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CURRENT ECONOMIC COMMENT BY DISTRICT

Prepared for the
Federal Open Market Committee
by the Staff

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SUMMARY*

According to bank reports, economic activity is improving and is expected to remain strong. Retail sales have been increasing and retailers expect Christmas spending to be heavy. Order backlogs are swelling in several areas as the tempo of manufacturing activity picks up; inventory building is also anticipated. Several districts report robust construction activity. Although problems are noted, the agricultural situation is termed "strong." Labor shortages are developing in some areas as the demand for workers strengthens. A moderate rate of inflation and continued gains in loan demand are expected during coming months.

The consumer spending outlook can be termed "favorable." Retailers in the New York district are optimistic about Christmas spending and those in the San Francisco district are looking for a 10 percent year-to-year Christmas sales gain. Recent increases in consumer spending are reported by Richmond, Chicago, Dallas and St. Louis. Automobile sales, however, are being held down by inventory shortages in several districts.

Reports disclose improved manufacturing activity. St. Louis reports gains in manufacturing sales and reveals shortages developing in the cement and paper industries. Boston indicates that several of its district manufacturers are operating at capacity. Capital good sales are expanding in the Chicago district and order backlogs are climbing. Increased inventories are planned by several Kansas City district manufacturers. Richmond reports that manufacturing shipments, new orders and backlogs are rising. In the Atlanta district plant and equipment expenditures continue to expand. The seasonally adjusted Texas industrial production index

*Prepared at the Federal Reserve Bank of Minneapolis.

experienced a sharp increase in September with all major industrial sectors advancing. Philadelphia, however, indicates some leveling off in manufacturing activity.

Richmond, Atlanta, St. Louis, and San Francisco all report strong construction activity. In the Sixth District, several major commercial projects and tourist attraction expansions are planned, and shortages of building materials are evident in some areas. Although national construction activity appears to be strong, there is vacant commercial space in Seattle, and very low commercial construction activity in St. Louis. Richmond suggests that the rate of increase in building appears to have slowed; and Dallas reports that residential and nonbuilding construction awards in the district have declined.

Agriculture continues strong. It is, however, encountering some apparently temporary difficulties in certain areas and for certain products. In the Midwest, crop damage and harvesting problems were caused by unseasonally wet weather. Recent income from tobacco sales has been disappointing in the Southeast. Prices for fattened livestock have weakened. But Minneapolis describes farmers, in general, as "cautiously optimistic" and cites strengthening loan demand for farm operating investments. Dallas concurs with the optimistic description, citing very high farm receipts, and Kansas City mentions thriving agribusiness industries.

The employment picture continues to brighten, leading to increased labor shortages in some parts of the nation. Expanding demand for labor is reported by Chicago, St. Louis, Kansas City and Dallas while New York indicates that the belt tightening period has ended and labor demand is starting to build. Labor shortages especially among skilled workmen, evidenced by increased turnover and absenteeism are reported by Chicago and St. Louis. Availability of nonunion labor, however, prevented trucking and building trade unions from pressing for large wage settlements in the Chicago district.

The outlook for wage and price increases differs, to some extent, in each district that reported on inflation. With the exception of Atlanta, where inflationary pressures remain strong, the expected rate of inflation for next year is generally termed "moderate." This assumes that some wage-price regulations continue through 1973. Farm prices should, in coming months, exert less upward pressure on consumer prices then they have recently.

There are mixed reports on both loan demands and deposit increases throughout the nation. A number of districts report relatively strong or expanding loan growth particularly in the business, mortgage, and consumer credit areas. In the San Francisco district, strong loan demand is reported for mortgage and consumer credit -- although the strength of business loans varied throughout the district. St. Louis reports expansion in business and mortgage loans while in the Dallas and Kansas City districts, business and consumer credit continues strong. The availability of funds is considered adequate in the Chicago and Boston districts with St. Louis, Philadelphia and Kansas City reporting some moderation in deposit inflows.

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FIRST DISTRICT - BOSTON

Reports from our directors indicate business is continuing to expand at a rapid pace. New orders are rising, as are expenditures for plant and equipment. A tight rein continues to be exercised over inventories, and new hiring is spotty.

New orders were generally reported up substantially in both manufacturing and commercial construction. One supplier of construction materials for prestige buildings indicates the company now has a high level of backlog work, a sharp change from six months ago. Some disappointment in the rate of new orders for can-making machinery has been expressed by two directors in this field. A supplier of white pigment, a widely used industrial material, reports orders as very strong and that this plant is working at capacity. Capacity level operation was also reported by a manufacturer of carbon black, a material used in the maufacture of tires, and by a manufacturer of specialty chemicals.

Large capital expenditures are being planned by a firm involved in putting up a liquified natural gas facility. Plant expansion is also reported under way in some sectors now operating at capacity.

