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CURRENT ECONOMIC CONDITIONS BY DISTRICT

Prepared for the
Federal Open Market Committee
by the staff

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SUMMARY*

Reports from the twelve Federal Reserve Districts indicate that there has been no material change in economic conditions. Output and employment appear to have leveled off after recent declines and, despite some optimism that a recovery will begin later in the year, the overall impression is that economic activity is at much the same level as the previous month. Price rises are still expected to continue, though at a lower rate, and employment to increase relatively slowly.

One reason for the lack of an immediate recovery is that consumer spending has not picked up uniformly. In most districts, consumers are still cost-conscious, responding to sales, but not willing to make new major expenditures. At best, retail sales are described as "more buoyant" (New York) and, at worst, "sluggish" (Dallas). But more common are reports that "sales are slightly ahead of last year" (St. Louis) or "reasonably good" (Kansas City).

Automobile sales in particular are not strong. In many Districts, they are disappointing and below what was expected after the settlement of the General Motors strike. Demand is concentrated in the lower-priced compact and subcompact models, and there is no expectation of a boom year for new car sales in 1971. Only in the Richmond and St. Louis Districts are sharp increases reported and, in the former case, the increase is a recovery from the strike-induced slump.

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*Prepared at the Federal Reserve Bank of San Francisco.

The lack of strong demand is reflected in automobile production. General Motors has reduced overtime schedules and the other automobile producers are operating at reduced levels.

Manufacturing shows no sign of a general recovery. There are industries which report a rise in output (containers, furniture, steel, some machine tools, and textiles), but other industries are still retrenching. Although major layoffs of workers are occurring less often, companies are continuing to reduce their workforces through attrition or unpaid holidays. Increased hiring is still not widespread. Investment plans similarly are restrained and expenditures on capital equipment in 1971 are expected to be at about the same level as last year.

Even rising new orders for steel are not a reflection of an upturn in the economy but rather represent hedging against either a steel strike or further price rises. According to steel industry economists, overall production for this year will not be above last year.

There is one sector which has favorable prospects for recovery. The demand for residential housing is picking up and sales of existing houses are increasing. Nonresidential construction is not as strong at the moment, and in many areas it is quite weak. But the net effect is to increase demand for the output of the building-materials industries and timber. In the San Francisco District, companies in these industries are already beginning to expand production and make heavier capital expenditures. An important factor in this expected recovery is the fall in mortgage rates.

The lower mortgage rates are part of the general decline of interest rates. Nevertheless, the slow-pace of overall economic activity has meant that demand, particularly the demand for business loans, has not responded to the lower rates. Banks are continuing to lower the rates they pay for funds. CD rates have already fallen in line with other market rates, and many banks are not looking for time deposits. Rates have been cut on savings-type certificates in such Districts as Philadelphia, Atlanta, and San Francisco; in the Chicago District sales of these certificates have been restricted or eliminated. There is pressure on passbook savings rates and some bankers advocate the lowering of rate ceilings for savings accounts.

Wage increases are still common and retail prices are continuing to creep up. But there are reports of price cuts (nonferrous metals, for example), and price shading (plastics, some oil products, and transformers), while other prices are higher (building materials and farm products).

Forecasts for the coming year of business and academic economists reported by Cleveland and Boston are for a GNP below that forecast by the Council of Economic Advisers. The CEA has forecast a GNP of $1,065 billion for 1971; the other forecasts reported were $1,045 billion by Cleveland and $1,047 billion by Boston. The economists' view on unemployment were also more pessimistic than those of CEA. The general view of bankers and businessmen is that rising prices will continue to be a problem for the rest of the year without much easing of wage pressures or any major increase in employment.

FIRST DISTRICT - BOSTON

First District business conditions show no material change from last month, with the hoped-for stimulus from auto sales and other retail areas failing to materialize. The commercial banking sector continues to log excellent deposit flows, as do thrift institutions in most areas. Residential mortgage rates have fallen further, in some cases by large amounts. Our academic respondents seem a bit less pessimistic than in December.

Reports of strong consumer response to January sales constitute the one bright spot on the retail scene. This is entirely consistent with the pronounced consumer cost consciousness which has been reported since last fall. Auto dealers have felt the same phenomenon, with very high proportions of their sales activity concentrated in the compact and subcompact classes. Intermediate and luxury class auto sales have run well below expectations following the conclusion of the GM strike, and dealers seem split as to whether they are up against a generally poor year or merely feeling unusual seasonal effects.

To date, improving mortgage conditions seem to have provided impetus mainly to sales of existing homes. Further mortgage rate cuts seem likely, however, and mortgage lenders generally expect a strong surge in new home activity with the spring. Declining mortgage yields have already led several area thrift institutions to drop their 6 percent savings certificates, and more are expected to follow.

