

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

June 1994

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SUMMARY¹

Districts report continued economic expansion, although in some areas growth has moderated recently. Contacts in a number of districts report slower-than-expected growth in May retail sales but some signs of increasing sales in early June. Manufacturing continued to show strength in most districts, with many contacts reporting increases in new orders and shipments. Defense-related industries, however, continue to be the weak spots. Home sales in most areas continued at a strong pace, and residential construction remains generally brisk, but some slowdowns in response to rising mortgage rates were noted. Industrial materials prices continue to rise; however, competitive pressures are mitigating price increases for finished goods. Some districts report tightening labor markets, but wage pressures appear moderate at this point. Loan demand is generally increasing, although rising interest rates have precipitated declines in some areas. Crop conditions are generally favorable in most agricultural areas; nevertheless, some districts are expressing rising concern over warm, dry weather.

Consumer Spending

Most districts report moderate gains in retail sales, although contacts in the Atlanta, Cleveland, Dallas, New York and Philadelphia districts report slower-than-expected sales. In particular, they cite declines in apparel sales and attribute this to unseasonably cool weather. Sales activity in the Boston district varied from slight declines to increases of almost 20 percent over last year, with strong demand for outdoor-related items since Memorial Day. The Kansas City, Minneapolis and St. Louis districts report moderate-to-strong sales in general merchandise, particularly in apparel. The Chicago, New York, Philadelphia, Richmond and San Francisco districts report strong sales in household goods and furniture, and strength in consumer durables and other big-ticket items. The Atlanta,

¹Prepared at the Federal Reserve Bank of St. Louis from information collected before June 14, 1994. This document summarizes comments received from businesses and other contacts outside the Federal Reserve and is not a commentary on the views of Federal Reserve officials.

Cleveland and New York districts found that discounting was needed to move merchandise; the Chicago, Dallas and Kansas City districts note that strong competition is keeping prices in line. The Kansas City, Minneapolis, Philadelphia, St. Louis and San Francisco districts report strong auto sales; the Chicago, Cleveland and Dallas districts report some recent slowing in auto sales. A number of districts report that a shortage of popular models is constraining sales.

Business Activity

Most districts report continued growth, particularly at manufacturing firms, although the San Francisco district has mixed reports from its contacts. The Chicago and St. Louis districts report strong growth, while the Boston, Cleveland, Minneapolis, New York and Richmond districts report accelerating activity. The Atlanta district reports a rebound of industrial production in May after a modest slowing in April. Machinery and heavy equipment orders and production are up in the Boston, Chicago, Dallas, Philadelphia and St. Louis districts. The San Francisco district says the aerospace industry, especially commercial jets, has stabilized, but this industry is weak in the Boston district. Business contacts in the St. Louis district report sales increases of between 10 percent and 20 percent in some instances. The Atlanta district reports that the demand for building materials in the Southeast is up recently, and that auto suppliers are receiving a steady stream of new orders. The New York district says that its manufacturing contacts are more optimistic than a year ago. A survey of contacts in the Philadelphia and Richmond districts revealed increases in new orders and shipments. The Dallas and Richmond districts also report a steady-to-moderate increase in demand in the service sector, particularly at law firms, hotels and cargo carriers.

Contacts in parts of the Kansas City, Minneapolis and St. Louis districts are having difficulty finding qualified employees. The St. Louis and San Francisco districts both report a shortage of skilled construction workers. Contacts in the New York district anticipate few employment cuts and see wage increases of between 2 percent and 4

percent. Contacts in the Richmond district plan no employment changes, but do expect to increase the average length of the workweek.

Foreign demand for products from most districts remains somewhat sluggish. The Dallas and St. Louis districts, however, report some strengthening demand from Latin America and the Pacific Rim countries, respectively. In addition, the Dallas district reports strong chemical sales to Europe. The Kansas City district reports that exports are stable overall.

Both the Atlanta and St. Louis districts report defense-related layoffs; the San Francisco district reports its defense-related industries remain weak. The Boston district says its durables producers are concerned that rising interest rates will reduce demand for their products, and Philadelphia district contacts are less optimistic now than they were at the beginning of the year.

Construction and Real Estate

Most districts report generally strong or improving home sales, although many also cite increased mortgage rates as a source of emerging or potential weakness. Residential construction remains brisk in many districts, with the majority of the construction occurring in single-family houses. The Minneapolis district stressed multifamily housing as its construction strength. The Philadelphia district, though, reports some recent slippage in residential construction. The Atlanta and St. Louis districts observed rising house prices, while the Dallas and Richmond districts report stable or slightly falling house prices. Contacts in the Atlanta district say mid-priced homes have replaced starter homes as the big sellers, but low and mid-priced homes are still the big sellers in the Philadelphia district. The shortage of construction workers in the St. Louis district is adding to the already large backlogs previously built up because of weather delays and strong demand.

The Minneapolis district reports that the commercial construction market is strong, and the Richmond district reports recent improvements in this market. The Philadelphia district, however, reports a soft commercial market with slightly increasing vacancy rates.

The Boston district reports declining vacancy rates in Boston, although Hartford's have increased. The New York district reports falling vacancy rates in Manhattan, and the Richmond district says that vacancy rates are falling throughout the district except in northern Maryland and West Virginia.

Prices and Wages

Most districts report that competitive pressures continue to temper price increases on the output side. Contacts in many districts report cost pressures on the input side—albeit modest in many instances. Increases in manufacturers' raw materials prices were noted in more than half of the districts. The Boston, Dallas and Philadelphia districts report increases in chemicals prices and certain metals prices, while the Atlanta, Kansas City, and Richmond districts report increases in construction materials prices. Tightening labor markets were noted in the Atlanta, Chicago, Minneapolis and Richmond districts. Nevertheless, upward pressure on wages, while noted by some districts, appears to be modest. In addition, Philadelphia reports continued increases in employment costs, mainly in benefits.

Banking and Finance

Despite weakness in some areas, loan demand has generally picked up in most districts. Dallas reports that loan demand is up strongly, and San Francisco indicates similar sentiment about loan demand in Idaho and Utah. Business loans have reportedly increased in the Cleveland, Kansas City, New York, Philadelphia and St. Louis districts, while demand for consumer loans has risen in the Kansas City, Richmond and St. Louis districts. The New York district reports that total loan demand has subsided because of increases in short-term interest rates; loan demand is reported to be flat in the Atlanta and Philadelphia districts. Loan demand also remains weak in California, although the San Francisco district reports that an uptick in business lending has occurred in southern California and Hawaii. Demand for auto loans has weakened in the Atlanta and Cleveland districts. The Dallas, Philadelphia and San Francisco districts noted increased competition

among lenders, leading some banks to offer more attractive terms to borrowers. Most other districts report little or no change in lending standards, although some report higher lending rates. For instance, the New York district reports that all of its surveyed banks have increased their rates charged on commercial and industrial loans. Despite recent increases in long-term rates, mortgage lending is mixed. New mortgage lending remains relatively strong in the Dallas, Kansas City and St. Louis districts, but has ebbed in the Atlanta, New York, Philadelphia and Richmond districts. Most districts report a pronounced decline in mortgage refinancing activity. After a strong first quarter, the Boston district reports that mutual fund sales in the second quarter have slowed considerably.

Agriculture and Natural Resources

Crop conditions were generally favorable in most areas, with crop development and planting ahead of schedule. Richmond reports that some recently planted crops may have suffered from unseasonably warm, dry weather. Likewise, St. Louis reports increasingly drier conditions, and some insect problems were noted in the wheat and corn crops. Dallas reports that the winter wheat crop is expected to be off 25 percent from last year because of adverse weather. Minneapolis and Kansas City report adequate soil moisture with most crops in good-to-excellent condition. Kansas City reports that the recent drop in cattle prices produced feedlot losses in excess of \$100 per head. As a result, the Kansas City district expects lower farm income in the livestock sector, although prospects are substantially more favorable for crop producers.

