing countries. However, more generally, the commercial airline industry is reported to be weak, and defense orders are up only a little at best. Demand for some new computers is increasing rapidly, while traditional lines are in decline. Sales volumes are reportedly rising for higher-end paper products, but competition is limiting revenues from commodity papers. A contact in the machine tool industry indicates that sales remain flat. European demand continues to slip for a wide variety of manufactures.

Contacts see little evidence of inflation, as selling prices are being limited by competition, greater operating efficiencies, and lack of cost pressures. Only one-quarter of the respondents report any increases in materials costs. These generally lie in the range of 3 to 4 percent, and are attributable largely to specialized electronics products and, more recently, textiles. Lumber prices have nearly stabilized after large jumps.

About four-fifths of the manufacturers contacted have reduced employment during the past year. Most of these businesses now plan to

stabilize their head counts, although further declines are expected at some manufacturers of aircraft parts. The other one-fifth have increased their employment during the past year by 7 percent or more, and plan to expand their capacity in the coming year.

First District manufacturers generally express optimism about the coming year. They are heartened by higher incoming orders, the reported strength in the U.S. economy (especially in consumer durables), and improved business profitability. Exporters expect a small pickup in European markets. Several contacts express hope that interest rates will remain stable in order to sustain economic recovery.

#### Residential Real Estate

The New England residential real estate market continued showing signs of strength in the third and fourth quarters. Construction of new homes is up considerably from the previous year; builders in some parts of Massachusetts are pushing the construction season as far as weather permits. Contacts also report sizable gains in existing home sales. One respondent says the Connecticut residential market is beginning to stabilize after several years of decline. Another contact notes that the recent uptick in long-term interest rates may spur transactions in the spring because some potential buyers and sellers have been waiting for interest rates to bottom out.

#### Nonbank Financial Services

Insurance companies report a downward trend in employment. Most respondents reduced employment in 1993 or plan to do so in 1994. Contacts report that new sales of group health insurance are slow because of uncertainty over the future of health care reform. Sales of variable annuities and mutual funds, however, continue to be strong.

## SECOND DISTRICT--NEW YORK

Reports on District economic developments seemed somewhat more favorable in recent weeks. Most retail contacts reported December sales results that were above expectations, homebuilders in several areas noted an unanticipated pickup in traffic and contracts at year-end, and nonfarm employment figures showed some further improvement. Unfavorable developments included subdued office leasing activity in Manhattan in recent weeks and additional announcements of large, planned layoffs by District employers. In the banking sector, most senior loan officers at small and mid-sized banks indicated no change in their willingness to lend over the last two months.

Consumer Spending

Most District retail contacts reported December sales results that were above plan following generally lower-than-expected sales in November. After a rather unenthusiastic start to the holiday season, shoppers became more responsive towards the end of the period, and many retailers found the weeks just before and after Christmas to be the strongest of the season. The environment was very competitive, however, with additional promotions and extensive price-cutting, particularly on apparel. Several contacts remarked that shoppers were especially value-conscious this holiday season, holding back purchasing until items were discounted. As a result, profit margins are expected to have suffered.

Over-the-year sales changes ranged from -2 percent to +15 percent in November and from flat to +12 percent in December. The annual survey of the Retail Council of New York State found that sales gains throughout the state averaged 6 to 8 percent above the 1992 level for the post-Thanksgiving through the post-Christmas period. A wide variety of merchandise sold well during the months of November and December, with the

best sellers including practical items such as home furnishings, electronics and cold weather clothing. Fashion apparel seems to have fared poorly for many retailers, however.

#### Residential Construction and Real Estate

Homebuilders in several parts of the District reported an unanticipated pickup in traffic and contracts as 1993 drew to a close. Partly as a result of this, a majority of respondents now believe that 1993 housing starts in their area either equaled or were somewhat above the levels in 1992. Some builders attributed the year-end improvement to a fear, on the part of previously hesitant buyers, that a recent rise in mortgage rates might be the start of an uptrend. Others, however, said they were unable to account for the increased activity. Several contacts stated that high and rising lumber prices are a problem which could result in higher home prices in the months ahead. Nonetheless, most builders were optimistic that residential construction activity in 1994 would surpass the 1993 level, but probably by only a modest amount.

Office leasing activity in Manhattan was somewhat subdued in recent weeks, particularly in the downtown area where the primary vacancy rate rose. Leasing activity showed a modest gain in midtown, however, and the vacancy rate moved somewhat lower. While vacancy rates remain high in both mid- and downtown Manhattan, they are down in both areas by close to a percentage point from a year earlier.

#### Other Business Activity

Nonfarm employment showed some improvement in the District as both New York and New Jersey sustained irregularly higher growth since August. However, unemployment rates continued to be volatile, with both states registering increases in December following decreases in November. New York's unemployment rate now stands at 7.6 percent and New Jersey's at 7.1 percent.

With regard to the employment outlook, recent announcements have mainly been negative. Miller Brewing Company plans to close its Syracuse-area plant by October

eliminating 700 jobs in addition to 200 currently unfilled positions. The first 300 layoffs are scheduled for January. Two other District manufacturers, Xerox and Bristol-Myers, have also announced additional layoffs without any details regarding location. Xerox, whose largest manufacturing facility is in Rochester, intends to cut more than 10,000 jobs over the next three years, and Bristol-Myers, headquartered in New York City, plans a 5000 job reduction over the next two years. A positive note is that Bethlehem Steel is selling an idle, modernized mill in an arrangement that is expected to result in the recall of 250 former workers in the Buffalo area.

The November surveys of purchasing managers in Buffalo and Rochester showed little change in current conditions. A slightly smaller percentage of Buffalo managers reported increased production, while a slightly larger percentage of Rochester managers noted an improvement in business conditions. However, there was a large increase in the percentage of Rochester managers anticipating a deterioration of general business conditions over the next three months.

#### Financial Developments

Most senior loan officers surveyed at small and midsized banks in the Second District indicated that they were as willing to lend as they were two months earlier. While a few officers mentioned an increased willingness to lend, none reported easing standards, and a few reported tightening them. Lending rates were mixed with a slight upward bias. For the first time in over two years, more than one out of every four respondents reported raising rates, a larger proportion than respondents lowering rates.