While noting his general satisfaction with the proposed Federal budget for fiscal year 1972, Professor Wallich expressed concern over the Administration's $1,065 billion GNP estimated for 1971. He suggested that it cannot be taken seriously and that, lest it be allowed to influence current policy, its origins within the CEA should be explored.

Professor Eckstein now reports an upward revision in the DRI forecast for 1971 to $1,047 billion. The adjustment was made largely on the basis of recent improvements in housing starts and retail sales, as well as continuing monetary ease and declining interest rate levels. The unemployment path commensurate with the $1,047 billion projection shows 5.9 percent for year-end 1971 and 5.4 percent at the close of 1972. Eckstein made a strong plea for continuing the current monetary stance, resisting any tendency to reduce the stimulus in response to recent signs of recovery and continuing signs of rapid inflation.

Professor Tobin expressed the view that the burden of achieving economic expansion over the next 18 months should properly fall on monetary, not fiscal policy. Accordingly, he feels that the System has for some time been overly cautious in its targets for credit market conditions and the aggregates. Tobin, Wallich and Eckstein all are expecting a reversal in the declining rate levels by mid-year as business credit demands turn round. Professor Samuelson was unavailable for comment this month.

SECOND DISTRICT - NEW YORK

Opinions expressed by the directors of the New York Bank and of the Buffalo Branch and other business leaders point to a significantly more buoyant retail sales picture and, on balance, a continued favorable outlook for residential construction. At the same time, most respondents looked for little or no immediate improvement in the unemployment situation nor for any easing of wage and price pressures.

Sentiments expressed by most respondents regarding consumer spending were noticeably more optimisitic than a month ago. The consensus was that the spurt in sales in the pre-Christmas week, and the continued favorable retail sales picture in January, might well signal the long-awaited improvement in consumers' attitudes. A typical opinion was expressed by the chairman of the board of a large New York City bank, with close contacts with several large retail firms, who saw a decidedly optimistic turn in outlook just before Christmas and into January. However, several directors of the Buffalo Branch were less optimistic regarding automobile sales, reporting that most auto dealers in their area were experiencing less business than had been anticipated with the settlement of the General Motors strike. One of the Buffalo directors felt that the high rate of savings in the recent past, together with declining consumer debt could well set the stage for a sharp rise in auto sales within the next few months.

Most respondents were generally optimistic about the outlook for residential housing construction. Several of the directors referred to the increased availability of mortgage funds available at lower rates at banks, insurance companies and other financial institutions. Several of the directors at both the New York Bank and the Buffalo Branch, however, noted that the high cost of land and other construction costs could inhibit increased residential construction.

While mixed, opinions regarding the unemployment picture on balance were relatively pessimistic. The chairman of the board of a large manufacturing concern felt unemployment would rise further, while similar feelings were expressed by an upstate banker and the president of another large manufacturing concern. The Rochester businessman reported that unemployment in that city was rising, and that the largest firm in the area was making its employees take one day off without pay a month and was considering ordering additional time off. An upstate banker, on the other hand, expected some improvement in the spring. Another director reported a trend toward less severe layoffs in airlines, electronics, computer-related industries, and light manufacturing, with many job cutbacks accomplished through attrition rather than actual layoffs.

The directors of the Buffalo Branch generally felt that unemployment had peaked, but they did not look for any dramatic improvement over the next few months.

The directors and other business leaders continued to show concern over the wage and price situation. None of the respondents saw evidence of an easing of wage pressures. The chairman of the board of a large New York state utility corporation expressed the feeling that until union leaders can be convinced inflation will actually slow, it will be difficult to get them to reduce their demands. The real purchasing power of workers has barely held even over the last 2 1/2 years, he noted, placing sustained pressure on union leaders to seek higher wage settlements. Most of the respondents saw no signs of price shading. The chairman of the board of the large manufacturing concern did report that while he knew of no appreciable price reductions in the industries with which he was familiar, he heard talk about such cuts elsewhere. Another leading businessman, a director, thought that the only area where price pressures might ease was raw materials.

THIRD DISTRICT - PHILADELPHIA

Business activity is accelerating in the Third District. Although expectations about future expansion in the economy are in a state of fragile optimism, retailers report that January was a good month, and they are hopeful about February. Manufacturers report improved business in January as well, and they too are cautiously optimistic about the coming months. Industrialists believe that more liberal depreciation allowances will give plant and equipment spending a boost. But, for the near term at least, business will hold the line on hiring. Loan demand at banks continues weak; also bankers remain concerned about the quality of loans in their portfolios.

Philadelphia department stores report that the good Christmas performance continued through January. Sales remain above last year even after adjusting for price increases. Demand is mixed across merchandising lines, however, "where customers see good values, they're buying," as one retailer put it. Sales clearance items such as women's coats, pant suits, and men's shirts, suits, and accessories are moving well; whereas furniture and other big ticket items remain weak. The test of consumer strength will come in February, one large retailer says. His reasoning is that post-holiday sales will be over and the new spring merchandise will be on display. If the newly stocked goods sell well, there is room for optimism. In the meantime, area retailers are keeping a sharp eye on inventories and holding new orders to a minimum.