Recent increases in crude oil prices have spurred slightly higher drilling activity in the Kansas City district, but little noticeable increase in the Dallas district. Minneapolis, on the other hand, reports a decrease in petroleum drilling activity in North Dakota and Montana. The Minneapolis and San Francisco districts reports that lumber prices have increased, while Minneapolis indicates that recent increases in copper and steel prices have benefited district producers.

FIRST DISTRICT - BOSTON

Economic activity continues to pick up in the First District. Among manufacturers, the recovery appears to have broadened considerably. Retailers, by contrast, seem to fall into either a high-growth or a no-growth camp. While prices charged by manufacturing and retail contacts are generally holding steady, some materials costs reportedly are increasing.

Retail

First District retail sales results varied widely in recent months. Two discount specialty chains reported increases in sales of roughly 20 percent in April and May compared to year-earlier levels. By contrast, other retail contacts experienced a drop in sales for one or both months, which they attribute to unseasonably cool weather, rising interest rates, and a truckers' strike. Even these retailers, however, have seen a sharp rise in shopping since the arrival of hot weather just before Memorial Day, especially for summer goods, such as garden supplies, patio furniture, and barbecue equipment.

Retail contacts' expectations also vary widely, with a range from 0 to 20 percent in anticipated sales growth over the next six months compared to a year earlier. Most contacts report little or no change in their own or vendor prices, with the exception of increases for wood products. Many retailers say they are struggling to maintain gross margins by cutting operating costs and reducing inventories. Employment levels remain flat, but a few contacts plan major capital expansions this year or next.

Manufacturing

Overall manufacturing sales growth appears to be accelerating, according to reports from First District contacts. Producers of automotive parts, computer components, and residential construction materials note double-digit rates of increase from a year ago. Sales of industrial machinery and replacement parts are rising strongly, with some contacts remarking that this phenomenon is relatively new. Makers of aircraft parts report scattered increases in demand, while noting broader signs of weakness in aerospace. Demand for consumer nondurables is growing in the low single-digit to low double-digit range. Contacts report declining medical equipment and mixed utility equipment sales.

Manufacturers producing consumer nondurables have increased prices by 2 to 5 percent, but most others report no possibility of raising prices. A majority of respondents cite some materials cost increases. Prices of steel, aluminum, copper, paper, chemicals, and plastics are reported to be creeping up, although one producer notes that paper prices remain below their level of a year ago. Prices of cotton and flax fibers have risen noticeably since the beginning of the year.

Most contacts do not appear concerned about materials inflation, in part because some other costs are falling. One-third of the respondents report success in negotiating reductions in purchased goods and services prices. Half express intentions to continue to prune their work force or introduce other efficiencies.

Manufacturers generally expect continued growth in the U.S. economy and their own business. However, those who depend on consumer durables spending expect their growth to slow as a result of rising interest rates.

Commercial Real Estate

Commercial real estate markets are improving throughout most of New England, except Connecticut. Vacancy rates in the Boston area office market continue to decline, with the conventional wisdom now suggesting that new office construction will be proposed in Boston within two or three years. Portland is reported to have limited availability of class A space. Hartford office vacancy rates are increasing.

The nonresidential construction industry is reported to be in fairly good shape after a hard winter, with one contact reporting that new business is coming from renovations of existing retail and institutional space. Margins are up and are expected to continue to rise.

Nonbank Financial Services

Investment management companies report that after a very strong first quarter, mutual fund sales have slowed considerably in April and May. The decrease was primarily in bond funds and was attributed to rising interest rates. Sales of equity funds continue to grow, though more slowly than in the first quarter, with international funds particularly popular. Even after the recent slowdown, the investment companies surveyed plan to increase employment at least 2 to 3 percent in 1994.

The Outlook

The New England Economic Project (NEEP), a nonprofit forecasting group, released its semi-annual regional forecast in mid-May. NEEP projects 2 percent growth in total New England employment in 1994. Work forces in construction, services, and retail trade are expected to expand at above-average rates, while manufacturing employment in the region continues to contract.

SECOND DISTRICT--NEW YORK

The Second District continued its moderate expansion since the last report although some signs of softness were noted. Unemployment rates fell substantially in May, and discussions with manufacturing firms suggest a continuing improvement in that sector. Office leasing activity in Manhattan resulted in lower vacancy rates in both the downtown and midtown areas. In addition, several recent and upcoming events indicate a pickup in the District's entertainment and tourist sectors. On the other hand, most District retailers reported disappointing sales results in May, and though homebuilders were generally positive, a slowing of traffic was noted in some areas. Officers surveyed at small and midsized banks reported a recent drop in mortgage loan demand but some strength in the demand for business loans.

Consumer Spending

Most District retailers reported disappointing sales results in May following April year-over-year changes that were better than expected at several chains. The slowdown in May was attributed in part to unseasonably cool weather which dampened interest in summer apparel. In addition, several contacts noted greater reluctance to spend.

Almost all retailers reported over-the-year sales gains in April despite the fact that Easter shifted from April in 1993 to this year's March. Sales results generally ranged from -2 percent to +10 percent with athletic apparel, jewelry, furniture, and electrical appliances cited as most in demand. With activity slackening in May, several retailers stated that sales were flat over the year and only one chain had results that were greater than plan. Durable goods sold more readily than soft goods in May. Inventories were generally at comfortable levels, aided by greater-than-planned markdowns at some stores. Retailers were hopeful that the May slowdown will prove to be a short-lived aberration.

Residential Construction and Real Estate

Homebuilders in the District were generally positive about conditions in the market for new homes though in some areas a slowing of traffic was noted in recent weeks. Higher

mortgage rates were cited as the reason for this slowing, but observers in other areas stated that rates were still relatively low and the increases had motivated buyers to act before rates moved still higher. A majority of respondents expected starts to be somewhat above last year's level, but this was on the assumption that interest rates would not rise much further.

In New York City, two long-delayed projects are scheduled to get underway in June. In Queens, ground will be broken for the \$2.3 billion Hunters Point riverfront project, under discussion for some ten years, which when completed is to comprise 15 apartment buildings and four commercial buildings. In Brooklyn, construction of the first in a group of 126 three-family homes is to start. The project, initially planned in the 80's, will eventually include two large retail centers as well.

Office leasing activity in Manhattan during recent weeks resulted in lower vacancy rates in both the downtown and midtown areas. The midtown vacancy rate on primary properties is now at its lowest level since the end of 1989, but, on balance, the downtown rate has shown little overall improvement.

Other Business Activity

As was true nationally, unemployment rates in the District dropped substantially in May. New York's State's rate fell to 6.5 percent from 8.2 percent in April while New Jersey's declined to 6.9 percent from 7.2 percent in April. It is possible that the seasonal adjustment factors for the revised household survey exaggerated New York's improvement. Nonfarm employment has been growing steadily in New York since last October and rose strongly in New Jersey during April following a moderate increase in March and a decline in February. No major new layoffs or expansions were announced lately in the District.

The results of recent discussions held with 25 manufacturing firms suggest a continuing improvement in the District's manufacturing sector. While a few large firms plan further employment cuts, most firms anticipate flat or rising employment, increasing unit sales, wage growth of 2-4 percent, and flat or rising capital spending. Such expectations contrast sharply with discussions a year ago which were dominated by anticipated sales

declines, and contracting employment and capital expenditures. Price competition, however, remains intense. All but one firm expect that unit prices will remain unchanged or decline in the next six months. A sizable majority anticipate strong gains in exports, well in excess of the expected growth rates for domestic sales.

Several recent and upcoming events indicate a pickup in the District's entertainment and tourist sectors. During the 1993-4 season attendance at Broadway theaters reached its highest level in six years, and hotel occupancy has been steadily rising since last fall in New York City. Looking ahead, more than one million visitors from all over the world are expected in late June to attend three World Cup soccer games in East Rutherford, New Jersey, and to participate in and watch the eight-day Olympic-style Gay Games and Cultural Festival to be held at numerous locations in the New York metropolitan area. In addition, the New York Knicks made the NBA finals, and the Rangers won their first Stanley Cup in 54 years--the extra games played in the City aided the region's economy as well as dominated the headlines.