The pattern of overall loan demand was mixed. The demand for commercial and industrial loans remained sluggish, while the demand for nonresidential mortgages weakened further. In addition, residential mortgage demand declined considerably, due both to seasonal factors and to a significant slowdown in refinancing activity. However, the demand for consumer loans, continued to show some signs of improvement. The majority of respondents reported either stable or lower delinquency rates during the preceding two months.

## THIRD DISTRICT - PHILADELPHIA

Reports from Third District business contacts in early January were generally positive. Manufacturers said demand for their products picked up in December and that both shipments and new orders were moving up at the beginning of January. Retailers indicated that Christmas sales ran a bit above their expectations, which had ranged around 5 percent in dollar terms on a year-over-year basis. The increases appeared to be broad-based among types of stores and varieties of merchandise. Bankers generally described loan demand as steady or slightly up, due in large part to seasonal factors, although they indicated that mortgage refinancing activity had eased significantly.

The outlook in the Third District business community is positive although not strongly optimistic, with most of those contacted for this report forecasting continued moderate improvement in 1994. Manufacturers expect to see orders grow through the first half, and they indicate they may step up hiring as the new year progresses. Retailers expect sales to increase in line with overall economic growth. Bankers believe consumer credit is on a growth trend and some noted signs of increased interest in borrowing by businesses as well.

MANUFACTURING

Manufacturing activity in the Third District continued to increase at the turn of the year, according to reports from area industrial firms in late December and early January. Around one-third of those contacted said

shipments and orders were moving up, while more than half said their shipments and orders were running at a steady pace. The increase in shipments was leading to a drop in inventories among regional manufacturers. However, the stepped-up demand was not affecting order backlogs, which were reported to be holding level by most manufacturers. A slight pickup in employment, on balance, at area plants may be attributable to the increased demand for their products.

The outlook among Third District manufacturers is generally optimistic. Among those contacted for this report, just over half expect business to improve through the first half of the year, while around one-third anticipate steady conditions, and only a few expect business to decline. Overall, area manufacturers expect orders and shipments to grow over the next six months, and they plan to hire more workers during the period.

#### RETAIL

Third District retailers generally described sales for the Christmas period as somewhat above expectations. Year-over-year gains in the range of 5 to nearly 10 percent, in dollar terms, were common among all types of stores and for a broad range of merchandise. As has been the case in recent years, the bulk of the sales came in the last week before Christmas and in the week after. While markdowns were prevalent, retailers indicated price reductions were not extensive, and most expect to show good profits for the fiscal fourth quarter (November-January).

Retailers said they believe consumer confidence is growing, but they do not forecast strong gains in spending. Looking ahead, merchants expect sales to be seasonally slow during the winter but to pick up about in line with overall economic growth in the spring.

FINANCE

Third District bankers contacted in early January noted the usual seasonal increase in total loan volume outstanding, mainly consumer credit and some business lending, but they said that mortgage refinancing activity had slowed considerably. While several bankers said seasonal patterns appeared to be dominating the recent pickup in lending, they expressed some optimism that a more basic positive trend might be taking hold. Most believe growing consumer confidence will lead to increased personal borrowing, and some cited increased interest in new or expanded credit facilities among potential business borrowers as a sign that commercial and industrial loan volume might turn up in the new year also.

## FOURTH DISTRICT - CLEVELAND

### *General Business Conditions*

The indicators of economic activity in the region remain decidedly positive. Employment, production, consumer spending, and credit demands all improved during the fourth quarter with considerable strength in the construction and industrial sectors. Capital goods producers in the District report continued strong growth in orders and production, despite softness in European markets. Although few manufacturers report plans to hire additional workers in the immediate future, many are operating at, or very near, capacity.

In Ohio, employment grew by nearly 3-1/2% in 1993, outpacing the 2% increase nationally. However, virtually all of the state's employment gains occurred during the final two months of the year. Jobs growth in Pennsylvania was a more moderate 1% last year. Unemployment in the District was just below the national rate (6.2% and 6.3% in Ohio and Pennsylvania, respectively, compared with 6.4% nationally). The jobless rates are all down about 1 percentage point from a year ago.

### *Manufacturing*

Though showing increases for three consecutive months ending in October, manufacturing production growth in Ohio continued to trail the nation for the year as a whole, rising 3.3% compared with 5.1%. Purchasing managers report rising new orders and production through November. In Cleveland, 55% stated that new orders were higher during the month, compared with 29% in Cincinnati and 33% nationally.

Virtually all of the District's major capital goods producers were reporting continued strong orders, particularly in the automotive area. However, defense-related cutbacks have been felt in the region, and export markets, particularly western Europe, have slackened considerably. The performance of the District's export markets remains an important question mark in the outlook for 1994. Nevertheless, domestic capital-goods

demand remains very strong, and most firms were thought to be operating near capacity. All of the producers we contacted noted rising backlogs.

While some manufacturers indicated little upward price pressure, most were reporting higher costs, particularly for materials such as steel scrap, and many expected planned 1994 price increases to stick.

### *Consumers*

Nonauto retail sales in the Fourth District continue to outperform the nation. Most observers say consumer attitudes were better this year than last, and consumers were more willing to use credit cards or to finance purchases.

Somewhat in contrast to the 1992 holiday season, much of the recent increase in Ohio retail activity appears to have occurred at department stores, although performance varied considerably by establishment. While discounters and off-price stores achieved small sales gains, and furniture and appliance stores did well, only specialty retailers seemed to actually lose sales on a year-over-year basis. Apparel sales here, as nationally, were noted to be particularly weak.

Retailers are still reporting thin profit margins--many reduced prices significantly prior to Christmas. Although retailers were not caught short on inventory this holiday season (as most were last year), many described stocks as merely adequate.

Retailers appear to be optimistic about consumer spending this year. Even apparel sellers believe that retail sales will likely strengthen in the first quarter.