Manufacturing activity in the Third District is still distorted by the aftermath of the General Motors strike. New orders and sales were up substantially in January. Looking beyond the strike make-up period, however, area manufacturers are cautiously optimistic that a mild upward turn in the economy is in prospect.

All of the directors with industrial connections agree that the recent changes in depreciation allowances will stimulate business investment, particularly for new equipment. One director with wide contacts in the industrial world says there is confusion about when the new depreciation rule will go into effect. The upcoming Treasury hearing of the new changes is causing some uncertainty, he says. But once the confusion is gone and the rule change becomes firm, he believes that investment outlays will be stimulated beginning about six months later.

Although the area business community is mildly optimistic about an economic pickup, they plan to hold the line on the number of employees at least for the near term. By mid-year, however, about one-third of the manufacturers we contacted indicated that some hiring may be taking place.

Several directors used the word "sober" to describe the general mood of people in their respective area. Rising unemployment and prices are making consumers cautious, say these directors. One director says that unless this sober psychology is altered, he does not believe that the pickup in the economy will be substantial.

At banks, loan demand remains flat. Also there continues to be a big concern about the quality of loans. Bankers report that they are going out of the savings certificate business. One country banker, for example, says that his bank no longer issues 5 1/2 or 5 3/4 percent certificates. He says he has not faced the renewal problem yet because these certificates have not started maturing. He is not sure yet how he will handle renewals when they arise.

FOURTH DISTRICT - CLEVELAND

This report is based on information obtained from about 40 economists who attended a regular meeting of the Fourth District business economists' round table held at the Federal Reserve Bank of Cleveland on January 29, 1971. In general, these economists have a considerably less optimistic outlook for the economy in 1971 than that contained in the recently released forecast of the Council of Economic Advisers.

The median forecast of the group was for a GNP of $1,045 billion in 1971, with a year-to-year gain of 4.2 percent in the price deflator and only 2.7 percent in real GNP. Views on the unemployment situation were generally pessimistic. With real GNP projected to rise 4.4 percent from the fourth quarter of 1970 to the fourth quarter of 1971, and with above-average gains expected in the labor force and productivity, most of the economists felt there would be little or no reduction in the unemployment rate by year end.

On the other hand, some members of the group expressed the view that the decline in consumer confidence has bottomed out, and that there was a favorable change in the climate for consumer spending toward the end of the fourth quarter of last year. New car sales are not expected to reach boom proportions in 1971, however, particularly after allowance for the recoupment of strike-induced losses during 1970. The median forecast of new car sales in 1971 (submitted by ten economists associated with the automotive, steel, and rubber industries) calls for domestic sales of 8.6 million units and imports of 1.2 million units. Auto production is expected to level off in February at roughly an 8.5 million annual rate and to continue at that rate through the second quarter. It was noted that part of the rebound in auto sales during the current quarter would be reflected in the producers' durable goods component of GNP as a result of the postponement of fleet car purchases and the shortage of GM trucks in the fourth quarter.

The three steel industry economists attending the meeting were not enthusiastic about the outlook for their industry. New orders for steel are up sharply (one major company said its orders were running 50 percent above the level of two or three months ago), but production for 1971 as a whole is expected to be virtually unchanged from last year. Price-hedging, in addition to strike-hedging, is now considered to be an important factor accentuating steel shipments during the first seven months of this year. Among the unfavorable developments reported was the expectation that the net trade deficit in steel is projected to widen from 6.6 million tons in 1970 to 13.3 million tons in 1971. The consensus of the steel industry economists was that if there is a steel strike, inventories held by steel consumers would last about two months. It would take a strike of at least three months before other industries would be seriously affected. If there is no strike, the liquidation of excess steel inventories would probably extend into the first quarter of next year.

With respect to capital goods, the business economists generally expect current dollar expenditures to remain flat during the first half of 1971 and to begin a modest recovery in the second half. One favorable straw in the wind was noted by an economist from a major machine tool company in Cleveland. He seemed to draw some encouragement from the fact that in January his company's new orders for metal cutting tools were about 25 percent above the extremely depressed rate of the fourth quarter.

Economists from several large commercial banks who attended the meeting mentioned that despite the recent sharp decline in short-term interest rates and the reductions in the prime rate, many banks had not relaxed compensating balance requirements in an attempt to increase business loan activity. According to these economists, big banks do not get "political mileage" out of reductions in compensating balance requirements.