Financial Developments

Senior loan officers surveyed at small and midsized banks in the District reported a marked difference in mortgage and business loan demand. There was a pronounced decline in the residential mortgage and refinancing segments where four-fifths of the officers reported a decrease. The demand for commercial and industrial loans was stronger, with about a quarter of loan officers reporting higher demand and fewer than one-sixth, lower demand. Overall, loan demand was down, and most bankers attributed the decline to higher interest rates. Without exception, surveyed banks were charging higher rates on commercial and industrial loans, and almost all reported higher mortgage rates as well.

More than two-thirds of loan officers noted that spreads have widened between their average lending and deposit rates. Credit standards have generally remained unchanged, and most officers are as willing to lend now as they were two months ago. Delinquency rates have been stable.

THIRD DISTRICT - PHILADELPHIA

Reports from businesses in the Third District suggest that economic activity in the region was increasing modestly in early June. Manufacturers indicated that orders and shipments were rising moderately. Retailers had mixed results: apparel sales were down from a year ago but sales of home furnishings were on the rise. Auto dealers generally indicated that sales were healthy. Bankers said that growth in consumer lending remained fairly strong while commercial and industrial lending was just edging up and real estate lending was dropping. Realtors generally reported that the pace of home sales remained good while demand for office space continued to be weak. Homebuilders reported that construction activity has eased recently.

The general outlook among the businesses polled is positive, although contacts have trimmed their forecasts somewhat since earlier in the year. Manufacturers anticipate continued improvement, but they do not expect demand for their products to grow as rapidly as they had forecast this past winter. Retailers remain optimistic, but they also have reduced the amount of growth they are forecasting for the balance of the year. Bankers expect commercial and industrial lending to continue moving up slowly. They expect consumer lending to expand further, but several bankers said they anticipate some slowing in the rate of growth. Realtors believe the rate of home sales will remain good unless mortgage rates begin to climb again, but builders are growing less optimistic about prospects for construction during the rest of the year.

MANUFACTURING

Third District manufacturers polled in early June reported that activity continued to move up at a modest pace. New orders were on the rise at about one-quarter of the firms surveyed, and about one-third were stepping up shipments. However, conditions varied across major goods-producing sectors in the region: manufacturers of machinery and transportation equipment were experiencing the largest gains while orders were either just steady or down somewhat at companies producing primary metals and metal products and at printing plants.

Most local manufacturers were holding inventories steady, although reports of decreases slightly outnumbered reports of increases. Delivery times were unchanged, on balance, as was employment. Manufacturers continued to report increases in employment costs, primarily as a result of increased costs for employee benefits, with relatively smaller increases in wage rates.

Manufacturers' expectations for the balance of the year are positive, although the level of optimism has edged down a bit since the first quarter. Just over 40 percent of manufacturers contacted for this report forecast gains in orders and shipments for the second half, while about 20 percent anticipate decreases. Based on these forecasts of demand, about half of the managers at area plants intend to hold inventories steady and one-third plan to make reductions.

Almost two-thirds of the manufacturers contacted for this report said input prices were steady, although nearly one-third said they were paying more in June than they had in May for certain raw materials, such as metals and chemicals, and for electricity and natural gas. Around 80 percent of the firms polled indicated they were holding the prices of their own products steady, but around 15 percent were raising prices. Looking ahead, around half expect both input and output

prices to remain at current levels, but 40 percent expect both to increase.

RETAIL

Third District retailers gave mixed reports on sales for May and early June. Most of those surveyed said apparel sales were off from last year, and merchants attributed the decline to unseasonably cool weather that dampened demand for spring and summer clothes. Sales of home furnishings and building supplies were generally described as good. Several merchants noted that consumers continue to look for price discounts, making markdowns necessary to maintain sales growth. With the traditionally slower sales pace of the summer months approaching, merchants said they are being very cautious in inventory planning. Retailers' sales forecasts for the fall are conservative as well.

Auto dealers continued to report year-over-year gains in unit sales for May and early June. Some dealers said they are unable to meet demand for a few popular models, but, in general, dealers said their inventories were adequate and they had no plans to increase them. Dealers forecast that unit sales for all of 1994 will be above sales in 1993 by 5 to 10 percent as long as auto loan rates do not rise from current levels.

FINANCE

Most of the Third District bankers contacted for this report in early June said trends in lending had changed little from earlier this spring. Overall loan growth was moderate, with gains resulting mainly from credit card and auto lending. Commercial and industrial lending was just edging up, and real estate lending was declining. Bankers generally described loan pricing for both business and consumer lending as very competitive, and some expressed concern that margins were narrowing as loan rates lagged behind increases in funding costs, despite the recent increase in the prime rate.

Looking ahead, the bankers surveyed in June generally said they expect commercial and industrial lending to grow just slightly in the months immediately ahead. They expect further growth in consumer lending but several mentioned that the pace may slacken, partly as a result of the slower growth in consumer spending that they predict and partly as a result of less aggressive marketing of consumer loans.

REAL ESTATE AND CONSTRUCTION

Commercial real estate markets remain soft, according to leasing officials, with the vacancy rate somewhat higher in central Philadelphia than in suburban areas. No major office construction projects are expected to be started this year. Contacts point out that pharmaceutical companies have expansion plans, but they have put them on hold while new legislation on national health care policy is debated.

Reports from homebuilders indicated that the pace of housing construction was slipping in May and June, and some builders said they were operating below last year's rate. Conversely, realtors continued to indicate that home sales were continuing at a healthy pace, especially for low- and mid-priced homes. However, they caution that home buying will drop if mortgage rates start moving up again.

FOURTH DISTRICT - CLEVELAND

General Business Conditions

District business conditions remain positive and manufacturing activity is brisk. The agricultural sector appears to be off to an excellent start this year and increased investment in farm-related equipment has been noted, although a drier-than-usual spring threatens to affect crop size. Consumer spending is thought to have cooled some from the strong first-quarter pace, although spending on durable goods is still growing at a substantial rate.

Manufacturing

Manufacturers are reporting similar conditions to those seen here since last fall-- orders remain high and generally growing, and orders backlogs have lengthened somewhat. However, cost pressures are moderate for most materials, including steel scrap. The industrial employment picture is still somewhat mixed, with only limited signs of new hires. Hours worked in manufacturing remain at historically high levels.

Many District manufacturers report a modest improvement in foreign orders, although the domestic economy, led by automobile-related manufacturing, is apparently providing the primary thrust to the region's industrial sector. Capital goods orders and shipments are reportedly running 10% or more above year-ago levels, and of these, metal-forming equipment is noted to be particularly strong, perhaps because of the rapid expansion of consumer durable-goods production.

Consumers

While not sounding as optimistic about summer prospects as in their April report, District retailers appear confident that sales will hold steady over the next few months. Part of the dampened expectations stems from unseasonably cool weather in May, but retailers also report a generally more cautious consumer.

Apparel sellers were the least positive of the respondents. Specialty stores are "struggling" to boost sales with promotions and special pricing, and clothing demand at department stores has been flat. Colder-than-average temperatures in May account for some of the slowdown. Cool weather is being blamed for slower-than-desired sales of seasonal building materials and garden supplies.

However, sellers of appliances and, to a lesser degree, furniture continue to report a very positive performance. Appliance dealers note that while year-over-year sales at comparable outlets are not improving at the double-digit rates seen in the first quarter, high single-digit gains are not uncommon. Sales growth has been broad based, but demand for computers and related equipment has been especially strong.

Autos

Similar to other District retail numbers, auto spending appears to have shifted to a slightly slower gear. Although auto sales continue to improve on a year-over-year basis, the pace has slowed from the first quarter. Dealers blame decreasing consumer confidence and continuing shortages of some popular models (mostly trucks and sport-utility vehicles) for the slowdown. Floor traffic is not quite as strong as earlier in the year, and demand for higher-priced vehicles and options has diminished somewhat.