A director from a large commercial bank reports there has been no recent change in business loan demand. While loans are running 19 to 20 percent over a year ago, loans outstanding have not advanced in the past six weeks. The heavy increase in loans this year mainly represents business from outside of New England. This Bank director said pressure on interest rates has subsided recently, due to a large supply of funds, a slackening of demand (the seasonal demand for funds in October did not occur) and political pressures to hold interest rates level. In effect, the banker stated, we now have rate controls.

Three academic correspondents available this month, Professors Eckstein, Samuelson, and Wallich, agreed upon a 6 percent target for monetary growth. Eckstein expected a 6 percent rate of growth in nonborrowed reserves in 1973 but preferred a 6 1/2 to 6 3/4 percent average rate. The primary danger in the current outlook, he felt, is for this rate to fall below 5 percent for several consecutive months. Wallich prescribed a 6 percent rate of growth for M1, under the assumption that velocity will be rising at a 2 to 3 percent rate. He urged the Board to undertake a study of what rate of growth of velocity can be expected to prevail in the future.

The three also agreed in their disapproval of the attempt, in Samuelson's words, to "talk interest rates down." Wallich said the current 7 1/2 percent level is too low for an economy with a 3 percent inflation rate. Granting there may be some psychological benefit in "talking down" rates, Samuelson insisted the main effect is to increase rationing. Eckstein argued it is impossible to go through an expansion without a rise in interest rates. Holding the prime rate below 6 percent would be an unfortunate, early trigger. He urged monetary authorities to reinforce the trend toward flexible rates and not to back "administered prices."

SECOND DISTRICT - NEW YORK

In the view of most of this Bank's directors and other business leaders recently contacted, the new federal revenue sharing program is likely to result in increased state and local government outlays over the near-term, rather than tax reductions. A cease-fire in Vietnam was expected to have little impact on the current business situation, since that outcome was believed to have already been largely discounted. Respondents in general were optimistic over the retail sales outlook for the Christmas season. Business hiring practices remain on the conservative side, with additions to payrolls still geared to current rather than expected future needs.

In the view of most directors, the recently enacted measure providing for substantial federal revenue sharing with state and local authorities could be expected to quickly stimulate increased outlays by these governmental units. Buffalo branch directors felt the measure would have a "bail out" effect, enabling state and local governments to meet demands from organized employee groups and other civic pressure groups. They also reported there were indications a number of localities intended to use part of the payments to undertake capital expenditures that had earlier been deferred for lack of funds. One director felt the measure would have a "substantial" spending impact that would be reinforced by the current strong cyclical rise in local taxes. Although some of the directors did not rule out the possibility that the program would lead initially to some local tax reduction -- or a moderation of increases -- the general feeling was that the lion's share of the available funds would be used to finance projects that had been postponed earlier due to a lack of funds. On the other hand, one New Jersey banker felt the revenue sharing measure would neither contribute to increased spending nor reduced taxes in the financially pressed cities in his area, but rather that a good deal of the funds would be used to liquidate outstanding debt.

Most of the directors agreed that a cease-fire in Vietnam would have little immediate impact on business and consumer spending, since that eventuality had already been discounted. A few of the directors, however, did feel such a settlement would contribute to an aura of stability by finally eliminating the major uncertainty that has adversely affected business and consumer attitudes over the past several years. The consumer sector was viewed as the area where Vietnam agreement would have its major impact.

Concerning consumer spending, respondents in general continued to express an optimistic outlook. A senior official of a New York City department store, specializing in high-priced, high-quality goods and having branches in the suburbs, reported that his firm's October sales had been "very good" and that he expected a higher level of business during this Christmas season than last year's. The chairman of the board of a Rochester department store, who previously had frequently been rather skeptical over the consumer spending picture, reported that retailers in his area were expecting holiday sales to run well ahead of a year ago. Indeed, he felt that the consumer is likely to spend a larger share of his income in the coming months. The New Jersey banker reported that retailers in his area were looking toward a good Christmas season. The Buffalo branch directors expressed views regarding the consumer spending outlook that, while varying in degree, were unanimously optimistic.

The directors were unable to detect any trend toward more aggressive hiring practices in private industry. It was, however, noted that the earlier "belt tightening" phase had come to an end and that, with the continued upswing in business activity, the need for additional employees was starting to build.

THIRD DISTRICT - PHILADELPHIA

The latest survey of business conditions in the Third District shows that some key indicators remain on the increase. New orders and sales increased at many firms responding to this month's questionnaire. More firms reported inventory increases than decreases. Outlays for plant and equipment are scheduled to increase at over one-third of the firms contacted. And many firms expect to increase their inventories within six months. In general, most area businesses remain optimistic about the future. On the darker side, however, employment opportunities are flattening out a bit in the Third District. Expectations of increased inflation within six months were reported by approximately one-third of the firms contacted.