FIFTH DISTRICT - RICHMOND

Surveys of businessmen and bankers in the Fifth District indicate general agreement on the following points: (1) Continuing weakness in the manufacturing sector in shipments, volume of new orders, and backlogs of orders; (2) Considerable post-holiday strength in retail sales including automobiles: (3) A weak but slightly improved employment situation; (4) Continuing evidence of price cuts in manufacturing, but not in retail trade and services; (5) A gradual slight improvement in residential construction; (6) Continued very weak loan demand at District banks; (7) An optimistic but somewhat guarded outlook for future business conditions.

District manufacturers report on balance that shipments, new orders, and backlogs of orders continued weak during the first month of the new year. Reports of weakness in such industries as chemicals, synthetic fibers, electrical equipment and nonferrous metals continue, while some improvement is noted in containers, furniture, and hosiery.

District bankers and businessmen in trade and services report that retail sales are continuing on the high side in their respective areas, following a good holiday season for retailers. Further improvement in automobile sales is also reported, particularly in relation to the severe slump of the last three months that was associated with the automobile strike.

Manufacturers' inventories are reported to have increased again in January while retailers report no recent change. Retailers' inventories were brought down considerably in December.

Respondents in manufacturing and District bankers continue to report on balance that employment is down, but reports of further decline are less numerous than during the final quarter of last year. Businessmen in trade and services report no change in employment in January.

District bankers report that available labor supplies in their respective areas remain high, and in the manufacturing sector, the length of the workweek continues down. Some prolonged strikes in the District account in part for the continuing weakness in the employment situation. Evidence of further deterioration which was present last fall, however, has decidedly waned.

The improvement in prices noted in the last two surveys by District manufacturers is apparently continuing. Some producers in nonferrous metals and hoisery report price cuts, and for the third consecutive month, reports of price increases are outnumbered by reports of declines. Businessmen in retail trade and services, however, report that prices are continuing to climb. Respondents across the board report that upward pressure on wages remains strong.

Some improvement in residential construction during January was reported by District bankers. Recovery in the residential building field, however, is not yet vigorous. Comments received from respondents indicate that considerable further increases can be expected in the months ahead, but thus far some evidence of weakness remains. Nonresidential building, which had been on the increase in the District since last August, was reported to be lower in January.

Business loan demand, which was reported down substantially in December, remains very weak according to District bankers. Mortgage loan demand is reported unchanged, following a sharp drop in December, and consumer loan demand is reported down after a December increase. According to banking respondents, loan demand in general is weaker than at any time during the second half of 1970.

Although sentiments are mixed, the general outlook of survey respondents remains favorable. The proportion of respondents expecting further improvement in economic conditions continues to be a majority. Although the outlook is favorable, a notable lack of enthusiam concerning future conditions is evident in the reports of respondents. Manufacturers in the District continue to be plagued with inventory problems and they show little inclination toward a resumption of spending for new plant and equipment. While District retailers were apparently satisfied with the sales of the recent holiday season, they also remain cautious but basically optimistic in their outlook.

SIXTH DISTRICT - ATLANTA

We recently surveyed a group of leading businessmen and bankers throughout the Sixth District about price shading and other topics. Six months ago, the identical group was questioned on similar topics. By comparison, attitudes toward economic prospects are slightly improved over six months earlier. Increases in manufacturing operations are now slightly more numerous, and there are fewer instances of cuts in capital expenditures. Rates on small CD's and savings accounts either have been lowered or probably will be shortly. On the other hand, price rises by suppliers continue to be numerous, price shading has not significantly increased, and business entrenchment remains widespread. Most of those questioned report that investment--residential construction excepted--will not be affected in the near future, if long-term rates come down further.

In our most recent questionnaire, several businessmen cited instances of price shading, but there was little increase in this practice. Specifically, selling below list prices was reported in transformers, copper cable, aluminum fabricated products, and plastics. A respondent in the metal fabricating business indicated that many producers and most distributors were selling below list prices. An oil business executive claimed that discounts of 8 to 10 percent were common.

As was the case with the earlier questionnaire, nearly all respondents cited price increases by suppliers. However, a feed producer said suppliers did not raise prices this January as they had a year ago. A steady and substantial increase in building material prices was noted.

According to those questioned, business entrenchment is still common. Failure to replace production workers and salaried employees leaving through attrition is evidently widespread.

Increases in manufacturing operations were reported in: paper products, meat packing, textiles (double knits, sport denim, corduroys, yarns), and apparel (low-priced suits). As a result of recent oil leases, there has been an increase in the demand for boats used by the offshore drilling industry. A businessman in the materials handling line reported a flood of inquiries in the past 30 days, which would indicate a substantial increase in the level of operations in that business shortly.

In the questionnaire six months ago, attitudes toward economic prospects varied widely, with about an equal division between those expecting an upturn in the near future and those seeing recovery delayed until the winter and next spring. In the latest questionnaire, most respondents were somewhat more optimistic in their outlook.