In contrast to dealers of domestic nameplate vehicles, Japanese auto dealers report sufficient stocks of most vehicles. They also note slower sales improvements relative to U.S. manufacturers.

Although auto lending rates have risen 1/4 to 1/2 percentage point in the past month or so, area dealers see little direct effect on sales. Some dealers suggest that the rapidly expanding lease market may have partially insulated consumers from the cost of higher interest rates.

Banking and Credit

Although lending activity has slowed from its winter peak, major banks in the District report a steady growth in loans. With the exception of the widely noted falloff in mortgage refinancing, rising interest rates have not yet appreciably impacted borrowers. Although automobile loan growth has slowed somewhat, sources conjecture that this may be due to shortages of certain popular models that have dampened the pace of auto sales.

Business lending is generally growing, with one respondent reporting that activity is stronger now than six months ago. Inventory financing needs and capital spending plans that had previously been financed internally lead some observers to anticipate a continuation of business loan growth. However, a cautionary note was sounded by at least one respondent, whose institution saw commercial loans dip in May.

On the deposit side, flows of funds into small certificates of deposit and money market mutual funds appear to have increased substantially, apparently attracted by the recent rate increases on these instruments.

FIFTH DISTRICT-RICHMOND

Overview

District economic activity increased moderately in May and early June. Tourism was robust, particularly over the Memorial Day weekend. Manufacturing indicators and retail sales increased, but service-producing firm activity rose only moderately and trade volume through District ports changed little. Mortgage lending activity declined although conditions in commercial real estate and housing improved. Reports indicated scattered labor shortages and some modest upward pressure on prices. In agriculture, spring planting neared completion, but some crops experienced heat stress.

Consumer Spending

Respondents to a regular mail survey indicated that District retail activity increased in May. Retailers reported gains in employment, wages, and sales, including those of big-ticket items. Other contacts, however, noted that auto sales weakened after April 15. Survey respondents indicated that retail prices increased 0.4 percent in May and foresaw price increases of 1.1 percent during the next six months. Looking ahead, retailers expected demand for their products to strengthen in the coming months.

Manufacturing

A mail survey of District manufacturers showed increased factory activity in May. Shipments, new orders, and employment were higher in recent weeks. Finished goods prices increased slightly, and raw materials prices rose by less than the general inflation rate.

Producers expected no change in employment, a longer average workweek, lower finished goods inventories, and a slight increase in prices during the next six months.

Service-Producing Sector

District service-producing firms indicated that activity increased moderately in May. Revenues and wages rose, but employment was steady. Respondents reported a 0.6 percent increase in the prices of their services. They expected that in the coming months their prices would rise 1.4 percent and demand for their services would increase.

Tourism

A telephone survey of hotels, motels, and resorts throughout the District indicated robust tourist activity in recent weeks. Over the Memorial Day weekend, many beach areas were booked to capacity and several reported record-setting activity. Other tourist areas also experienced strong increases in bookings, which they attributed to unusually favorable weather and a surge in group reservations. Based on current bookings, respondents anticipated that summer tourist activity would far exceed last year's level.

Ports

Representatives at the ports of Baltimore, Charleston, and Hampton Roads (Norfolk) indicated that the volumes of exports and imports remained about the same in May as in April. Compared to a year ago, imports were higher and exports were unchanged. Baltimore and Hampton Roads expected exports to increase faster than imports during the next six months, but Charleston expected no change in activity.

Finance

District financial institutions indicated that credit conditions were mixed during the last six weeks. Interest rates rose on both commercial and consumer loans. Consumer loan

demand remained fairly strong, but commercial loan demand declined slightly. Mortgage lenders indicated that originations were relatively slow and that refinancing activity virtually disappeared. Commercial and mortgage loan officers were cautious but optimistic about loan demand in the months ahead.

Residential Real Estate

According to District contacts, housing sales and building permits were steady in April and May, but buyer traffic decreased. Homebuilders indicated that they started fewer houses because of the recent rise in mortgage rates and their uncertainty about future rates. Home prices remained stable, although lumber prices and construction wages increased. Some builders reported that non-lumber materials prices also rose, but at a slower pace than in previous months.

Commercial Real Estate

Commercial real estate improved further in recent weeks, according to industry analysts. Office building vacancy rates fell in most areas of the District, but were unchanged in northern Maryland and in West Virginia. Commercial rents were steady, but contacts expected slight increases in the near future. The availability of large blocks of office space continued to tighten, particularly around Charlotte and Washington, D.C. Some construction of office buildings for owner/occupants was underway across the District, but no new speculative projects were reported. Several contacts indicated that renovations of older office buildings temporarily lessened the need for new office building construction in their areas. Large discount retailers continued to expand in North Carolina, Virginia, and West Virginia, and demand for warehouse space remained strong in northern Maryland and in Greenville, S.C.

State Revenues

State government tax revenues continued to grow at healthy rates in most areas of the District. Based on May sales tax receipts, state forecasters indicated that retail sales ranged from "good" in Maryland to "booming" in North Carolina. Analysts suggested that overall revenue collections were consistent with real economic growth rates of 2.5 to 3.5 percent, except in the District of Columbia, where revenue growth was just keeping pace with inflation.

Agriculture

Unseasonably warm, dry weather in recent weeks aided farmers' planting and harvesting activity but stressed some recently planted crops. District planting activity was ahead of its normal pace, as was the harvesting of wheat and other small grains in the Carolinas. Early yields indicated that the small grain crop had not been substantially damaged by the severe cold of last winter. Inadequate soil moisture in many areas of the District, however, hampered the development of corn, soybeans, and peanuts. In West Virginia, the peach crop was in poor condition as a result of damage to orchards from last winter's ice storms.

SIXTH DISTRICT - ATLANTA

Overview: According to business contacts, the Southeast economy continued to expand through May and early June, but at a more subdued pace than earlier in the year. Most retailers reported an unseasonably large drop in May sales, although some noted a rebound in consumer spending in the first week of June. Auto dealers also noted a slowdown in sales in May. While home sales slowed modestly in the last month, contractors report that single-family home building remains brisk. Multifamily and commercial real estate markets continue to improve, with several new apartment and commercial developments being announced in the last month. Bankers, however, generally report that business and consumer loan demand was flat in May. Wages and prices were reported to be stable for the most part, although several manufacturers said that they have begun to pay higher prices for raw materials.

Consumer Spending: After posting strong gains in the first quarter, retailers throughout the District reported disappointing sales in late April and May. However, most contacts noted an upturn over the Memorial Day weekend and stronger sales in the first week of June. Women's apparel sales, which had improved earlier this year, softened in May, and sales of men's and children's apparel also slowed. As a result, several retailers reported that they have had some unintended inventory accumulation. According to contacts, pricing at both the wholesale and retail level remains very competitive, with several merchants reporting deep discounting. Although retailers generally have revised downward their projections for sales through the summer and early fall, many remain hopeful that back-to-school shopping will be relatively strong this year.

Manufacturing: According to factory contracts, industrial production rebounded slightly in May after slowing modestly in April. Suppliers of building materials continue to report increases in production and new orders, although rising interest rates have led some

producers to adjust downward their long-term demand projections. Suppliers to the auto industry continue to receive a steady stream of new orders, and several firms reported that they have begun to invest in new plant and equipment in order to meet expected future increases in demand. Producers of industrial equipment and machinery noted that they have extended their average workweeks to meet recent increases in the volume of new orders. District carpet producers report that order backlogs have risen, while strong demand for bedding and healthcare textiles reportedly has stimulated new hiring at several firms in this industry. On a less positive note, NASA and Defense Department budget cuts continue to produce layoffs at regional aerospace and defense electronics firms, particularly in Florida and Alabama.