This Bank's business survey respondents reported their manufacturing activity continued to rise, but the number of increases dropped slightly this month. The vast majority of firms completing the survey's monthly questionnaire report either no change or an increase in their new orders, new shipments and the length of their delivery time. However, a small but growing number do report decreases in orders received, shipments and delivery times.

Employment opportunities in the area have leveled off somewhat. Over half of the firms responding to the business survey expect no change in the number of employees or the average number of hours worked during the next six months. Of those firms which are changing their employment schedules, increases predominate on the six month planning horizon. On the one month planning horizon, as many firms reported increases as reported decreases.

About half of the responding firms report no plans to change the size of their inventories for at least six months. However, of those firms which do anticipate inventory adjustments, twice as many foresee increases as decreases.

Plant and equipment spending plans remain at the slightly higher level reached last month. The majority of firms are evenly divided between those undertaking investment increases and those anticipating no change in their present capital expenditure rate. Very few firms are cutting their investments in plant and equipment.

Most businessmen responding to this Bank's survey expect to pay and receive the same prices next month as they do now. However, a large minority do foresee rising prices on the six month horizon. This is essentially the same price outlook reported last month.

Area banks report little or no growth in their demand and time deposits. Business loan demand is good from small firms but large national businesses are hardly borrowing at all. This holds back growth in the overall business loan category. Consumer and mortgage loans are expanding in the Third District again this month.

FOURTH DISTRICT - CLEVELAND

The thrust of recent statistical evidence and information received from economists, businessmen and directors indicates that economic expansion is continuing at a strong pace in the district with few signs of weakness. The manufacturing sector appears to be gaining momentum, and the near-term outlook remains good. Signs of strength are broadly based, including improved orders and sales in defense and producers' goods and particularly high levels of activity in consumer-related areas. Our directors continue to be optimistic about the prospects for business next year. In addition, there is sentiment among our board members for continuation of the controls program in view of the crucial labor contracts up for renegotiation in 1973. Bankers are experiencing strong loan demand, especially from consumers.

Some of the principal economic indicators that describe the continued expansion in activity in the district are: the unemployment rate, which has continued to edge down; payroll employment, which has shown strong gains in recent months (particularly in durable goods manufacturing); our electric power indexes of manufacturing activity, which began to post new highs during the past few months for all major metropolitan areas of the district (after having recouped losses incurred during the past recession); and residential construction contracts, which remained close to a record high in August and September. Nonresidential building, however, still appears to be sluggish. Our most recent survey of district manufacturers shows evidence of strengthening in the pace of the recovery. Key indicators, such as new orders, shipments, backlogs, employment, and the workweek, registered solid gains in October, and firms expect business conditions to be even stronger in November. Our survey also indicates that prices continue to be held reasonably well in check, with the diffusion index for prices paid having hovered around the 60 percent level since February.

The strong tone of business conditions in the district is also apparent from comments from our directors. Industrialists associated with consumer-related activities reported excellent business conditions in areas such as automotive parts, paints, glass and rubber. Capital goods producers indicated defense-related business is improving in several firms. A director in the machine tool business reported that new orders were up 50 percent from a year ago, and that his firm, along with others in the machine tool industry, is experiencing difficulty in rehiring the skilled workers they had to lay off when business was poor. On the other hand, several directors whose firms are experiencing sizable increases in orders plan to meet the rising demand without significantly expanding employment. Office equipment business continues to be excellent, and backlogs are rising. Several directors whose firms have had a significant recovery in business reported that total profits had increased, but that profit margins were comfortably under the ceilings of the control program. An exception to the favorable business reports from our directors was the remarks from one director who noted that his firm's specialty construction business, which is almost entirely related to the steel industry, has been poor this year; he expects the steel industry to increase construction spending next year, however.

Some directors are quite concerned about a possible reemergence of inflationary pressures in 1973. Although the directors were beginning to note some complaints among industrialists because of what were described as unfair rulings of the Price Commission, a number of them seemed to favor continuation of wage-price controls in 1973. The directors were particularly concerned over the implications for wage increases and strike activity if the controls were to be dropped in the face of forthcoming labor negotiations.

Banking directors reported strong loan demand, especially from consumers, and increasing demand and time deposits. One director from a large reserve city bank, however, noted that the savings and loan institutions in his area were receiving a disproportionate share of the increased savings flow.

FIFTH DISTRICT - RICHMOND

Reports from businessmen and bankers indicate further business expansion in the Fifth District. Manufacturers report sharp increases in shipments, new orders and backlogs. Retail sales remain strong, although delivery problems have apparently dampened automobile sales somewhat. Reports fail to show any sign of an inventory buildup on the part of district firms. Improvements in employment and hours worked per week were reported. Prices received remained relatively stable while wages generally increased. Construction activity remains strong and a general mood of optimism prevails in the district's business community.