### *Autos*

Fourth District motor vehicle dealers are considerably merrier than they were a year ago with year-end sales, profit margins, and inventory positions all reported to be improved. Although the end of the year has traditionally been slow for motor vehicle sales, many District auto dealers reported double-digit increases over 1992. The strongest postings belong to the domestic model dealers, although sales of Japanese models were also significantly higher. Dealers note that sales gains are being achieved with fewer price

discounts than in the previous few years, and many managers report that profit margins are up and that buyers are seeking more options.

Dealers cite a variety of reasons for their strong year-end performance. Most say that improved income and jobs prospects resulted in more consumer optimism than at any time since the recession. Domestic model manufacturers say that price increases on many of the 1994 models have been modest and that interest rates continue to be very favorable. Leasing is still a popular option.

### ***Banking and Credit***

Loan demands around the District were apparently rising at year's end, with virtually every major credit category showing some improvement. While refinancing activity is still high, it seems to have dropped off a bit during the last several weeks. Net new loan activity, even for mortgages, was reported to have improved.

Consumer loan demand was characterized as solid, particularly for automobiles. The overall increase in consumer borrowing furthers a strengthening pattern that became evident last summer. Commercial credit is reported to have picked up surprisingly in the fourth quarter, although some of the improvement may be a result of increased floor-plan activity due to the rise in retail sales.

## FIFTH DISTRICT-RICHMOND

### Overview

Most sectors improved further since the last Beige Book. Activity in the manufacturing, retail and wholesale trade, tourism, and real estate industries grew. Loan demand was mixed, and exports declined at District ports. Worse-than-normal weather impeded agricultural activity.

### Manufacturing

Our regular mail survey of manufacturers indicated that District factory activity continued to strengthen in December, following improvements reported in our two previous surveys. Manufacturers saw increases in shipments, new orders, and exports. Order backlogs and employment changed little, while raw materials inventories declined. Raw materials prices rose faster than finished goods prices, but both rose by less than recent general inflation rates.

Most manufacturers expected shipments and exports to increase and raw materials inventories to remain unchanged over the next six months. They expected employee hours to increase somewhat, employment to remain the same, and the recent modest price increases to continue.

### Retailers and Wholesalers

Our survey of retailers and wholesalers indicated very strong revenue growth in

December. All other indicators grew, including employment and seasonally adjusted sales of big-ticket items. Respondents reported that their prices rose by less than the general inflation rate; they did not expect their price increases to exceed that inflation rate during the next six months. Demand for retail and wholesale services was expected to rise in the same period.

### Ports

Representatives at District ports--Baltimore, Charleston, and Hampton Roads (Norfolk)--indicated that on average, exports and imports were unchanged from November to December. Compared with a year ago, imports and exports were generally unchanged. All three ports expected exports to increase faster than imports during the next six months.

### Tourism

Hotels, motels, and resorts throughout the District indicated that tourism was higher in December than in November and a year ago. Respondents attributed the improvement to increased popularity of vacation packages and growing consumer confidence. Almost all respondents noted that their bookings this winter were higher than last winter's, and all expected tourist activity to continue to improve during the next six months.

### Finance

District financial institutions indicated that credit conditions were mixed during the last six weeks. Respondents stated that commercial loan demand was moderately higher, while consumer loan demand was unchanged. Commercial and consumer loan rates were steady. Residential mortgage demand fell during the last six weeks; mortgage originations were off slightly, and refinancing activity was sharply lower. Residential mortgage lending rates were up slightly.

### Residential Real Estate

Real estate agents and homebuilders reported that seasonally adjusted residential real estate activity strengthened throughout most of the District in November. Most respondents indicated moderate to strong growth in home sales and housing starts. Home prices apparently changed little during the period, but most homebuilders reported that lumber costs continued to increase significantly. Several homebuilders reported increases in the cost of wallboard and other building materials.

### Commercial Real Estate

Commercial real estate analysts reported that leasing activity improved in most of the District during December because of stronger consumer confidence and job growth. Vacancy rates declined in all areas, and some landlords raised rents, either directly or through reduced concessions. Some businesses began construction of facilities they had previously delayed; however, very little speculative activity was reported. While activity was growing in Maryland and the D.C. suburbs, some analysts were cautious about the sustainability of that growth.

### Agriculture

Below-normal temperatures and above-normal precipitation in recent weeks hampered District agricultural activity somewhat. Weather conditions delayed late fall and early winter sowing of small grains across much of the District. Ranging livestock were subjected to stress from the weather, and cattle producers in the western part of the District expressed concern over survival rates during the winter calving season. Above-normal snowfall was expected to reduce hay stocks, already low because of last summer's severe drought.

## SIXTH DISTRICT - ATLANTA

Overview: Sixth District contacts reported that growth in economic activity in the Southeast accelerated moderately in December and early January. Merchants were generally pleased with holiday sales, especially for durable goods, although some types of apparel sales were flat, and retailers are cautiously stocking for spring. Auto dealers continued to report strong year-over-year sales gains. New orders and production increased moderately for District manufacturers, and most factory contacts expect further near-term improvement. Home builders and realtors reported increasing activity and anticipate a busy spring; commercial real estate is also slowly improving. Consumer loan demand is continuing to grow modestly throughout the region, according to bank contacts. There were scattered reports of increased wage pressures at this time and with few exceptions contacts noted stable prices.

Consumer Spending: Retailers around the District reported generally stronger-than-expected holiday sales, although many contacts said that improvements were due in large part to deep discounting, and those specializing in women's apparel reported clothing sales were flat-to-only-slightly improved over last year. Home furnishings, furniture, and home electronics sales continue to benefit from the strong single-family housing market. Many contacts noted that post-holiday sales have also been good, and several stated that this could lead to healthy spring sales. Nonetheless, most retailers stated they are keeping their inventories for spring merchandise lean until they better assess interest in the new spring lines.

Reports from the tourism and recreation industries suggest that bookings from domestic and South American tourists are up, while those from Europe are lower. Winter travel to Miami is said to have fallen this year because of reports of crime; however, activity north of the city is reported to be a bit stronger than normal. Casinos and riverboat gambling continue to stimulate tourist activity in Mississippi and now in Louisiana.