The majority of the bankers answering the questionnaire indicated that rates on small CD's and savings accounts had either been reduced recently or would be in the near future.

Information received from other sources shows the following consensus about wage and price guidelines among 16 leading businessmen in the Tampa area: Guidelines are impractical; Wage increases are the main source of inflation; Neither The White House nor Congress can or will clamp down on labor unions; And a reduction in government spending would have a favorable effect on reducing the inflationary spiral.

SEVENTH DISTRICT - CHICAGO

Most businessmen, lenders, and economic analysts in the Seventh District expect a gradual rise in general activity throughout 1971. But it is impossible to disentangle individual views from the conclusion of "experts" now publicized, more widely than ever before, in newspapers, periodicals, and on television. Many decision makers respond favorably to the general idea of an "incomes policy," but their statements usually are so vague as to be classified as gibberish.

Prices and terms of trade in the wholesale markets reflect increasingly competitive conditions. If these trends are also present at the retail level, it is through special sales and promotions, not readily subject to measurement. Announcements of price increases are less frequent than a year ago and announcements of decreases are more frequent. Delivery times are shorter, order backlogs are lower. Continued large increases in worker compensation, however, convince many manufacturers that further price increases for their products are essential. Reductions, or slower than expected growth, in volume relative to capacity also are offered as arguments for higher prices. This is particularly evident in public transportation and regulated public utilities.

Overall employment in this area appears to have stabilized. Unemployment probably is continuing to rise, but at a slower rate. Help-wanted ads are about 50 percent below the year earlier level in the Chicago area. Response to such ads is extremely heavy compared with any period of the past several years. Unemployment among people of long experience, and those with professional and executive experience, is probably the most widespread since the 1930's. This situation is related to cost-cutting efforts aimed at reversing declines in profit margins. Employees of divisions of conglomerates are especially vulnerable.

Scattered evidence suggests that the improvement in most types of retail sales, which developed shortly before Christmas, continued in January. Buyers are still cautious, however, on purchases of luxuries and big ticket items.

General Motors has reduced overtime schedules because its inventories of finished cars are being rebuilt rapidly. Other motor vehicle producers have been operating at reduced levels in recent weeks.

The steel industry provides the most optimistic reports, currently, from any District industry. Orders for steel are said to have picked up "rapidly" in recent weeks. This development is believed to be more than a mere reflection of the prospect of a strike next August 1.

Some manufacturing firms will increase, or maintain, capital expenditures in 1971. In total, the physical volume of fixed investment by business firms, with the exception of utilities, doubtless will be lower. New commercial building projects are much less frequent than a year ago.

Prices of meat are expected to remain firm, following declines in 1970. Prices of farmland in the District turned up in the fourth quarter after two years of decline. Greater availability of credit may have produced this result in the face of declining net farm income.

Rural banks are now more interested in real estate loans. These banks always are slow in following general trends. Recently, they have cut rates on feeder cattle loans.

All savings associations we know of have reduced rates on mortgage loans once or more in the past month or two, with total reductions averaging about one half of one percentage point. Further rate reductions are expected. Relatively few of these institutions have lowered down payments, reduced fees, lengthened maturities, or eased credit standards.

Business loan demand at commercial banks continues very slow, but some institutions think the trend has firmed recently. Not only have rates been cut substantially on large CDs, but there is no interest in obtaining funds through this route. Some banks have eliminated or restricted sales of consumer CDs. Some smaller banks would like to see the board reduce the ceiling rate on passbook savings.

EIGHTH DISTRICT - ST. LOUIS

The slight increase in optimism reported last month by businessmen in the Eighth Federal Reserve District continues to prevail. Retail sales, which picked up seasonally just prior to Christmas, are still slightly ahead of this time last year. The labor picture remains unchanged in the absence of strikes. Firms interviewed report that belt-tightening plans have been completed. Some capital spending plans are slightly higher than last year, but these tend to be the exception. Homebuilding continues to exceed year-earlier levels, and prospects for this activity in the future are good.

Most respondents engaged in retail sales indicate that their business is better than during the autumn months. Some automobile dealers report sharp increases in new car sales. Although overall sales improvement has not led to major changes in inventories or plant size, retailers generally feel that a moderate upswing is underway. Prices are expected to continue up, however, reflecting high wage settlements and rigidities in the labor market.

No major improvement in the unemployment picture is anticipated in the near future. Respondents reported no employment expansion plans, but some indicate that the workweek may be lengthened.

Although one large firm reports a capital budget that is higher this year than last, the increase is due to long-term commitments rather than to any additional optimism based on recent sales or other factors. Most firms are still wary of plant expansion, and in the St. Louis area the number of new plant inquiries is still down from the corresponding period in the previous year.

