CONFIDENTIAL (FR)

CURRENT ECONOMIC COMMENT BY DISTRICT

Prepared for the
Federal Open Market Committee
by the Staff

October 9, 1974

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SUMMARY*

On balance this month's comments indicate a further slowing in overall economic activity and more widespread pessimism regarding the near-term outlook. Residential construction remains in a depressed state throughout most of the nation. The situation in the housing sector is causing a marked decline in consumer outlays for durables related to housing, and aggregate real consumer spending appears to be weakening further. Business capital spending continues relatively strong although there are further reports of delays and cutbacks of previously scheduled outlays. The manufacturing sector presents a mixed picture with reduced demand pressure and fewer shortages in some industries, particularly those industries serving primarily the housing and consumer durables sectors, but continued tightness and shortages elsewhere. Several Districts report that the improved supply-demand balance in some industries has reduced the upward pressure on prices for certain raw materials and intermediate industrial goods, but no precipitous softening of industrial prices is yet evident. Adverse weather conditions are apparently restricting crop yields and hampering the growth of farm income in the central portion of the country, and conditions in the livestock industry have deteriorated further. Most Districts report more restrictive bank lending policies and a consequent slowing in the growth of business loans. Thrift institutions experienced further net deposit outflows in several Districts during September.

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*Prepared by the Federal Reserve Bank of Richmond.

Retail sales appear to be generally flat in current dollar terms implying the possibility of some decline in real consumption during recent weeks. Boston, New York, and Philadelphia report that consumers are more cautious and bargain conscious. Several Districts indicate a further decline in sales of big ticket items, notably furniture and home appliances. Cleveland and Chicago report new model automobile sales are off to a slow start. Dealers in the Minneapolis and San Francisco Districts fear that higher prices, difficulties in obtaining financing, and the recent spurt in 1974 model sales will constrain new model sales in coming months.

Conditions in the construction sector remain dismal, although Philadelphia reports a higher rate of nonresidential building than last year due to increased public works construction. Dallas, on the other hand, foresees a sharp curtailment of nonresidential outlays in coming months due to a lack of interim financing. Nonresidential building permits have dropped by 50 percent in the Dallas District during the last three months. No District expects any near-term improvement in the residential sector given the pervasive lack of mortgage credit.

Business fixed investment remains the strongest sector of the economy, although there are additional signs of a reduced rate of planned capital expansion. Atlanta and San Francisco report sizable reductions in planned outlays by utilities. Chicago notes a reduction in the demand for certain types of capital goods due to postponements and cancellations by utilities and automobile manufacturers. In the Cleveland District machine tool orders, while still strong, are running somewhat below their peak earlier this year.

Conditions in the manufacturing sector are spotty, reflecting the sluggishness in the housing and consumer sectors on the one hand and the relative strength of capital spending on the other. Industries closely related to housing and consumer durables (lumber, glass, textiles, furniture, and appliances) are noticeably weaker. In addition, several Districts (New York, Chicago, Kansas City, and San Francisco) report that some industrial materials, particularly fuels, certain chemicals, and paper, are more readily available. The easing of supply constraints in these industries is contributing to less aggressive purchasing and some declines in order backlogs. Cleveland, Chicago, Kansas City, and Dallas indicate somewhat softer prices for chemicals, fuels, and other materials, but no major break in industrial prices has occurred to date. Steel markets remain tight in most Districts, due in part to the prospective coal strike. Both Cleveland and San Francisco suggest an easing in the steel situation in coming months, however, due to the increased availability of foreign steel.

The agricultural outlook appears generally weaker. Atlanta reports favorable harvest yields with the exception of the hurricane-damaged Louisiana sugar cane crop. But Chicago, St. Louis, Minneapolis, and Kansas City indicate that early frosts will substantially reduce corn and soybean yields, reducing farm incomes and increasing feed costs.