**Manufacturing:** The District's manufacturers continue to report expansion in December, and most factory contacts were more optimistic than before about future prospects. Nonapparel textile products, such as carpet and home furnishings, continue to report strength coming from residential home sales and refurbishing. Building materials producers as well as furniture and fixture producers also note an increasing volume of new orders for both residential and commercial construction. Business hookups for telecommunications firms are reportedly ahead of plan. Regional capital equipment producers note a recent upsurge in optimism about future orders because of improving economic conditions and they expect to expand capacity.

In contrast, the region's apparel producers continue to report strong foreign competition and soft demand resulting in further employee cutbacks and a shrinking factory workweek. Firms that rely on defense spending continue to downsize, although contacts expect defense conversion to civilian production to help stabilize employment rolls for some of the affected District manufacturers.

**Construction:** Realtors from across the District reported strong end-of-year home sales. Most contacts stated that December sales outpaced year-ago levels by a large margin. Many noted that homes are selling much faster than in the recent past, and in some areas contract prices are rising. Demand for new homes remains strong, and home builders continue to report increased construction in anticipation of a busy spring selling season. However, many builders noted that a short supply of subcontractors has pushed up wages. Real estate agents and builders are optimistic that home sales in 1994 will at least equal, and in many areas surpass, the levels achieved in 1993.

Commercial and multifamily real estate contacts said that market conditions are improving. While build-to-suit and retail projects continue to provide most new construction, slowly falling vacancy rates for office and industrial space have helped effective rental rates

improve. In addition, several contacts reported that large blocks of space are becoming difficult to find in the most desirable areas, and that some speculative building may be possible in these areas by the first quarter of 1995.

Financial Services: Bankers around the region reported that loan demand was up modestly in late November and December. The majority reported increased consumer demand, many citing auto lending as the strongest area. Residential mortgage lending continued on a torrid pace as the recent uptick in rates and the end of the calendar year caused a flurry of closings in December. Activity has calmed since, but is expected to pick up again at the end of the quarter. Commercial loan demand was spottier, reported as flat in some areas, and up moderately in others.

Wages and Prices: There were minor reports of increased wage pressures in December. Although most manufacturers continue to report that prices for finished products and raw materials have remained unchanged, producers of building products as well as some realtors note recently increasing prices.

large chain that reported relatively strong holiday sales gains stated that sales growth strengthened, if anything, in late December and early January. Another large chain reported that sales growth increased significantly in early January, with sales gains in the District running in line with the national average. Bigger-ticket items (including housewares and electronics) continued to lead overall sales, and hard-line inventories were running below plan for the first time in several months. This contact noted that post-holiday season promotional activity was somewhat stronger than last year, but did not express a great deal of concern in light of the surprisingly strong sales pace in the holiday season for 1992. Retail prices continue to rise slowly at best, and most firms indicated that competitive pressures on margins were little changed, including those that enjoyed relatively successful seasons. With the dramatic exception of Rose Bowl items sold in Wisconsin, reports generally indicated that apparel sales remained relatively weak. One department store chain stated that a shift in sales mix would constrain its overall margin relative to last year, but consumers seem to have extended their purchases beyond the basics within low-margin categories to a greater extent than they did in the 1992 holiday season.

**Manufacturing.** Purchasing managers' surveys and reports from District contacts generally indicated moderate to relatively robust gains in manufacturing activity. The overall index for the Chicago purchasing managers' survey flattened out in December, but for the fourth quarter the index average was at its highest level since 1988. Surveys conducted in Western Michigan indicated that growth in December proceeded in line with--or perhaps slightly faster than--the significant pace experienced in October and November. The price component of these surveys offered scant evidence of significant price pressures overall, although expectations firmed that announced steel price increases would hold, and several respondents reported that finding qualified production workers and tradespeople was becoming increasingly difficult. The prices-paid component of the Chicago survey actually declined during the second half of 1993, falling well below year-earlier levels. The overall index for the Detroit purchasing managers' survey strengthened significantly in December (from already high levels), and supply shortages and price pressures were reported somewhat more frequently in this survey than in others around the District.

## SEVENTH DISTRICT--CHICAGO

**Summary.** Economic expansion in the Seventh District continued to run at about the same pace as the fourth quarter as a whole, while firms' and households' confidence in future growth improved. District retailers generally enjoyed moderate sales gains in the holiday season, with most reports indicating sales gains in line with expectations. Retail sales growth in the District seems to have proceeded somewhat faster than in the nation as a whole, and several large retailers reported unchanged to somewhat stronger sales gains in early January. Manufacturing activity continued to expand at a relatively robust pace, led by auto production. Corn and soybean prices rose sharply in recent weeks, reflecting expectations that harvest estimates will be revised downward even further. The consensus forecast of 33 Midwest economists called for real GDP growth to run at about the same pace in 1994 as in 1993, with continued above-average growth in most durable goods sectors where Midwest production is relatively concentrated.

**Retail Sales.** Retail sales generally grew at a moderate pace in the holiday season that was in line with District retailers' expectations, and several large chains stated that their sales growth was little changed or somewhat stronger in the post-holiday period on a seasonally adjusted basis. A number of surveys prior to the holiday indicated that District retailers expected somewhat stronger gains than the national average, and post-holiday results did point to relative strength in sales growth in the region. A review of credit card purchases by a retailers' association in Michigan indicated that credit sales rose over 14 percent from 1992 for surveyed firms on a same-store basis. A study by a check authorization firm indicated similar growth in sales paid with checks, which ranged from 6 to 15 percent among District states. This study indicated that sales growth in the region exceeded the national average, and strengthened late in the holiday season. A group of retailers in Central Michigan reported same-store sales gains averaging roughly 7 percent over a surprisingly strong year-earlier period, although results were somewhat below the optimistic end of expectations. An association of restaurants in the District reported that its members enjoyed robust sales gains during the holiday season.