The picture remains bright with respect to homebuilding. Building permits issued in suburban St. Louis are currently running more than double those of a year ago. Traffic of homeseekers has improved as more people are actively shopping for houses. The major drawback in the industry is the increased cost of housing due to rising input prices, especially labor costs. The directors of one branch of this Bank noted that labor costs constitute 50 percent of total housing costs. Whereas the corresponding proportion in automobile manufacturing is only 25 percent. This factor is pricing some people out of the market despite the lower mortgage rates now available. One respondent felt that this may be a hindrance in meeting the President's announced goal of 2.6 million new housing units in 1971.

District banks had an above average increase in profits in 1970. Loan demand, however, is not increasing, while deposits are rising slowly, and rates paid on passbook and other savings-type deposits are generally unchanged. Thus the outlook for banking in 1971 is for a substantial decline of the margin between the cost of funds and the rates on bank assets. Some banks report that although net income may be maintained at current levels, any expansion in net income will definitely be less than the average rate of recent years.

The agricultural situation is characterized as "dreary." Losses and late harvesting of field crops are reported to be cutting returns in this sector. Prices of some crops are said to be satisfactory, but the volume of sales is disappointing. Despite the dissatisfaction, however, farm cash receipts remain above corresponding levels of a year ago in most Eighth District states.

NINTH DISTRICT - MINNEAPOLIS

Business loan rates at Ninth District commercial banks have tended to slip more noticeably than consumer loan rates in recent weeks. At the same time, rates offered on consumer savings deposits have held steady while rates for large CDs have dropped precipitously; some banks have even stopped trying to attract large CDs. Liberalized depreciation rules, which were announced by the Treasury, are expected to have only a minimal impact on District manufacturing firms. There is no consensus among District community leaders regarding the current stance of monetary policy. Some people feel the Fed has moved too far too quickly on the side of ease while others prefer to see even lower interest rates.

To our knowledge, most major banks in the District have now reduced their prime rates to 6 percent, but other loan rates have not fallen accordingly. Loan rates to less-than-prime business customers have edged down in the wake of prime rate cuts, but reductions have been less than proportional. One reason given for this was that these rates did not rise as fast as the prime rate and, as a result, would probably not fall as fast. In addition, one director felt that even though there was money available, banks were still trying to maintain their rates and reducing them only to their low risk, old customers. One South Dakota director felt, however, that production credit associations are giving banks stiff competition, and that banks will have to reduce their rates sooner than they would like. In general, mortgage interest rates are slipping in the District, although rate levels still seem to be slightly higher than those in some sections of the country. The one exception to this is in South Dakota where one S&L quoted a rate of 7 percent on "real prime property." Consumer loan rates have slipped a little, but in the words of one bank director, "usury ceilings stopped them from going up, so consumer loan rates will be slower in coming down." Another director said that consumer loan rates in his area have not fallen because rates being offered for savings have not softened.

Commercial banks in the District are competing less vigorously for large CDs, and there are a few instances where banks are not even accepting large CDs. Rates on consumer savings deposits, however, have not shaded, although the banks and S&Ls would probably like to see them soften. One bank director from outside the Twin Cities said that savings rates in his area have not fallen, but that banks are constantly watching developments in Chicago and Minneapolis. An S&L officer also stated that his S&L would like to offer lower rates but is afraid that savers would move their funds to those institutions which would pay higher rates. To him, the only logical solution to the dilemma is for the FHLBB and FRB to lower ceiling rates on savings deposits.

The liberalized depreciation rules announced by the Treasury are not expected to significantly change District manufacturers' capital spending plans this year for at least three reasons. First, District manufacturers are not large enough to notice any significant changes in their cash flows as a result of the new rules. Second, the lag between planning and expenditures is such that manufacturers cannot immediately take advantage of the new rules. Third, manufacturers are already concerned about excess capacity. One director, however, thought that highway contractors are taking advantage of the new ruling, because in the long run liberalized depreciation rules turn out to be the difference between buying new equipment more cheaply and purchasing used machinery. Another director was aware of one case where the new rules will have a significant change on cash flows, but he thought it would not have a large effect on the company's spending plans.

The directors of the Bank were queried regarding their and other people's opinions concerning the current stance of monetary policy. Public opinion appears to be quite divergent. In general, those people who are even aware of monetary policy think that the Federal Reserve is acting "about right." The directors also are in general agreement with recent monetary policy actions although three directors voiced some doubts. Two directors wondered whether the Fed was moving too aggressively, and one of these questioned if this would not rekindle inflationary pressures later this year, especially in view of the major labor negotiations coming up. Another felt that monetary policy is too confusing and that the Fed should stay with one set of rules or another. Businessmen are confused and when this happens they become conservative in their actions.

TENTH DISTRICT - KANSAS CITY

There are indications that the economy of the Tenth District may be showing renewed strength. A growing optimism is present in some parts of the District, beyond what may be inferred from current business statistics. Reports from Head Office and Branch Directors support the evidence from the statistical indicators that construction activity and outlook is a relatively bright spot in the economy of the Tenth District. Both residential and nonresidential building are responding favorably to factors such as increasing availability of funds, improving economic conditions, and the resumption of activity following the end of the construction workers' strike in Kansas City.