There was a sharp rise in the number of manufacturers reporting increases in shipments, new orders and backlogs. Widespread increases were reported by producers of steel, textiles, furniture and chemicals. Some producers are apparently experiencing a delay in shipments because of a shortage of box cards. In our latest survey the number of manufacturing respondents reporting higher than desired inventory levels declined substantially, although a sizable number continue to view inventories as on the high side.

Following a slight decline last month, manufacturing employment appears to have improved somewhat in the current period. Manufacturers in our latest survey report increases in both employment and hours worked and banker respondents indicate general employment gains in their areas. Prices received by manufacturing are reported to have remained relatively stable but both manufacturers and retailers indicate fairly widespread recent increases in wages.

Trade respondents report further improvement in general retail sales, with all geographic areas of the district now sharing in the improvement. However, the number of respondents indicating an increase in automobile sales declined over the previous reporting period. Several respondents referred to delivery and inventory problems, which have apparently dampened sales of domestic models.

Loan demand continues to show strength although the rate of increase in the demand for consumer and mortgage loans slowed somewhat over the previous reporting period. Even so, more than 50 percent of the banking respondents reported an increase in the demand for all types of loans.

The pace of advance in the construction sector may have slowed somewhat in recent weeks although both residential and commercial building continue strong. In our previous survey 50 percent of the banking respondents indicated that construction activity in their areas had increases whereas in the most recent month only 25 percent reported increases.

The situation in district agriculture is little changed since our last report. Weaker demand, declining prices, and poorer quality offerings have marked flue-cured tobacco sales during the past several weeks.

The mood of businessmen and bankers in the Fifth District remains distinctly optimistic. The majority of the banking respondents expect further improvement in business activity in their areas in the immediate future. Several bankers reported growth and optimism among their customers.

SIXTH DISTRICT - ATLANTA

According to reports of businessmen and bankers, the region's economy continues extremely prosperous and the outlook is optimistic. The number of new plant announcements has increased. Construction continues at a hectic pace. There are scattered reports of building material shortages. Inflationary pressures continue.

A pickup in announcements of new plants and plant expansions that began earlier this year continues. It was recently announced that four synthetic gas plants will be built in Louisiana by 1975. One of the plants, representing an investment of nearly $350 million, will be the largest such plant in the nation. The other three plants will cost about $160 million each. An $80 million fertilizer plant will be built near Tampa. A $60 million expansion is slated for a paper mill in north Alabama, and a $15 million weaving plant is planned for southwest Alabama. Western Electric will build a $5 million plant in Montgomery. An aircraft assembly plant in Tampa has been reopened to make subassemblies for small two-engine planes. In addition, there have been a number of announcements of smaller plants or expansions. However, 550 jobs will be lost in the Birmingham area because two firms are phasing out pig-iron production. Reasons mentioned for this action include foreign competition, pollution problems and rising cost of furnace repairs, freight and raw materials.

Three large residential communities have recently been announced -- one near Atlanta, one on lakefront property near New Orleans and one in south Florida. Florida's residential construction boom may eventually be slowed by a pollution board ban on new permits in areas with inadequate sewer treatment. However, effects will not be felt for at least several months because builders have large backlogs of permits. There is a growing cement shortage in Florida, with no relief in sight. A shortage of building materials is also reported in Tennessee. In addition, a retail food chain executive reports a shortage of refrigeration equipment is delaying the opening of seven new stores.

Construction will begin soon on a new plaza in downtown Jackson, Mississippi. A 22-story bank building and adjoining hotel will highlight the plaza. A seven-building warehouse complex has also been announced for Jackson. A 200-room motel will be built near Busch Gardens in Tampa. Three motels totaling over 300 rooms have been announced for Alexandria, Louisiana. A multimillion dollar "Holy Land U.S.A." tourist attraction is planned on a parcel of land between Mobile and Pensacola. Both Disney World and Opryland are planning major expansions. Ground will be broken before the end of the year for a $20 million hospital-medical complex near Pensacola.

Inflationary pressures remain. An executive of a large airline company says that industry is ready to lead a new round of inflation if controls are lifted. A retail food chain official claims his industry could increase prices 7 to 9 percent and still not see the return of reasonable profit margins. TVA is expected to increase power rates in the first half of 1973. A steel company executive claims environmental controls alone may push up the price of steel at a rate of 4.6 percent per year.

SEVENTH DISTRICT - CHICAGO

Business sentiment has improved further in the past month. Labor markets are tightening; retail trade is strong; order backlogs are building in many industries and lead times on new orders are lengthening. The upswing in capital goods appears to be gathering steam and is spreading to a broader base. More firms are planning on the general business expansion to continue quarter-by-quarter through 1973, with no significant slowdown in the second half. Soybean and possibly corn harvests will be reduced by adverse weather conditions.