Discussions with individual retail firms were largely consistent with the picture painted by survey data, and several large retailers indicated that moderate sales growth continued in early January. One

Reports from individual manufacturing firms generally reflected a rising note of optimism about prospects in the new year, although growth was expected to moderate in several durable goods markets following strong gains in 1993. A large steelmaker noted that space on order books is on an allocation basis into the second quarter of 1994, and the auto industry remained its strongest market. A machine tool manufacturer reported continuing strength in orders from automakers and their suppliers, but stated that overall industry orders growth should slow somewhat in 1994 after a strong year in 1993. Pricing and margins remain under considerable pressure from European and Japanese machine tool producers with underutilized capacity. Heavy-duty truck orders strengthened further, according to an industry analyst. This contact stated that many industry suppliers are "stretched to their limits." A manufacturer of fluid power equipment expected further gains in output of construction machinery and other forms of heavy equipment.

**Agriculture.** Corn and soybean prices have risen sharply in recent weeks, reflecting analyst's expectations that the final estimates of the 1993 harvest will show further downward revisions. A near 20 percent rise since early November has pushed corn prices to the highest levels in ten years, reaching levels roughly 40 percent higher than a year ago. The higher prices are helping to buoy the earnings of crop farmers who were able to avoid the brunt of the flood losses last summer. Alternatively, the higher crop prices translate into sharply higher feed costs for livestock and dairy farmers. The latter is apparently contributing to a downturn in livestock production, at least in District states. Similarly, milk production on dairy farms in the District in recent months has lagged year-earlier levels by nearly 6.5 percent.

**Expectations for 1994.** The consensus forecast of 33 economists attending the Chicago Fed's annual economic outlook conference called for real GDP to grow 2.9 percent on a year-over-year basis in 1994, with little change in the inflation rate (as measured by the CPI) and only a negligible increase in the prime rate. Business fixed investment was anticipated to continue to rise faster than overall GDP, but growth was still expected to slow somewhat from its robust pace in 1993.

## VIII-1

### EIGHTH DISTRICT - ST. LOUIS

#### **Summary**

District economic activity continues to pick up, as many firms report increases in sales and employment. District retailers report good-to-strong sales of most types of merchandise during the holiday and post-holiday period. Unseasonably strong single-family home construction is providing a boost to the regional economy. Bank loans continue to increase at a sample of large District banks. District rice producers have been buoyed by an order from Japan and continued strong prices.

#### **Consumer Spending**

Preliminary reports suggest that sales during the 1993 holiday and post-holiday periods were strong. Although double-digit sales growth was reported in isolated cases, the majority of respondents estimated a 4 percent to 6 percent increase over the 1992 holiday season. Many respondents cited increased advertising and a growing economy as reasons for strong sales levels. Deep discounting has generally not been necessary to move merchandise. In most cases, inventories are at (expected) low levels.

Contacts indicate that furniture and household goods, including appliances and towels, were the best sellers this holiday season. Sales of toys and consumer electronics were also strong. Women's apparel and shoes, usually a strong source of holiday sales, did not do as well as expected. Most retailers are anticipating a solid 1994, with some predicting as much as 10 percent sales growth in the first half of the year. Similarly, most auto dealers contacted are expecting 1994 to equal or surpass 1993's strong year.

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

A number of District firms report increases in sales and employment, continuing the growth from last quarter. A refrigerator manufacturer and a maker of bathroom fixtures both report strong sales, driven primarily by increased housing starts; replacement

of older equipment also contributed. A poultry processor plans to add more than 250 jobs when it expands a hatchery and processing plant to increase production 33 percent. In Arkansas, new chrome plating and food processing plants have led to 300 new jobs, while a Mississippi maker of construction materials broke ground for a new plant that will employ 150 workers by the end of the year. An airline with a District hub will overhaul its operations and add about 300 ground workers. The six-month-old United Mine Workers of America strike has ended, returning about 3,000 to their District jobs.

A few minor setbacks were also reported, some of which had been anticipated. For example, an auto plant closed on schedule in December, eliminating the remaining 1,200 jobs. A bakery that was displaced by airport expansion dismissed 525 workers when it finally closed its doors, another anticipated closure. An auto parts maker will close its plant early this year, laying off more than 260 workers. A defense contractor let another 200 workers go after the cancellation of a program.

A national temporary employment agency's recent survey of the St. Louis area reveals that 12 percent of the firms plan to hire during the first quarter of 1994. This is down from 20 percent one year ago. Nationally, 18 percent plan to hire this quarter. According to a recent survey of District firms by the National Federation of Independent Businesses, 14 percent think now is a good time to expand. However, 23 percent of the surveyed firms increased their average selling price between August and November, while just 10 percent reduced prices. About 24 percent plan to increase prices during the first quarter of 1994 (4 percent will decrease prices), and 35 percent plan to increase capital expenditures. More than half of the respondents felt current inventories were at acceptable levels, but only 43 percent will keep them at the same level during the first half of the year. The remaining 57 percent are split between increasing or decreasing their inventories.

**Construction and Real Estate**

Single-family homebuilding is unseasonably strong in many parts of the District, as builders scramble to start and finish projects that were delayed in the latter half of 1993 because of wet weather. Multifamily housing construction, after several years of stagnating, also appears to be on the upswing as apartment occupancy rates and rental prices edge up. Sales of new and existing homes have been relatively strong in the District lately, as they have been nationally, and average selling prices continue to rise.

**Banking and Finance**

Total loans on the books of 11 large District banks rose 1.7 percent during the last two months of 1993 after a 0.1 percent increase in the prior two-month period. All three major categories of loans—commercial, consumer and real estate—registered positive growth rates in the November-through-December period. Consumer and real estate loans posted stronger growth rates in the last two months of 1993 than they did during the same period of 1992.

**Agriculture and Natural Resources**

A major processor of rice and rice products recently announced its first-ever shipment of rice to Japan because of that country's poor harvest; the company expects to make additional sales this year. Contacts in the rice industry expect a 10 percent to 15 percent increase in planted acreage this spring because of recent strong prices and a reduction in government set-aside requirements. Crop prices have risen sharply in most District states recently, while livestock prices have retreated slightly. Increased domestic and foreign demand for cottonseed oil continues to bolster processor profit margins, which have tripled in the last few months. A contact in the coal industry reports that prices are expected to soften with the end of the coal strike. Through mid-December, coal production was running ahead of last year's pace in western Kentucky and Indiana, but behind in other District states.

and South Dakota. Manufacturers of builders' hardware, residential heating equipment controls and other construction-related products report excellent sales. Responding to continuing high demand for building materials, a Canadian firm reportedly plans to establish a building-board plant in North Dakota that will use wheat straw and other crop residues as raw material.