Tourism: Reports from tourism industry contacts were mixed in May. In Florida, contacts said that tourism has been flat in key market areas, largely because of competition from other vacation destinations and negative publicity about crime. Convention business in the state, however, has been better than anticipated, and is expected to remain good through the end of the year. Similarly, convention business in New Orleans and Atlanta has been unexpectedly strong this year. Casino gambling along Mississippi's Gulf coast continues to draw large numbers of visitors to the area. Tourism in the state of Alabama also was reported to be up significantly over year-ago levels.

Construction: According to District realtors, May home sales were down slightly compared with last year's relatively strong levels. Although they said that rising mortgage rates initially stimulated an increase in home buying from "fence sitters" pushed into the market, more recently they have begun to put a brake on single-family home sales. Nevertheless, most contacts continue to characterize current sales levels as very good. Mid-priced homes have replaced starter homes as the most popular sellers, while sales of luxury homes also have improved. Although District building contractors have noted a decrease in traffic through new subdivisions,

the pace of new home construction remains brisk. The rising cost of home building materials continues to push new home prices higher, but most realtors and builders remain optimistic that new and existing homes will continue to sell well into the fall.

Contacts in commercial and multifamily real estate markets report sustained improvement in these sectors. Multifamily occupancy rates continue to rise, and rental rates also have been increasing. New apartment developments have been announced recently in many areas of the District. Commercial real estate agents report that falling vacancy rates and rising rental rates have led to the possibility that some speculative building may occur within the next year. Currently, most construction continues to be build-to-suit and public buildings, although the number of these projects has increased in the last few months.

Financial Services: According to District bankers, overall loan demand remains flat in the Southeast. While some reported that business loan demand improved slightly in May, others noted that consumer lending, particularly auto loans, had weakened. Residential mortgage refinancings have dried up completely, while mortgages for home purchases were down slightly compared with month-ago levels.

Wages and Prices: Reports of increasing wage pressures continue to be limited to those areas where skilled construction workers are in great demand. Although some manufacturing contacts have reported price increases for raw materials, competitive market forces have made it difficult for firms to pass these costs on in terms of higher prices for finished goods.

SEVENTH DISTRICT--CHICAGO

Summary. Seventh District economic growth slowed during the second quarter, as both consumer spending growth and manufacturing activity moderated. Light vehicle production declined on a seasonally adjusted basis in recent months, and preliminary schedules show flat to slightly declining output in the third quarter. District payroll employment has grown more closely in line with the national average during 1994, but household survey data and help-wanted advertising indicate that labor markets in the region remain tighter than for the nation as a whole. The consensus forecast of 30 Midwest economists prepared for an auto industry outlook conference called for moderate GDP growth to continue during 1994 and 1995.

Manufacturing. District manufacturing activity generally remained quite vigorous in recent months, with purchasing managers' surveys depicting slower but still-strong growth through May. The composite index of production components of purchasing managers' surveys in Chicago, Detroit and Milwaukee declined from 75.0 percent in April to 70.6 percent in May. The May level was still consistent with moderate-to-robust expansion in manufacturing activity, however, and this indicator remained well above the national average. The Chicago production index climbed to 76.5 percent in April -- nearly its highest level since 1970 -- but then fell back slightly during May. A larger drop was registered in the Detroit index during May, however, consistent with the slower momentum seen in auto industry output. A large utility reported that growth in power sales to industrial customers in Michigan eased during early June, after outpacing total sales through most of 1994.

Among key industries, District steel production rose on a seasonally adjusted basis in April and May, climbing to its highest level for May since 1989. Output is expected to slow somewhat in coming months, however, partly because some large integrated mills are bringing production facilities down for necessary maintenance and repair. Third quarter production is still "sold out," with continued strength in orders from the motor vehicle, appliance, farm machinery, and construction equipment industries. Reports from manufacturers of farm machinery and construction equipment remained upbeat. Production and retail sales of heavy-duty trucks continued to climb in recent months, although current schedules imply a small decline in output in the third quarter. An industry analyst stated that any output gain in the latter half of the year is not likely to be significant, given current capacity levels, but order backlogs are still believed to be of high quality, and the order cancellation rate remains below year-earlier levels and well within historical norms.

Consumer Spending. Surveys and reports from large retail chains suggest that retail sales growth moderated (on a year-over-year basis) during April and May. An index of same-store sales growth constructed by a check authorization firm showed a declining rate of growth in retail sales in the Midwest during April and May. A survey of a large number of retail locations in Illinois and Indiana showed sales growth moderating in April, except for hardware and other housing-related outlets, where sales growth remained relatively strong. A survey of shopping centers also pointed to a slower sales growth during April. While the April slowing has been partly attributed to the early Easter holiday this year, reports from a number of retail chains as well as a group of single store owners suggested sales growth remained sluggish during May. One large retail chain reported that modest growth was little changed during May and early June, and this contact stressed that competitive pressures on price and margins continue to intensify in most of its market areas.

Autos. District light vehicle output has increased slightly more than the national average during 1994, but assemblies declined on a seasonally adjusted basis in recent months, and preliminary schedules show little sign of any substantial rebound during the third quarter. Reports from large automakers and a small sample of large auto dealerships suggested that vehicle sales have also slowed in recent months, partly due to capacity constraints in production of some popular models. One large automaker stated that "we can no longer confirm that the market is red-hot." Higher interest rates have increased vehicle financing costs and dealer floor planning expenses, curtailing some sales gains. Another large automaker reported that dealer showroom traffic flattened out in March and April, while sales closures rates declined slightly. Reports from a small sample of large auto dealers were mixed but still suggestive of slower sales, with most of them indicating that increased interest rates have cut into sales gains.

The recent slowdown in auto industry momentum is coming from high sales levels, however, and most industry contacts expressed optimism about renewed growth in the latter half of the year. Some industry analysts have expressed concern that a surge in cars coming off lease could curb new car sales during 1994 and into 1995, much like the bubble of "nearly new" cars that arose after the acceleration in deliveries to captive rental car fleets in the early 1990s. A large automaker emphasized that it has planned its leasing promotions to avoid a serious problem in this area. No car dealers expressed concern about the phenomenon, with one noting that "the average person holds on to a new car for three years, if they buy it or if they lease it. We don't see this being a very big deal." Another dealer expected the increased share of leasing to promote new car sales by encouraging people to buy new cars more often. Asked what happened when 2-3 year old cars started coming back into the dealership, this contact stated

"we can't buy enough 2-3 year old cars as it is." An automobile dealers' association reported that its measure of dealer optimism rose to an all-time high in April. A large automaker stated that pent-up demand for motor vehicles remains substantial and should provide a strong base for growth over the balance of 1994 and into 1995.

Employment. District labor markets continued to strengthen in April and May. A survey of employer hiring plans conducted by a large personnel services firm showed a slight decline (to still-high levels) in the majority of Midwest employers planning to add to their workforce next quarter. Hiring plans among durable goods manufacturers continued to top the list of 10 industrial categories within the region, and remained significantly stronger than their national counterparts. Purchasing managers surveys generally confirmed the upward momentum in District manufacturing employment during May. Reports from a number of retailers and manufacturers pointed to shortages of workers in lower-wage level positions, adding to wage pressures in this area.

Growth in total payroll employment in the District has fallen in line with the national average during 1994, but help-wanted advertising and unemployment rate estimates point to relatively tight labor markets in the region. For example, among the 11 large states for which the Bureau of Labor Statistics computes direct unemployment rate estimates, Michigan and Illinois had the second and third lowest unemployment rates, respectively, during May, while the unemployment rate in Michigan has fallen to a 20-year low during 1994. The unemployment rates for Indiana, Iowa and Wisconsin are below those for Illinois and Michigan, and the gap between the District unemployment rate and the national average continued to widen in the District's favor this year.