More firms are finding skilled workers in short supply and shortages of suitable trainees are reported. Labor turnover and absenteeism rates have increased, but remain below the high rates of the late 1960s. A larger volume of want ads and a steady reduction in claims for unemployment compensation also suggest a stronger demand for workers. Nevertheless, unions in some sectors, e.g., building trades and trucking, are not pressing for large settlements. They fear further losses of jobs to nonunion operators.

Retailers are pleased with recent sales levels, especially of seasonal merchandise, such as apparel and sporting goods. Color television output schedules have been increased again. Output of some household appliances was reduced in September and October, but sales since then have been somewhat in excess of expectations and inventories have declined.

Trucks continue to lead the general expansion in capital goods. Producers of engines and rear axles for heavy trucks are working three shifts a day, seven days a week. Capacity restraints are limiting sales of most types of trucks. Some orders are being booked for delivery next

March and April. Most truck producers are in the midst of programs to expand production.

Auto sales would be appreciably higher if inventories were adequate. Output has been hampered by a series of "quickie" strikes over working conditions. The union treasury is depleted, and strike benefits are not paid for work stoppages that last less than a week. Perhaps more important than strikes in holding down output are the problems producers have been having making body panels of new models fit together properly.

Many firms are reporting slower deliveries from vendors. Half of the Chicago and Milwaukee purchasing agents report higher backlogs, compared to only 25 percent a year ago. Twenty-five percent of the agents report that production supplies must be ordered 90 days in advance, compared to less than 10 percent in the first quarter.

Order backlogs are building for a variety of capital goods. Some producers of components are reporting new orders up 30 or 40 percent from last year, although an improvement was already under way at this time in 1971. Demand for hydraulic excavators, concrete mixers and environmental control systems is especially strong. Recently, orders for overhead cranes, usually associated with major new plants, have increased from a sluggish pace.

Order backlogs of one steel firm are the highest on record, in tonnage terms, except for strike-hedge buildup periods. Lead times are lengthening for steel. The improvement in demand now includes all major product lines. Steel shipments are forecast at 96 million tons for 1973, up from 92 million tons in 1972. Output of some products may be close to capacity.

Significant stretchouts in order lead times are reported for such items as plastic molds, metal fasteners and bearings. Producers of these items do not now have the effective capacity to achieve levels of output reached in the late 1960s. They must expand staff and add facilities.

Crop yields are reported at record levels, but wet fields, especially in Indiana and Illinois, are causing delays in harvesting. Crops of some farmers, especially those raising soybeans, are already damaged. Higher prices associated with a shortfall in the harvest may boost total farm income. Delayed harvests will relieve some of the burden on the transportation industry associated with grain shipments for export. Wholesale prices of cattle have weakened in recent weeks as supplies of red meat have increased. Heavier weight cattle are being marketed. Pork supplies are increasing seasonally.

Business firms are said to be easing restrictions on expense accounts, including first class air travel. Advertising budgets are also being raised. In part, these moves are said to reflect the fact that some firms' profit margins are approaching the guideline ceiling.

Loan demand increased at most large banks in the past month. Nevertheless, bankers are reducing their forecasts of the extent of the probable rise in short-term rates next year. In the long-term markets a large volume of funds are available and most analysts expect level or even declining rates for new corporate bonds in 1973. The volume of funds seeking investment in real estate, especially from S&Ls and insurance companies, is very heavy. Lenders are not able to obtain "equity kickers." Some S&Ls are taking advantage of their new powers to make consumer installment loans, including loans on recreational vehicles and mobile homes, but the movement has not yet gathered great momentum.

EIGHTH DISTRICT - ST. LOUIS

Economic activity in the Eighth Federal Reserve District has continued vigorously upward in recent weeks, according to a selected group of businessmen. There is a rising wave of business optimism. Sales continue to rise on a broad front. Manufacturing activity continues to expand, and more industries report their operations are approaching capacity levels. From the businessman's viewpoint, labor markets are tight in most of the district. Employment still trends upward, and the unemployment rate is down. Construction remains at the relatively high plateau attained more than a year ago. Financial institutions report a vigorous loan demand and large savings inflows. Long-term interest rates remain relatively stable, but upward pressure on short-term rates continues.

Sales of goods and services in recent weeks have apparently continued up at about the trend rate of the past year. Retailers report further moderate gains on a seasonally adjusted basis. Manufacturers also report further increases in sales during the third quarter. Some items, including cement and paper, are reported to be in short supply. In addition to developing paper shortages, the packaging industry reports the quality of paper delivered is more varied and less dependable than earlier in the year.

Vigorous expansion in manufacturing activity is reported throughout the district. Paper, construction materials, metals, textiles, food processing and chemical firms all report operations at a relatively high rate of activity. A representative of a large diversified cigarette manufacturing company reported an increase of 17 percent in sales and 10 percent in employment from year ago levels. Representatives of both paper and cement industries report their industries are operating at capacity. A representative of the packaging industry reported that unless expansion of kraft paper output occurs, rationing will soon be necessary and that there is no incentive to expand capacity at current price and profit levels.