#### Natural resource industries

Refinery output in December was up from year-earlier levels, largely due to 1993 capacity expansions in Minnesota and Montana. Crude petroleum production was marginally below year-earlier levels, reflecting aging of producing wells, and drilling activity was essentially unchanged.

Production of oriented-strand board and other wood-based plywood and lumber substitutes is very strong in Minnesota, Wisconsin and Michigan. But the forest products industry's outlook continues to vary by product and location. A recent timber sale in Montana set a record for stumpage prices in that state, reflecting generally declining quantities of timber offered for sale. The paper industry continues to experience overcapacity and low prices, but output is essentially stable.

"Mine operators are generally optimistic about 1994 and expect output to exceed levels of the previous three years," said one iron ore industry spokesperson. This is in spite of a slight output decline in 1993 relative to 1992, largely related to a strike-related closing of one mine. Other mining is essentially stable. Copper and gold output is unchanged from earlier in the year. Copper prices have recovered slightly from lows set earlier in the year, allaying fears of possible mine closings.

#### Agriculture

Agriculture showed little change in the final weeks of 1993. Grain prices were generally high, reflecting low stocks due to adverse growing conditions earlier in the year. Fall tillage in corn and soybean growing areas was completed at near normal levels prior to freeze-up, in spite of wet conditions earlier in the year. In northwestern Minnesota and eastern North Dakota, though, these tillage operations lagged considerably, which may retard spring 1994 planting operations. Cattle, hog and sheep slaughter numbers are essentially the same as a year ago, while prices continue to trend slightly downward. While prices for feeder cattle have declined somewhat from earlier in 1993, they remain high relative to other recent years, apparently reflecting confidence in farmer and feeder expectations of continued profitability.

**NINTH DISTRICT--MINNEAPOLIS**

As 1993 ended, most economic sectors in the Ninth Federal Reserve District showed signs of growth. Commercial and residential construction is very active in virtually all areas of the district. Manufacturing, particularly in small and midsize firms, continues to grow. Refinery production is up, demand for construction-related forest products remains high and prospects for iron mining are positive. Conditions are unchanged in agriculture, which ended 1993 with much lower grain stocks than a year earlier and essentially stable livestock output. Consumer spending through the holiday season continued improving at the pace set earlier in the fall. After a slow start, winter recreation enterprises report good business. Unemployment rates remain substantially below those of the United States as a whole and employment is up from year-earlier levels. There is little evidence of upward pressure on wages or prices.

**Construction and housing**

One city building inspector in Minnesota characterized 1993 as "a year that is nothing short of phenomenal." Construction was the strongest sector of the economy across the Ninth District throughout 1993, with no apparent slackening as the year ended. News media, district directors and other sources reported continued strong residential construction across the district and active commercial building in many areas. Residential construction is booming in western Montana, Sioux Falls, S.D., and Rapid City, S. D. 1993 was also a record year for construction in Fargo, N. D., and Moorhead, Minn. Construction of new retail facilities continued in the Upper Peninsula of Michigan. Publicly bid commercial and heavy construction in Minnesota and the Dakotas for the year through November was 12 percent ahead of year-earlier levels.

**Manufacturing**

Manufacturing continues to grow. "Many firms reported strong third-quarter growth and the fourth quarter was even better," said one director, speaking of manufacturers in the Minneapolis-St. Paul area. He also noted that most manufacturing firms were now running at 85 percent of capacity, up substantially from a year ago and that small and medium firms had the most growth in orders. Moreover, a director from South Dakota reported an increase in the establishment of small and midsize manufacturing facilities in that state. Growth in industrial electricity use continues above the five-year trend rate in Minnesota

Consumer spending and tourism

Reports from a broad range of sources including directors, advisory council members, news media, mall managers, vehicle dealers associations and company representatives reaffirmed earlier reports that consumer confidence has rebounded from earlier in 1993 and that consumer spending is growing. In late 1993, passenger vehicle sales were strong across the district and several sources noted that pickups and sport utility vehicle sales were particularly strong. Retail reports on holiday season sales of general merchandise are largely positive. The manager at a large Minneapolis-area mall reported very strong sales as did counterparts in Sioux Falls, S. D., and in Grand Forks and Fargo, N. D. And a director from Montana reported that holiday season sales in that state were very good and generally well above 1992 levels. But a few firms reported a disappointing holiday season; one major retailer had December department store sales that were essentially flat from a year earlier.

In the closing weeks of 1993 the winter tourism and recreation season picked up momentum, particularly in Montana. Lack of snow in several ski areas had retarded activity in November and early December, but snowfalls just before Christmas improved business considerably. Ski resorts in Montana report strong holiday seasons that helped recovery from the slow start, although decreased traffic from Canada continues to hamper resorts near the border. One source reported that snowmobile rental companies at Bozeman, Mont., and near Yellowstone National Park were booked through March. Snowmobilers and skiers were traveling to the Upper Peninsula of Michigan and northern Wisconsin at slightly higher than year-earlier rates at the end of December and in early January. Tourist traffic to the Black Hills was steady in South Dakota.

Employment, prices and wages

With unemployment rates below 4.5 percent in Minnesota and the Dakotas, Ninth District labor markets continue substantially better than the national average. These three states contain over 80 percent of the Ninth District labor force. In November, employment numbers in all district states stood 1 percent to 3 percent above year-earlier levels.

Directors, industry sources and news media report virtually no upward price movements except for those grains where 1993 production was curtailed by flooding. In the last weeks of 1993, retail gasoline prices stood 5 to 7 cents below 1992 levels in Minneapolis-St. Paul and even sharper drops were reported in some other areas. District and branch directors report very limited wage increases for both private and public sector workers, in some cases limited to maintenance of health insurance coverage in the face of premium increases.