The slowdown in the growth of personal income seems to have been reversed in the District as a whole, and the District unemployment rate has apparently stabilized. Of course, there are variations within the District and among different industries. For example, further layoffs have been announced for several defense-oriented establishments. In contrast, business conditions generally seem stronger in Colorado, New Mexico, and Oklahoma than in the remaining District states. Abnormally severe winter weather also has reduced the pace of economic activity in the northern section of the District. On the whole, retail activity during the Christmas season was reported to have been reasonably good--in many cases, better than earlier expected.

Strength in the value of construction contract awards is found in both the residential and nonresidential parts of the industry. Again, the northern section of the District appears to be somewhat laggard as far as construction is concerned. Some Branch Directors from Wyoming and Nebraska report that Section 235 and 236 housing is about the only kind of residential building going on in their areas. In the Omaha area, there is very little in the way of new commercial and industrial projects, only spotty interest in apartment building, and not much custom building of new single-family dwellings.

Elsewhere, construction activity is relatively strong--especially in Oklahoma, New Mexico, and Colorado. An upsurge in home building is reported for both Tulsa and Oklahoma City, and both also are experiencing a good deal of commercial construction activity. Albuquerque, too, is having an increase in both multiple-unit and single-family building, and considerable optimism is reported in business circles there--with regard to the general business outlook as well as in housing. Commercial and residential building (both single-family and multiple-unit structures) growth is vigorous in Colorado, both in Denver and in other urban centers as well. There (as elsewhere in these states), strength in housing is reported across the spectrum from smaller, less expensive single-family homes (some due to Section 235 and 236 subsidies) through higher-priced single-family dwellings to high-rise, high-price apartment buildings.

The general retrenchment of livestock prices during the last half of 1970--due primarily to the new sharp increase in hog marketings--had a pronounced impact on District farm income. Last year, cash receipts from District farm marketings--73 percent from livestock sales--increased 2.4 percent above 1969 levels, as compared with a 3 percent rise for the nation. However, third and fourth quarter receipts in the District were, respectively, 2.6 and 4.1 percent lower than in the comparable periods for 1969, with both crops and livestock contributing to the decline.

There are indications that the District livestock picture may show improvement in 1971. Recent reports point to a likely abatement of the increase in sow farrowings, compared with the levels of a year ago. Likewise, the number of cattle on feed in the District, as of January 1, was 3.9 million head--down 1 percent from 1970. For the nation, the decline was 3 percent. Marketings in the District during the October-December quarter were 11 percent higher than in the year-earlier period, while placements were down 4 percent. Hence, the production adjustments currently underway in the hog industry, together with a likely reduction in fed cattle marketings, point to higher livestock prices in the months ahead.

After declining farm prices from March to December 1970 helped to introduce some stability into the overall wholesale price index, the January 1971 increase in the WPI was spurred mostly by rises in the farm products and processed feeds components of the index. In view of the prospects for higher livestock prices, it is unlikely that declining farm prices will exert a stabilizing influence on the overall WPI in 1971.

ELEVENTH DISTRICT - DALLAS

Continued inflation appears to be the major concern of the directors of this bank. Of the ten head office and branch directors surveyed (none of whom is a commercial banker), most expect a growing economy in 1971, characterized by a resurgence in consumer spending, a further downward movement of interest rates, and continued wage and price increases. With respect to the economy of each respondent director's local area, prospects were viewed as being only fair. Some major public construction projects are planned for 1971, and it is expected that these capital outlays will require tax increases in some localities. Retail sales are anticipated to remain sluggish, and few of the respondents are planning any increase in capital expenditures. Job opportunities are expected to rise only slightly as the year progresses. All foresee higher labor costs, but few expect to make changes in present levels of employment.

With respect to the national economy, a fairly optimistic outlook apparently holds. Most directors expect renewed economic growth, largely as a result of a rise in consumer spending and an increase in the Federal budget deficit. All but one of the respondents feel that interest rates will move down further through 1971. In addition, the gap between short-term and long-term rates is anticipated to narrow somewhat as long-term rates decline relative to short-term rates. However, most expect that inflation will continue to be a problem during the remainder of the year--in fact, much more so than unemployment. And, while some feel it would be wise to institute wage and price controls, none believes that this action will be taken.

The economic outlook for most local areas is somewhat less optimistic, the directors report. A few do expect growth in their cities' budgets, as some major public construction projects are planned. However, it was mentioned that increased taxes--particularly property taxes--are likely to accompany these additional governmental expenditures. Local consumer spending is not expected to provide much strength this year, with retail sales anticipated to be about the same as in 1970. Moreover, job opportunities may improve only slightly. All are expecting rising labor costs in 1971, with some anticipating an increase of more than 10 percent. And while few think they will have to release additional employees, none mentioned a need to add to employment in 1971.