Employment expansion continues and more communities report a shortage of labor in all skill groups. Additional workers have been added to payrolls in recent weeks throughout the district. An Arkansas representative reports that the local labor force is fully employed, employee turnover is becoming critical and most Arkansas plants are trying to add to their labor force. In a few areas of the district, such as southern Indiana and St. Louis, where some unemployment pockets remain, employment has picked up and the unemployment problem has become less severe.

Excluding the St. Louis area, both residential and commercial construction continue at the relatively high rates of the past year. Residential construction is at a high rate in the St. Louis area, but the construction industry here remains somewhat depressed because of a very low level of commercial building.

Commercial banks and savings and loan associations report continued strong demand for loans, with some slackening in savings inflows in recent weeks. Demand for mortgage loans remains vigorous, but mortgage interest rates remain about unchanged from midsummer levels. Commercial loan demand is expanding and upward pressure on commercial loan rates continues.

NINTH DISTRICT - MINNEAPOLIS

Although Bank directors foresee no resurgence in inflation, they generally feel wage-price controls should remain past April 30. District farm income is at a record high level and district farmers are cautiously optimistic about the future. Improved farm income has reduced the demand for short-term agricultural credit, but has bolstered the demand for intermediate- and long-term loans. Rising interest rates are not expected to impede the pace of district economic activity.

Although future price increases are anticipated, Bank directors generally foresee no significant pickup in the rate of inflation. One director indicated that farm prices in coming months would not be exerting as much upward pressure on consumer prices as they have recently. Also, according to another report, consumer resistence to price increases was tending to dampen inflationary pressures in one director's area. On the other hand, another director stated that recent advances in wholesale prices made future increases in consumer prices inevitable. One director revealed that some of his area's merchants view the prospect of more inflation as a spur to their current business, as consumers purchase now to avoid future price increases.

The consensus among Bank directors was that wage-price regulations should be continued past April 30, even though they dislike controls. Several directors, however, would favor liberalizing Phase II guidelines and gradually lifting controls. One director indicated wage-price controls will become ineffective if continued too long. Another advocated terminating Phase II and holding federal expenditures at $250 million.

Due to high grain and livestock prices, district farm income has swelled to a record high and district farmers are cautiously optimistic about the future. Two directors stated that livestock prices should remain generally high. The grain price outlook is also considered favorable, providing export demand continues strong. A director from the South Dakota cattle feeding and feed grain producing area, however, pointed out some weak spots. Corn prices remain relatively low and unseasonably wet weather in South Dakota has caused problems, depressing local prices further. Also, fat cattle prices have recently declined, and currently the margin between fat and feeder cattle prices will not allow cattle feeders to realize a profit. Canadians recently have been buying fat cattle in South Dakota and this should help raise prices. Furthermore, two directors indicated that hog prices will drop as production increases next spring.

According to our recent Agricultural Credit Conditions Survey, a strengthening farm income situation has produced a disparity between demands for short-term credit and demands for longer-term loans. Demand for short-term loans fell as this year's stronger cash income from higher livestock prices, larger grain marketing receipts and government farm program payments decreased the need for short-term funds. Stronger incomes, however, have recently made farmers and ranchers more confident of investing in their operations and this has bolstered the demands for intermediate- and long-term loans.

The survey points toward a resurgence in farmer borrowing in the fourth quarter at some district banks, which will be about evenly balanced by further declines at others. Farmers' and ranchers' incomes are expected to continue strong, displacing needs for short-term funds. Farmer spending will increase as will investment, which will cause some increases in demands for debt refinancings. Comments from respondents indicate that investment plans will lift overall demands for intermediate-term loans. Still, however, only a very small percentage of banks expect problems in meeting loan requests during the next three months.

District businessmen and bankers generally foresee some advance in interest rates, but don't consider these increases of sufficient magnitude to affect district economic activity. One director reports, for example, that the prospect of higher interest rates doesn't bother his area's businessmen. Also, two bankers believe jawboning efforts have and will dampen interest rate increases. Nevertheless, a director associated with the construction industry reported that businessmen are currently lining up financing on future projects in order to avoid expected interest rate boosts. Although he doesn't anticipate higher interest rates locally, one director indicated that money in his area will become tighter as local bankers will allocate more funds to investments in order to take advantage of improved yields.

TENTH DISTRICT - KANSAS CITY

Tenth District business continues to improve, with manufacturers planning to increase inventories further in anticipation of more sales growth. The breadth and strength of economic activity is indicated by revenue gains and optimistic outlooks of almost all major district firms contacted, a sample representing a wide variety of products sold across the country and overseas. With strong business and consumer loan demand at commercial banks, and an indication of some flattening of deposit growth, some interest rates have risen and district bankers expect further increases in short rates. Changes in Regulations D and J continue to concern bankers, while businessmen are worrying about the upcoming heavy calendar of labor contract negotiations and their impact on costs and prices.