Outlook Conference. The Federal Reserve Bank of Chicago's annual Auto Outlook Conference was held in early June. The consensus GDP forecast of 30 economists from around the District that was prepared for the meeting called for a 3.6 percent increase in real GDP in 1994. While a significant improvement from the forecast prepared in December 1993, the growth rate implied by the latest forecast over the balance of 1994 was unchanged from the pace expected last December for 1994 as a whole. The consensus called for car and light truck sales in 1994 to total 15.4 million units, up from 13.9 million units in 1993, while a smaller gain was anticipated for 1995. Presentations by auto industry representatives were largely upbeat about the underlying upward momentum in the marketplace, although several expressed a note of caution about recent sales trends. Competitive price and market pressures continue to concern many industry suppliers.

EIGHTH DISTRICT - ST. LOUIS

Summary

District economic activity continues to expand vigorously as contacts report growth in both employment and sales. Defense-related firms, though, reported some layoffs. Contacts also report minimal cost pressures and see future price increases as unlikely. Retailers and auto dealers report generally brisk sales and are optimistic about the second half of the year. While recent increases in long-term interest rates have slowed residential construction activity somewhat, they have not had much effect on home sales, which remain robust. Consumer and business loan demand continues to rise at District banks. Favorable crop conditions are reported in most areas of the District.

Manufacturing and Other Business Activity

District firms report strong growth, citing plant expansions and sales increases. In some places, particularly in St. Louis, contacts are beginning to report shortages of available workers, forcing some to offer higher wages. This shortage is reflected in St. Louis' low April unemployment rate, 4.8 percent, its lowest since July 1979. One contact said that his firm had trouble retaining newly hired employees.

Growth is occurring in both manufacturing and nonmanufacturing firms in all parts of the District. For example, two poultry processors report new plants opening in Kentucky, one initially bringing 850 jobs, and the other bringing 1,300. An apparel maker will also move to Kentucky and employ 600 by year's end. Contacts in western Tennessee report the opening of a new auto parts plant, employing 500 workers, and the expansion of a paper factory, adding 200 workers. A greeting card company, expanding into northeast Arkansas, will employ 250 workers. Because of a new contract, a St. Louis corporate services firm hired an additional 400 workers. A heavy equipment dealer says demand has outpaced supply, creating severe shortages but leading to sales increases of more than 20 percent over last year. Other contacts also report sales increases over last

year and expectations that this will continue at least through next quarter. For example, a building supplies company and a pallet manufacturer both report sales increases of 15 percent, while a die casting company's sales grew 10 percent.

Domestic markets remain strong for most products, particularly animal feed, although some slowdowns in the hospitality and metal plate products industries were noted. Reports about foreign markets vary with company and destination. Most say that overall exports are weak with only the Pacific Rim countries as a source of rising demand.

Most reports of layoffs in the District are defense-related. An army base reports it will lay off about 250 civilian employees by the end of September because of restructuring within the military. An electronics company producing engines and other parts for defense aircraft laid off 100 white-collar employees because of spending cuts, and a missile producer will eliminate about 240 positions because of scheduled production decreases. Separately, the catfish industry reports that nationwide shortages of catfish are causing firms to release workers. One firm laid off its entire night shift of 295 people.

Most discussions with area business people suggest that cost pressures are minimal. In general, the largest average reported increase was about 3 percent. Many of these contacts state that increased foreign competition prevents them from increasing prices on their products. Some even stipulated that when presented with opportunities to raise prices, they decided not to. In addition, some claim they can now find their raw materials overseas when there is a shortage domestically, which helps to keep prices down. The consensus among contacts was that District wage increases are running between less than 1 percent and 3 percent.

Consumer Spending

Retailers throughout the District report moderate to strong sales in recent months, with some contacts reporting increases as large as 25 percent over one year ago. Most contacts report that recent sales have met or exceeded their expectations, and most are optimistic about the second half of 1994. Auto dealers also report strong sales, and most

expect sales growth at or above its current pace over the remainder of 1994. Rising interest rates have had a minimal effect on sales thus far. Truck and sport utility vehicle sales are particularly strong. In addition, sales of imports have picked up some of the momentum they had lost in recent years.

Construction and Real Estate

Though residential construction activity remains brisk in most parts of the District, some areas are reporting a slowdown, which contacts attribute to recent increases in mortgage rates. Still, the single-family housing market can be characterized as strong, with sales of new and existing homes at or above last year's pace. A shortage of homes for sale, rising prices and quick turnaround are reported in many areas. Some areas also report a shortage of skilled tradesmen for construction jobs, which is further adding to backlogs previously built up because of weather delays and strong demand.

Banking and Finance

District bankers report continuing improvement in consumer and commercial loan demand. While refinancing activity has come to a standstill, mortgage lending is still relatively strong, with consumers increasingly showing a preference for adjustable-rate mortgages. Commercial loan demand from small businesses is especially strong. Some bankers report that deposit growth is not keeping pace with loan demand growth, which is increasing funding costs.

Agriculture and Natural Resources

Crops appear to be in mostly fair-to-good condition across the District. In parts of Illinois and Missouri, however, an outbreak of insects has affected the wheat crop, and in parts of Arkansas the cotton crop has suffered some herbicide damage. Moreover, some contacts report a significant upsurge of European corn borer activity in parts of the Midwest. In general, soil moisture seems adequate, although drier conditions are becoming increasingly prevalent in many areas.

NINTH DISTRICT--MINNEAPOLIS

Strong growth is evident in the Ninth Federal Reserve District. Automobile sales are booming, general merchandise sales continue to increase, and summer tourism appears off to a strong start. Both commercial and residential construction remain strong. Manufacturing output apparently continues to grow. Iron ore shipments are up, and prospects for other metal mining have improved. Crops are in excellent condition across most of the district, while livestock numbers remain high. Employment levels continue about 2 percent to 3 percent above year-earlier levels, while unemployment rates have dropped from one-half to one full percentage point in the same period. Despite this strong growth, there is little evidence of significant upward movement in wages or prices. Employers in certain areas continue to report problems in securing qualified new employees, some manufacturers report difficulty in obtaining steel, and price increases are reported for industrial metals.

Consumer spending and tourism

A North Dakota auto dealer's comment, "My inventory has never been so low," characterizes the strong pace of vehicle sales across the district. Dealers' association spokespersons echo this sentiment and note that some popular models are in very short supply.

General merchandise sales continue to strengthen. "Traffic has been very good," reports a North Dakota mall manager. Another mall manager in North Dakota commented that sales of appliances and electronics seemed particularly strong but that virtually all stores in his facility had good business. Regional department store chains also report very good sales, and a Minneapolis Fed poll of district business leaders disclosed that nearly half expected consumer spending to be up in coming months. Only 4 percent expected it to drop.

The 1994 tourist season is apparently off to a strong start. Visits at several South Dakota sites since January 1 were up as much as 19 percent over year-earlier levels and tourism officials in that state predict an excellent season. Their counterparts in Minnesota and Montana express similar optimism.

Construction

Residential and commercial construction continues strong in all states of the Ninth District. New housing permits in Minnesota for April were 13 percent above 1993 levels, which already reflected a fast-pace. Virtually all of the increase over 1993 was in multifamily construction. In the rest of the district, residential construction reportedly is active in most regional centers, including Sioux Falls and Rapid City, S.D.; Billings, Bozeman and Missoula, Mont.; Grand Forks and Fargo, N.D.; and LaCrosse and Eau Claire, Wis.

The strong pace of commercial and heavy construction set last year continues in the 1994 season. In Minnesota and the Dakotas, contracts through April were down about 1 percent from 1993's very active levels but still 22 percent above 1992.

Strength in this sector is indicated in April construction employment, which is up nearly 6 percent in Minnesota, 7 percent in South Dakota, 16 percent in North Dakota and 18 percent in Montana compared to year-earlier figures.

Manufacturing and natural resource industries

District directors note growing business for manufacturers. One reported that a small plastic components producer was running three shifts seven days a week. Electricity sales to industry by one large Minnesota and South Dakota utility is growing at twice the five-year trend rate. Some of the increase is attributable to a major expansion at a petroleum refinery, but sales to machinery manufacturers increased at nearly three times the overall trend.