## TENTH DISTRICT - KANSAS CITY

Overview. The Tenth District economy is still growing moderately. Housing activity and retail sales are both increasing and loan demand at commercial banks is generally rising. Farm income is flat, however, and activity in the energy sector is slowing. Prices for both retail goods and manufacturers' inputs are holding fairly steady.

Retail Sales. Most district retailers report sales are moderately higher than a year ago, as Christmas buying generally met or exceeded expectations. Merchandise categories with especially strong sales included home furnishings and appliances, apparel, and jewelry. Sales are expected to continue to rise at a moderate pace. Most retailers, satisfied with current inventory levels, expect to maintain stocks in line with sales after normal post-holiday adjustments. Retail prices remain generally flat and little change is expected in the months ahead as competition keeps prices in check.

Reports on last month's automobile sales are mixed, but dealers are generally optimistic about 1994 sales. Some dealers are still expanding new car inventories, while others are satisfied with current stocks.

Manufacturing. Purchasing agents report a mixture of changes in input prices, with some prices rising modestly and others falling slightly. Few expect prices to rise in the near term. Most agents find materials readily available and expect few availability problems in the months ahead, although some lead times have lengthened slightly. A few firms continue to trim inventories, but most are satisfied with their inventory levels. Most respondents who sell abroad report somewhat higher export sales.

Energy. Activity in the district energy sector slowed recently as oil prices continued to fall. The price of West Texas intermediate crude

fell in December to its lowest level in nearly five years. Overall, the average number of operating rigs in district states slipped to 292 in November from 294 in October. The rig count continued to fall in the first four weeks of December to 283, off about 14 percent from one year ago.

Housing. Housing starts and sales of new homes in most areas of the district remain significantly higher than a year ago. Most builders also report increases in the last month but note slower growth, which they attribute partly to increased lumber prices and a lack of skilled labor. In the period ahead they expect further increases in starts and sales of new houses along with higher prices for new homes. Inventories of unsold homes remain very low. Mortgage demand is reported to be mixed, with most respondents expecting seasonal factors to be most important in the near term. While respondents generally report modest increases in mortgage rates, there is no consensus on how rates will behave in the near future.

Banking. Loan demand was higher last month at almost all reporting banks. Most respondents report increased demand for consumer, residential construction, agricultural, and commercial and industrial loans, and for home mortgages. Demand was generally constant to higher for home equity and commercial real estate loans. Loan-deposit ratios increased at more than half the banks and remained unchanged at the rest. Investments were mostly unchanged from the previous month.

No respondents changed their prime rate last month and none expect to do so in the near term. A few banks trimmed their consumer lending rates, but most left them unchanged. One bank eased its lending standards while the rest reported no change.

Deposits increased last month at most reporting banks and were unchanged at the others. Demand deposits and NOW accounts were up at almost all banks. Money market deposit accounts and small time and savings deposits were constant to up at most banks. Large CDs were mixed, with about half of the respondents reporting increases and half reporting decreases.

Agriculture. District agricultural bankers view farm prospects for 1994 as mixed. Higher crop prices will bolster incomes for district crop producers. But the higher crop prices will push up feed costs and squeeze profit margins for district livestock producers. Overall, the bankers expect little change in district farm income in the year ahead.

Most district farmers and ranchers enter 1994 in solid financial condition, according to district agricultural bankers. Despite large crop losses caused by last year's wet weather and flooding in the eastern part of the district, the bankers note only slight slippage in the quality of their farm loan portfolios. The bankers plan to deny credit to very few of their current farm borrowers in 1994.

Despite the outlook for flat farm income, most small business owners in district rural communities are optimistic about their prospects in the coming year. Sales during the recent holiday season were generally above normal. As a result, many rural businesses enjoyed improved sales in 1993, and they expect stronger sales in 1994.

## ELEVENTH DISTRICT--DALLAS

The Eleventh District economy expanded in December. Manufacturers reported growth in orders, particularly for construction-related goods and computer-related electronics. Energy-related manufacturing was boosted by strong international drilling and a strengthening domestic economy. Residential construction exceeded expectations while commercial construction increased across much of the District. Business service firms reported increased activity and retail sales continued to expand. Bankers reported a pick up in loan growth and optimism. Drilling continued to slow as real oil prices fell to 1973 levels. Dry weather weakened agricultural conditions across most of the District.

District manufacturers reported continued growth in orders. Demand for construction-related products and computer-related electronics remained strong while energy-related manufacturing increased. Demand for brick, glass and cement continued to be strong and contacts said they had increased their prices. Brick producers reported that they were hiring additional workers. Sales of lumber for residential construction was strong while lumber sales for industrial construction picked up. Lumber prices had increased. Primary and fabricated metal producers reported that sales were much higher than this time last year. Substantial international drilling boosted demand for oil services and machinery, while a strengthening domestic economy increased demand for refined products and petrochemicals. Lower oil prices reduced costs for these industries but continued overcapacity pushed prices and margins down. Sales of electrical and electronic machinery remained strong particularly for personal

computers, communications equipment and construction-related equipment. Several electronics contacts reported recent hiring for new facilities. Demand for paper products was up slightly. Apparel manufacturing slowed but remained above a year ago. Sales of food and kindred products increased.

Business service firms reported increased activity. Demand was particularly strong for temporary services and contacts said they had increased their prices. All other service contacts, however, reported that heavy competition was forcing their prices to remain unchanged. Costs had held steady at most firms and some companies reported that they are getting ready to hire additional experienced workers.

Retail sales continued to expand. Retailers said that holiday sales met their expectations but were not outstanding. Sales of women's apparel was reported to be particularly slow, however. Heavy discounting kept prices at or below last year's level. Retailers said that consumers were very value oriented and merchandise was discounted earlier than last Christmas. As a result, stores were not left with excess inventory. A few retailers reported that they may have over-discounted because their inventories fell below desired levels. Auto dealers reported steady sales gains. A recent increase in the price of new cars had combined with a shortage of used vehicles to boost used car and truck prices.

Construction activity had increased. Single family homebuilding remained strong and contacts said that 1993 had exceeded expectations. Commercial construction expanded across much of the District, with strong demand for large discount retail stores and retail "power centers". Industrial construction also increased. Shortages of concrete, fiberglass insulation, and

gypsum wallboard were reported to have slowed construction in some markets. Houston and Dallas office markets remained weak.