Most Tenth District bankers report moderate growth in demand deposits. Trends in time and savings deposits are mixed, with some banks experiencing strong growth and others reporting essentially no change. Most banks have increased rates on certificates of deposit, in some cases to the Regulation Q maximum. One bank has already noted a slight outflow of CD money as a result of the recent rise in competing market issues. Most bankers anticipate a further rise in short-term interest rates over the coming months, with some anticipating significant disintermediation as a result.

Demand for loans in all major categories has been strong at most district banks. No leveling in construction loans is evident as yet, though some bankers expect such leveling in coming months, particularly due to seasonal factors. Demand for business and consumer loans continues strong.

District bankers express considerable uncertainty about the effects of changes in Regulations D and J on deposit levels. Officials at several banks expect an adverse impact, but one large bank is sufficiently confident of a 2 to 3 percent increase in deposits and is already extending loans on the basis of the anticipated rise. Even those bankers contacted who anticipate an adverse effect on deposit levels expressed approval of the changes in the regulations.

Several manufacturers plan to increase inventories. Their intentions reflect improved sales outlooks, desires to provide cushions against lengthening lead times for raw materials, and efforts to improve customer service. Other manufacturers, including some who overestimated sales in recent months, feel their current inventory levels will prove adequate for expected sales increases.

Agribusiness is thriving, thanks to record farm income. Firms selling supplies to farmers report sales increases up to 20 percent over last year. The favorable high price and high production situation includes the sugar beet industry, and two major sugar refineries expect substantial revenue increases this year.

Reviving private demand and new government contracts have pulled the cyclically sensitive Wichita economy up from an 8.1 percent unemployment rate a year ago to its current 4.3 percent level. Wichita's private airplane manufacturers -- a key industry in the city -- report very good business and expect 1973 to be equally strong or better.

The improvement in general business conditions nationwide is also reflected in current sales and optimistic expectations of several other types of Tenth District firms with extra-regional markets. Consumer-oriented firms include a manufacturer of luggage, a large nursery, two big manufacturers of rubber products, a large manufacturer of small home appliances, a leading greeting card company and a manufacturer closely tied to the auto industry.

Producer-oriented manufacturers, including giant truck, steel drum and water-cooling tower firms, generally have experienced a somewhat less impressive sales increase over last year than have manufacturers of consumer products. But most are optimistic about sales prospects in the months ahead.

Publications and contacts in the district report an excellent summer tourist season. A good winter sports season already has begun. The recreational land boom continues.

While a discouraging word was seldom heard, a few respondents, ranging from a machine tool manufacturer to a manufacturer of snack foods and one of plastic bags, reported sales not much improved over last year. The worst expected, however, was another year of the same.

Several nonbank businessmen also were asked about their expectations regarding inflation and interest rates and their choice of a continuation or end to wage and price controls. The responses on interest rates were too mixed to permit a conclusive prevailing opinion. As to the price level, most say the bargaining ahead, and the controls applied, will determine the outcome. While two want controls ended and replaced with antitrust action against unions, the others feel some controls must be maintained.

ELEVENTH DISTRICT - DALLAS

Most major indicators of economic activity in the Eleventh District continue to show growing strength. Both Texas industrial production index and total employment in the five district states advanced to record levels in September, and department store sales continued strong in October. Nevertheless, construction contract awards eased slightly in September, and registrations of new automobiles also slipped. In a recent survey, the directors of this Bank and its branches revealed considerable optimism over the outlook for the first half of 1973. The directors generally agreed that the prospects were good for continued improvement in general business conditions, employment, and profits. However, they also expected increasing upward pressures on prices and wages.

The responding directors overwhelmingly expected business conditions to improve in the first half of 1973. They were also optimistic about the unemployment rate with almost all of the respondents expecting the rate to be lower, or at worst no higher, than its present level. The consensus was that total construction activity would also be either equal to or above its current level. An unsettling finding, however, was that almost three-fourths of the respondents expected the rate of inflation to increase in the first six months of next year.

Directors representing district banks reported that demand for business and consumer loans increased over the past three months. Banking respondents also felt that loan demand would continue to increase over the next six months, with business and consumer loans continuing to show the greatest strength. Although the availability of funds to meet these loan demands was generally described as either adequate or plentiful, there was widespread agreement that short-term rates would be rising over the first half of 1973. Banking directors were about evenly divided, however, in their expectations for long-term rates between those anticipating rates to remain the same and those expecting them to rise.