There are some positive notes in natural resource industries. Copper prices have increased over 25 percent in recent weeks, allaying fears of possible mine closings. Strong demand from the steel industry has buttressed iron ore shipments from Lake Superior ports. And substantial new drilling for gas is under way in Montana. However, petroleum production continues to drop in North Dakota and Montana.

Agriculture

In spite of localized problems with hail and topsoil dryness, 1994 crops are reported good or excellent in virtually all farming areas. Moisture levels are adequate in most areas, and very little land in the Ninth District suffers any of the lasting damage from the 1993 floods that is reported in downstream states. Development of all major crops was generally equal to or ahead of five-year averages in all district states. Yields on the first cutting of hay in Minnesota and Wisconsin are reportedly down slightly from 1993 but quality is excellent.

In the livestock sector both cattle and hog numbers remain high in comparison to historic levels. Hog slaughter levels are largely unchanged in spite of sharp price declines in recent weeks. Cattle slaughter is down slightly from year-earlier figures, but industry observers continue to expect hog and cattle numbers to grow modestly through the rest of the year.

Employment, wages and prices

Strength in the Ninth District economy is demonstrated in tightening labor markets. Employment shows increasing growth. April non-farm employment numbers across the district are 2 percent to 3 percent above year-earlier levels. Unemployment rates have dropped from April 1993 levels in all areas of the district. Drops range from 0.6 percent in the Dakotas to 1.1 percent in Minnesota. Excepting Montana and Michigan's Upper Peninsula, unemployment levels throughout the Ninth District are about two points below the national average. Directors and other sources report that many firms have difficulty in attracting qualified new hires, but wage increases remain modest. One Minnesota computer manufacturer did announce a 200-worker reduction, largely through early retirements, and the reassignment of an additional 300 workers in a cost reduction move.

Despite indications of strong economic growth there is little evidence of generally increasing prices. However, raw materials are one area with some evidence of price pressures. Prices of steel, copper and aluminum have increased and several firms report delays in securing steel, particularly in specialty grades. Wood particle board for manufacturing remains difficult to procure. Lumber prices remain higher than a year ago. Petroleum fuels, however, continue 3 to 10 cents per gallon below early 1993 levels.

TENTH DISTRICT - KANSAS CITY

Overview. The Tenth District economy continues to grow at a healthy pace. Retail sales are increasing and manufacturers are operating at high levels of capacity use. While sales of new homes are showing signs of slowing, residential construction remains on the increase. In the farm sector, weak cattle prices are bringing steep losses to the cattle industry but conditions for crop producers are favorable. District energy activity is generally sluggish although firmer oil prices are beginning to spur drilling activity in some areas. Retail prices remain stable, while manufacturers' input prices are increasing modestly.

Retail Sales. Most district retailers report moderate sales increases led by strong apparel sales relative to both a year ago and the past month. Retail sales are expected to increase in the next few months. Competition continues to keep retail prices stable and is expected to preclude any significant price increases in the near term. Most retailers are satisfied with current inventory levels, although some respondents expect to increase inventory purchases in response to rising demand.

Auto dealers generally report sales increases from last month. Dealers are optimistic that sales will continue to grow over the next few months and thus are expanding or maintaining inventories. A few respondents report difficulty in obtaining enough new cars from manufacturers to meet their demand. Financing is available for both dealers and potential buyers.

Manufacturing. Most purchasing agents report input prices are modestly higher than a year ago, but few expect further price increases in the near term. Some agents report longer lead times and difficulties in getting materials. Most respondents are boosting inventory levels but expect a

reduction in the coming months due to increased sales. Firms are generally operating at high levels of capacity use. Some firms are experiencing bottlenecks due to shortages of skilled labor. Export sales have been stable and are expected to remain so in the next few months.

Energy. District energy activity remained sluggish in May restrained by a further dip in natural gas prices. The average number of drilling rigs in the district fell to 207 in May from 213 in April. However, steady increases in crude oil prices are beginning to boost district drilling activity. For the first week of June, the district's rig count stood at 225.

Housing. Housing starts increased over the past month and remain higher than a year ago. Single-family homes accounted for most of this increase. For the remainder of the year, builders generally expect starts to level off. Sales of new homes are slowing, but builders continue to report tight inventories. Prices of building materials remain high. All respondents report problems with cement availability.

The demand for mortgage funds continues to subside with increasing mortgage rates. However, most respondents expect rates to level off and the demand for mortgage funds to remain stable or increase slightly.

Banking. Loan demand rose last month at almost all reporting banks. Most banks reported higher demand for commercial and industrial loans, consumer loans, home mortgages, and residential construction loans. Demand was flat to up for commercial real estate loans and mixed for home equity and agricultural loans. Loan-deposit ratios were up from the previous month. About equal numbers of banks reported that security investments were up, down, and unchanged.

All respondents raised their prime rate last month and almost all expect to leave the rate unchanged in the near term. Banks also raised their consumer lending rates last month, although most banks anticipate no further change in the near future. Lending standards were unchanged.

About half of the banks reported no change in deposit levels last month, while the other half were divided between increases and decreases. Changes in deposits were mixed in all deposit categories.

Agriculture. Recent rainfall has improved prospects for district crops. The winter wheat crop is generally in fair condition and normal yields are expected throughout most of the district. The wheat harvest should be in full swing by late June. The corn and soybean crops are in excellent condition due to favorable weather and adequate soil moisture. With crop inventories unusually lean, prices are likely to remain volatile as crop prospects shift during the growing season.

An abundance of market-ready cattle and large supplies of competing meats have pushed fed-cattle prices to the lowest level in nearly three years. As a result, losses in many district feedlots exceed \$100 per head. Little recovery in cattle prices is expected until autumn, pointing to further losses for the district's most important agricultural enterprise.

Farm income prospects for 1994 diverge widely by type of farming due to the bleak outlook for the district cattle industry and a more favorable crop outlook. Most district bankers expect a sharp downturn in incomes among district cattle producers. But higher crop prices and a rebound in crop production after last year's weather-induced losses are expected to boost incomes for district crop producers.

ELEVENTH DISTRICT--DALLAS

The rate of economic growth appeared to be unchanged in May and early June. Demand remained moderately strong in many industries, and most contacts did not expect a change in the rate of growth of economic activity through the end of the year. Manufacturing orders were steady, and demand for business services remained moderate. However, retail sales growth was reported to be sluggish and below expectations, particularly for apparel. Although construction and real estate activity continued at fairly high levels, softness in the homebuilding industry has begun to appear. Energy production, drilling and services continued to rise at a moderate pace, but did not accelerate with higher oil prices. District bankers said that loan demand had increased strongly, but competition for loans was intense. Planting and crop growth was generally on schedule, but weather damage affected some areas.

Manufacturing orders were steady. Demand for construction-related materials remained strong, with brick, cement and glass producers reporting higher demand and prices. Brick and cement producers were operating at 100 percent capacity, and said that they were having trouble filling orders. Several non construction-related manufacturers expect demand growth in 1994 to be good but lower than in 1993. Demand continued to be strong for electrical and electronic machinery, particularly telecommunications products. Selling prices of semiconductors stopped declining, and demand decelerated slightly as manufacturers had expected. Although orders for primary and fabricated metals remained strong, contacts said that steel and scrap metal prices had fallen. Sales of lumber and wood products were steady to slightly higher but below this time last year. Demand for paper products was up, and contacts reported that they had increased their prices slightly. Apparel producers said that sales were steady or slightly higher. Garment contacts were mixed about upcoming changes in the industry resulting from NAFTA. Some contacts have found entering the Mexican market to be harder than they expected but believe that Mexico will be a source of future sales. One contact is concerned that

increased demand for labor in Mexico will raise the firm's production costs there. Sales of food and kindred products were down slightly. Demand for drilling services and machinery was steady for natural gas but down slightly for oil. Foreign demand for services and equipment remained sluggish, especially from the Middle East and Nigeria. However, sales had increased to Latin America, particularly Venezuela after privatization of its oil industry. The arrival of the summer driving season increased demand for gasoline, but higher crude oil prices squeezed refinery profits. Demand for chemicals continued to increase, and prices rose 10-15 percent for some products. Sales were strongest for the styrene chain, especially polystyrene, and went up for ethylene and polyethylene as well. Chemical sales to Europe increased strongly, but Asian markets generally remained weak.