Drilling declined with lower oil and natural gas prices. The Baker-Hughes rig count for the United States ended 1993 at 814 working rigs, well below the 883 working rigs at the end of 1992, and below expected seasonal increases. Weak global demand and large supplies pushed down real oil prices to 1973 levels. Natural gas prices also fell, with the February futures contract below \$2.00 per thousand cubic feet. Contacts said that they do not know whether current price levels will hold.

District bankers reported a pick up in loan growth and optimism. Lending for housing construction remained strong while contacts reported an increase in consumer and commercial loan demand. Demand for loans is reported to have increased mostly from established customers, with many companies using existing lines of credit. Bankers reported intense competition for consumer loans from retailers and captive finance companies. Most contacts said they are hoping to accommodate loan growth without additional hiring.

Dry weather had weakened agricultural conditions across most of the District. Contacts reported that insufficient moisture had damaged pastures, the winter wheat crop and contributed to a shortage of hay. Supplemental feeding of livestock was above normal and some producers had culled their herds earlier than usual. The Texas cattle on feed inventory continued to reach record high levels. Higher prices for all major crops more than offset declines in major livestock items causing the Texas All Farm Products Index of Prices Received to increase 3 percent above December 1992.

TWELFTH DISTRICT -- SAN FRANCISCO

Summary

Economic weakness persists in California, particularly in the southern part of the state, but much of the rest of the Twelfth District shows signs of solid economic growth. Weakness in manufacturing, construction, and real estate markets continues to drag down the Los Angeles area economy, while other regions of California are showing signs of bottoming out or of modest improvement. Economic activity also lags in western Washington, reflecting retrenchment in aerospace, and in Hawaii, reflecting a weak visitor industry. Oregon and Arizona, however, are experiencing solid growth across several sectors. Furthermore, the economies of intermountain states continue to boom. Business sentiment is strong, and holiday retail sales were reported good in most markets.

Business Sentiment

Sentiment among Twelfth District business leaders has improved significantly in recent months. Almost all 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 up from three-quarters in November, two-thirds in October, and one-half in August. Furthermore, it is the highest such proportion in the six-year history of this survey. Respondents from California and western Washington, however, expect their regions to have slower growth relative to the nation.

Retail Trade and Services

Retail activity is reported generally strong, with contacts in most District markets reporting good retail sales for the Holiday season. In Utah and Idaho, retail sales were reported nearly 10 percent above their year-earlier level. Sales of automobiles and household durables associated with new-home purchases accounted for much of this increase. A contact in Oregon reports that sales

were 6 to 8 percent above a year earlier, with major strength in appliances and housing-related expenditures and relative weakness in apparel spending. In the Puget Sound area, retail sales were reported generally good. In the California central valley, a contact reports stronger sales than a year earlier--and also strong post-holiday sales. In the Los Angeles area, retailers were reported to be generally pleased with holiday sales, but the sales peak was late this year as customers waited for price discounts. Post-holiday sales were reported particularly strong. San Diego retailers reported good holiday sales stimulated by advertising and discounting. Another contact, however, reports that sales in southern California were worse than in northern California, reflecting the divergence in overall economic conditions.

Conditions in service-related industries are mixed. A contact in the newspaper industry reports that advertising activity was disappointing in 1993, but showed an increase in both volume and revenue during the fourth quarter. The southern California visitor industry is reported in the doldrums. Hotel occupancy in the region was very weak in the fourth quarter, and while bookings for early 1994 are above a year earlier, it is uncertain whether actual occupancy rates will improve. Hotel occupancy also is reported to be still dropping in Hawaii.

### Manufacturing

Manufacturing activity is mixed in the District, with lingering weakness centered in aerospace and defense-related industries. Layoffs in these sectors continue in several District states--with southern California and western Washington most affected. Aircraft-quality aluminum continues to be sold at substantially discounted prices, with both raw material and fabricated products prices reported soft. In contrast, the electronics industry in Oregon is reported to be performing well. A contact in the electronics industry reports that spending on personal computers and network peripherals continues to grow rapidly. A contact in the California telecommunications industry reports a slight gain in both usage and new business in the fourth quarter, but that gain is still well below what is

typical of a recovery.

Capital spending plans are reported generally cautious in most industries. Commercial lenders in Oregon report that, with the exception of the high technology industry, the general sentiment is one of caution for capital spending in 1994, with the level planned at or slightly above the 1993 level. A contact in the auto dealer industry, however, reports that low interest rates are having a beneficial effect on capital expenditures.

#### Agriculture and Resource-Related Industries

Most contacts report a generally favorable outlook for agriculture. Average farm prices are below year-earlier levels due primarily to lower prices for beef and wheat. Production of potatoes is reported to be down in Idaho. However, Washington and Oregon contacts report strong potato production. Midwest weather conditions were reported to create unusually strong markets for the frozen vegetable industry in the Pacific Northwest during the fourth quarter of 1993. Another contact, however, projects continued weak conditions in the seafood industry with both demand and prices decreasing. Several contacts report that agricultural exporters are pleased with the passage of NAFTA and the successful conclusion of the GATT negotiations.

#### Construction and Real Estate

District construction and real estate markets are mixed. Weak conditions are reported in southern California, both in residential and nonresidential markets. A contact in northern California reports that commercial real estate is still weak, with office rents expected to remain low for several years, and virtually no transactions in the transfer of office properties. In contrast, contacts in Idaho report continued strong housing construction as growth in jobs and population has resulted in vigorous demand for housing. Several contacts report shortages of skilled construction labor.

Financial Institutions

Varied conditions are reported across District financial markets. In California, a contact reports that the banking industry continues to show signs of modest improvement, including stronger asset quality and a slight pickup in loan demand. Much of the improvement, however, has come from large banks. Small and medium-sized institutions remain under pressure, showing less improvement in asset quality and greater exposure to real estate loans. A contact from the Puget Sound area reports somewhat weaker loan demand and increasing price competition for commercial and industrial loans and also for mortgage loans. Vigorous rate competition for loans also is reported by contacts in Utah.