Directors from the nonbanking sector were also confident about the first half of next year. About a quarter of these directors expected their firms to increase employment and over half indicated that their companies were planning to increase expenditures for plant and equipment. Inventory levels were generally not expected to fall any lower and a good many respondents indicated plans to increase their level of inventories. Almost half of the nonbank directors expected their profit rates to be higher in the first half of 1973 than in the most recent quarter. These directors were not so optimistic about prices and wages, however. Over four-fifths expected prices and wages in their industry to increase, with wages increasing faster.

Seasonally adjusted employment in the five southwestern states rose again in September as both the manufacturing and nonmanufacturing sectors recorded gains. Monthly employment gains were reported in every sector except mining, where employment levels were unchanged from August. Despite the increase in employment, the unemployment rate in the five district states remained at 4.4 percent in September as the expansion in the labor force matched the gains in employment.

The seasonally adjusted Texas industrial production index rose sharply in September to a record level as all major industrial sectors of the index advanced. Within manufacturing, the production indexes for both durables and nondurables increased over August. The largest gains were recorded in petroleum refining and utilities.

Oil allowables were kept at their maximum rates for November in the district's two largest producing states, Texas and Louisiana. Nevertheless, demand for petroleum continues to outpace domestic production and imports are being depended upon to close the gap.

Recent indicators of consumer spending were mixed. Sales of department stores continued to show monthly and year-to-year gains through October. Among the four largest metropolitan areas of Texas, Dallas and Houstin recorded the most substantial gains. The rate of new automobile registrations in these four centers, however, declined from the rate of a year ago. San Antonio was the only major area to post an increase over last year.

The value of construction contracts awarded in the district fell slightly in September as residential and nonbuilding construction awards in the five-state area fell from their August levels while nonresidential building increased slightly.

Prospects for farmers and ranchers in the five district states remain bright. Total agricultural production continues well ahead of last year. Much of the increase comes from a larger cotton crop and the steady rise in cattle on feed. Farm prices also remain considerably higher than a year ago. The gains in both production and prices have combined to boost farm receipts in the first eight months of this year to a level 17 percent higher than in the same period a year ago.

TWELFTH DISTRICT - SAN FRANCISCO

Directors in the Twelfth District were asked to assess wage and price trends in their area or industry. Their consensus is that increases in both prices and wages would be moderate and consequently there would be less inflation in the coming year. For the economy in general, further expansion is expected in most industries, with the possible exception of construction where some leveling off is foreseen.

Wage increases in the 5 percent range are judged to be likely for the coming year. There are some exceptions, however. For example, one manufacturing firm expects a 6 1/2 to 7 percent increase for the year. Unionization of farm workers is a factor that would add to wage pressures in agriculture, and the expansion of aircraft production in Seattle will create pressure on the wages of some classes of skilled and office workers. Wage controls cause problems for some firms that lose key managers and skilled personnel through their inability to match outside offers. In the view of most directors, maintenance of wage controls will be a major element in keeping wage increases in line through 1973, a year when many major contracts expire.

Associated with the lessening of wage increases will be slowing of price increases. In several industries the ceilings have stopped price rises, while in others insufficient demand is a major reason for restraining increases. Therefore, a 5 percent increase in list prices may mean only 1 to 2 percent in effective prices due to competitive pressures forcing price concessions.

Agricultural prices, which have been very good in 1972, are not expected to be much higher according to directors in agricultural areas. Several directors believe both wheat and cattle prices in particular are not likely to climb much more. On the other hand, smaller crops elsewhere in the country will maintain prices for western potato growers.

One effect of price ceilings has been to narrow profit margins. A large producer of processed foods reports that the inability of several large firms to get approval for price increases on some product lines has prevented others from raising prices. The lower margins exist in such lines as canned beef, fresh milk and ice cream. Firms affected are continuing to watch inventories and to reduce their labor force whenever possible. Another problem, in one director's view, is that price cutting by one major chain is cutting food retail margins to levels that may have a serious financial impact on a number of quite substantial chains throughout the country.

The overall performance of the economy remains satisfactory. Retailers in the Twelfth District are expecting excellent Christmas sales at levels about 10 percent above the previous year's sales. As a result, some stores have been increasing their sales force earlier than usual.

However, a hesitant attitude by wholesalers may lead to inventories that are too thin to meet expected consumer demand for some products and thereby keep sales to a lower level.

Construction activity, although high, is causing some concern. In Seattle there remains considerable vacant space in commercial office buildings and warehouses, and in Portland there is some evidence of overbuilding of apartments. A recent court decision in California requiring environmental impact studies for large construction projects is singled out as another factor causing uncertainty about future construction activity in the state.

Bankers in southern California report strong demand for mortgages and for consumer credit. Deposit inflows are also strong. In Portland, business loan demand is described as disappointing, while in Utah and Idaho it is described as very strong. Generally, banks are able to meet foreseeable loan demand with minimal stress.