Respondents indicated that capital expenditures are also likely to remain about unchanged from last year. In fact, only a few reported increases in capital expenditures last year even though dollar sales volume rose fairly substantially. Most of the increase in dollar sales was the result of inflation, as physical-unit sales either rose only slightly or declined. Moreover, few anticipated any major change in product composition. Thus, in most cases, present plant capacity is quite adequate. However, some indicated that they may face future changes in capital equipment in relation to new anti-pollution regulations.

On the whole, the district economy continues to remain fairly strong in comparison with the rest of the nation. Retail sales were up slightly in December, but consumer spending still remains subdued. Industrial production continues strong, reflecting mainly the high level of oil activity in the District. Although oil allowables for February are down slightly, the longer-run outlook for production is bright as transportation problems caused by the shortage of world oil tankers continue to place demand on domestic sources. Unemployment in Texas rose substantially in December, but it is still significantly below the national average. In the agricultural sector of the District economy, there is some concern about the recent dry weather, which has forced supplemental feeding of livestock in some areas.

TWELFTH DISTRICT - SAN FRANCISCO

Businessmen and bankers in the Twelfth District expect little change in economic activity until later in 1971. Despite the easing of financial conditions through lower interest rates and the greater willingness of banks to lend, the demand for loans has not changed significantly. Business investment plans are cautious, and consumers, instead of increasing their spending, are increasing their saving. It is expected that activity in the housing market will increase in 1971, stimulated in part by the greater availability and lower price of mortgages.

Retail sales are not showing any signs of marked increase; in most areas they are proceeding at a moderate to slow pace. There had been a jump in sales during the ten days before Christmas, but this increase has not been sustained, and post-Christmas sales are described as disappointing. As a result, inventories are higher than desired and staffs are being reduced by some stores.

Automobile dealers in particular are finding that their sales are disappointing since 1971 models are not selling as well as expected. One factor, it seems, is that customers are reluctant to increase their indebtedness. Dealers have heavy inventories and some are complaining about manufacturers' pressures to build up stocks still more. A favorable factor is that lower interest rates have reduced the costs to dealers of carrying their inventories.

Business expectations are in line with consumer behavior. In general, businessmen are maintaining their current activities in line with their expectation of no immediate recovery in the economy. Business investment plans indicate that expenditures will be somewhat smaller than in recent years. A survey of anticipated expenditures for plant and equipment among Arizona companies found a definite shift toward caution. For 1971, only 37 percent of the firms reported they would have higher expenditures, while 35 percent reported lower spending plant. In contrast, the figures for the 1969 and 1970 surveys averaged 60 percent for increased outlays and 16 percent for lower expenditures. The Seattle-Tacoma area continues to report poor business prospects and one bank there describes local business loan demand as being at it lowest level in 24 months. A Southern California steel mill recently has made a sharp cut in its work force. In Arizona, a state which is otherwise prosperous, manufacturing employment is at its lowest level since June 1968.

The liberalized depreciation allowances, recently announced, are not expected to have any immediate impact on business spending. Most businessmen report that the change is too small to affect their decisions or that their investment plans are based on longer-run forecasts of the demand for their products.

There are some favorable trends in manufacturing. A large oil company reports that it is maintaining its planned investment in 1971 at the same $800-million record set in 1970. A major electronics firm in Oregon, which had previously announced a layoff of 1,000 employees, has reversed itself and, instead of a layoff, will only require each employee to take a 10-day, unpaid vacation before May 1. In the face of an expected increase in housing demand, building materials firms are expanding production and beginning to undertake new investment in plant. Timber mills are starting to increase output and rebuild inventories of certain product lines. Some mills which had been closed are being reopened.

Changes in housing demand are in line with these expectations. In Southern California, sales of houses are rising according to reports of local real estate firms. In Idaho and Utah, construction activity continues to expand. Overall, most of the strength has been in residential rather than nonresidential building.

Agriculture in the District has mixed trends. Fruit prices have held up well. Other crops have had large yields, but their prices are likely to fall as a result. There are also large stocks of poultry and beef on hand which make any substantial increase in livestock prices less likely.

Banks are intensifying their efforts to obtain good business loans, but no major increase is reported. Consumers seem to be willing to increase their instalment debt and the counterpart of this is an increase in savings deposits. Banks have cut their interest rates on various classes of loans in line with market trends. Several major banks have stopped accepting 5 3/4 and 5 1/2 percent consumer-type savings certificates. The maximum is now 5 percent and reductions are becoming general. There are complaints of a profit squeeze by some bankers and they hope that Regulation Q ceilings will be lowered to facilitate the movement to lower rates on all savings accounts.