Most business service firms reported steady demand. Activity at temporary service firms remained unchanged overall with higher demand from electronics and telecommunications firms. Law firms said that activity was slightly higher, and they were trying to do more work without hiring. Demand for advertising and communications had declined. Hotels reported increased bookings but fewer than they had expected for the World Cup. Airlines noted slower passenger demand than expected, although traffic was above a year ago. Air, rail and trucking cargo continued to increase strongly. Competition and lower fuel prices kept transportation prices unchanged despite higher demand.

Many contacts reported that May retail sales growth was slower than expected. Sales picked up slightly in early June leading retailers to be cautiously optimistic that sales growth would continue. Demand for apparel products remained weak, while sales of building and home improvement products were strong. Some national contacts reported that Texas retail sales growth was slower than the rest of the nation's with particular weakness along the Texas-Mexico border. Competition was keeping selling prices below last year's levels, and contacts said that they were purchasing fall merchandise at the same price or slightly higher than in 1993. Automobile sales were sluggish in May but picked up in early June. Still, dealers reported that they would like

to increase their inventories of some vehicles. Auto prices were stable.

Construction and real estate markets remained fairly strong, but homebuilders reported a slowdown in new home sales and traffic. Although contacts were optimistic about the outlook for the rest of the year, home prices have generally flattened, and some builders reduced their prices. Apartment markets, however, remained tight and occupancy rates and rents moved higher. A pickup in demand for office and industrial space boosted commercial construction. Prices and rents increased for office and industrial property.

Energy production and drilling continued at a moderate pace but did not accelerate with higher oil prices. Oil prices rose to \$18 per barrel in mid-May from a low of \$14 in March. Natural gas prices fell briefly in May encouraging distribution companies to make major injections into storage tanks that had been depleted by winter's cold weather. Drilling had not staged its normal seasonal turnaround, but the rig count remained well ahead of last year. Most drilling continued to be for natural gas and in the Gulf of Mexico.

District bankers said that although loan demand continued to increase strongly, competition for loans was intense. Contacts said that some banks were loosening their credit standards to extend business loans. Bankers complained that regulations, such as mandatory appraisals, were making it difficult for them to compete with mortgage bankers and other lenders. Home mortgage refinancing had fallen dramatically, but originations for home purchase had not.

Planting and crop growth was on schedule, but unfavorable weather weakened some agricultural production. Heavy rain prevented some cotton producers from planting their crop, although planted cotton was in good condition. Dry conditions had stressed ranges in the Trans-Pecos and South Texas, but livestock remained in fair to good condition. Texas farmers expect to harvest about 25 percent less wheat than last year because the crop was damaged by dry weather and a hard freeze earlier in the year. The Texas May All Crops Price Index was 7.2 percent above 1993's level, while the Livestock and Livestock Products Price Index declined 10.6 percent from last year.

TWELFTH DISTRICT -- SAN FRANCISCO

Summary

While economic conditions are reported to be improving slowly in California and Hawaii, activity is strong in most other parts of the Twelfth District. Business leaders remain optimistic overall. Retail sales and tourism continue strong in many areas of the District. Manufacturing activity still is mixed, as weakness is reported in the aerospace industry while improvement is expected by some Silicon Valley firms. Livestock and dairy prices are soft. Construction and real estate activity generally remains strong, although home sales in some parts of the District are reported to have slowed in May in response to higher interest rates. Lending activity is rising, and banks are reported to be more aggressive in pursuing loans.

Business Sentiment

Twelfth District business leaders remain optimistic. Almost two-thirds of respondents continue to expect national growth to exceed 2 1/2 percent during the next four quarters. Respondents in Arizona and the intermountain states expect especially strong growth in their regions. However, only about two-fifths of business leaders now expect housing starts to improve during the next four quarters, down from more than one-half in April. Less than a third of respondents now expect the inflation rate to rise during the next four quarters, compared with over one-half in April.

Retail Trade and Services

Retail and service industry conditions remain strong in most parts of the District. Consumer durable sales are reported to be especially strong, with only a little evidence of slowing in response to higher interest rates. Prices for food and clothing show little increase.

Auto sales in Idaho are reported up 25 percent in the first quarter of 1994 from the level of a year earlier, although sales in May slowed somewhat. Auto and light truck sales in the Pacific Northwest are reported strong, and sales are improving in parts of California. In Arizona, furniture and building materials sales through April are reported to be increasing at double-digit annual rates. Retail sales are reported to have picked up in California, especially for replacement furniture and appliances in the areas affected by the Northridge earthquake.

Tourism is strong in many parts of the District. Strong gains are reported in eastern Oregon. The Portland airport reports a 16 percent increase in passenger traffic in the first four months of the year from a year earlier. Tourism is reported to be rebounding in Hawaii, giving a boost to retail sales.

The demand for telecommunication services in California is reported to be strengthening slowly. Cellular subscriptions in the Pacific Northwest are reported to be increasing at a substantially accelerated pace. In Idaho, computer programmers are earning higher wages as the growth in demand outstrips the increase in supply.

Manufacturing

District manufacturing activity is reported mixed. Commercial aircraft activity in the District is reported stable as manufacturers await the certification of Boeing's new 777. One aircraft parts supplier noted a pickup in sales to Sweden, Indonesia, and Brazil. Defense-related aerospace industries remain weak in Southern California. In Silicon Valley, the demand for executives with marketing skills is reported to be increasing as companies begin to position themselves for future growth.

Agriculture and Resource-Related Industries

Agricultural conditions generally are good. Prices are high for field crops, like wheat, cotton, and rice, as well as for vegetables, including tomatoes, beans, and peas. Lower prices are expected for almonds, walnuts, and peaches. Milk prices are expected to fall sharply by July. High cattle inventories have pushed beef prices below production costs in some areas.

Oil prices have risen, but remain relatively low. The proposal to allow Alaskan crude oil to be exported may improve prices for oil producers in California's Central Valley by reducing supplies on the West Coast. Lumber and plywood prices are reported to be firming after falling between December 1993 and mid-May. Electricity prices in the Pacific Northwest are reported lower because of the additional water being spilled over the dams in the area to help the salmon run.

Real Estate and Construction

Real estate markets generally remain strong, but residential activity in many parts of the District slowed somewhat in May in response to rising interest rates. Home sales are reported to have slowed recently from the strong pace of March and April in the Pacific Northwest, parts of Northern California, and parts of Arizona, although the Tucson market remains strong. Sales in the intermountain states remain brisk, and May home sales in Hawaii are reported up 31 percent from April and up 67 percent from a year earlier. Home prices are reported up in the Pacific Northwest, Arizona, and in the intermountain states, and prices have stabilized in California's Central Valley. In Washington, office vacancy rates have fallen and rents are up. In San Francisco, vacancy rates remain high and rents are below the costs of maintaining the buildings in some instances.

Construction activity remains strong in many parts of the District. In Arizona and the intermountain states, both residential and commercial building is reported strong, with shortages of construction materials and skilled labor reported in these areas. Residential construction is reported flat in Northern California, improving in Southern California, and down from earlier levels in the Central Valley. In Salt Lake City, the airport is expanding and several new hotels are under construction. Interest rate increases are reported to have slowed the development of affordable housing in Southern California.

Financial Institutions

Banks in the District are reported to be pursuing loans more aggressively by easing lending criteria and offering more attractive terms. Loan demand remains strong in Idaho and Utah. In Arizona, loan demand is reported to be increasing, especially for consumer credit. In California, loan demand generally remains weak, but some strengthening is noted in Northern California and in business lending in Southern California. Loan demand also is reported to be showing signs of life in Hawaii, but delinquencies remain high. Throughout the District, interest rate increases are reported to have put an end to the refinancing boom.