The demand for business loans remains strong in most Districts, although St. Louis notes a leveling off following the sharp upward trend earlier this year. Philadelphia, Richmond, Minneapolis, Kansas City, and Dallas all report slower growth in outstanding loans and commitments due to more restrictive bank lending policies. Several Districts indicate that both banks and thrift institutions are restricting new loans to established customers.

FIRST DISTRICT - BOSTON

Our Directors' outlooks remain mixed. Those close to primary products and producers goods see many lines as being "sold out forever," while Directors more familiar with retailing worry about the vitality of the economy. Whereas concerns last month focused on high interest rates, this month those expressing misgivings discussed layoffs and demand weaknesses as well.

We specifically inquired about discounting policies. Though most responses dealt with regional behavior, the experiences of certain firms dealing in a wide range of national wholesale markets were included. The picture is surprisingly uniform: there is very little discounting from list prices, with the possible exception of retail prices on expensive lines. Even in cases of improving supply and deliveries, lists seem to be firm. Industries facing softer demand prospects seem to do little more than offer better terms. One Director, however, anticipates discounts in textiles and home furnishings so that the goods keep moving.

All Directors entertain a gloomy outlook for general economic conditions. Nonetheless, metals, chemicals, machine tools, military-related hardware, producers' metal products, and diesel engines were lines singled out for their generally strong performance. With one exception, all Directors noted a worsening of unemployment in their regions, and all anticipate a deterioration of the situation in the future. In the Boston area, major employers are releasing significant numbers of employees, and one large firm servicing a national consumer market has just announced a 2 percent across-the-board lay-off. One telephone

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CORRECTION

Current Economic Comment by District
(Red book)

On page 1 of the report for the First District (Boston), the figure in the bottom line should be 20 per cent rather than 2 per cent.

company is reporting furloughs of personnel while another faces historically high delinquency rates.

Income squeezes on firms and households are encouraging less wasteful practices. Supermarkets report that consumers are becoming more sophisticated in their purchasing behavior, paying closer attention to bargains and specials. Electricity consumption has declined 6 percent from the previous year. Firms are closely managing cash flows and money positions. Demand deposits have fallen behind those of a year ago according to two banking Directors. Firms are also learning to run their businesses more efficiently, and this development may soon affect purchase orders.

High interest rates still plague utilities. A state legislator has introduced a bill which would relegate one major utility to the status of a power distributor; the state would assume power generation responsibility. In any case, it is one Director's opinion that today's crunch may lead to a power shortage in the 1980's.

All of the academic correspondents contacted this month, Professors Eckstein, Samuelson, and Tobin note further deterioration in the economic outlook. Eckstein reports that businesses have universally adopted more cautious behavior with regard to inventories and hiring even in those industries where markets have held up. He now forecasts real growth to be less than 1 percent next year with no increase in constant dollar business fixed investment. Tobin points out that the weakening in the real economy, particularly in investment behavior, is consistent with his presentation to the Board last spring. Samuelson cited George Perry's forecast of a 7 percent unemployment rate by mid-1975 and Perry's statement that the major error of the Summit Meeting was not to have realized the severity of the current recession.

SECOND DISTRICT - NEW YORK

Second District Directors and other business leaders who were contacted recently on balance felt that retail sales were holding up better than had been expected. There continued to be reports of easing shortages in a number of lines along with persisting tight supply conditions in others. The respondents did not think that firms were raising prices because of apprehension of a return to price controls. No significant easing of liquidity pressures was noted.

Regarding consumer spending, the Buffalo Directors generally characterized retail sales, other than automobiles, as being stronger than had been expected, a sentiment shared by an official of a nationwide chain of department stores. An upstate businessman, a Director, felt that although the higher price for 1975 automobile models might have an initial adverse impact on auto sales, if the new models appealed to the public, such sales would return to normal. In this context, a New York City representative of a major auto manufacturer stated that while only a few days had elapsed since his firm's new models had been introduced, dealers were reporting a very favorable public reaction to the design and engineering improvements in the firm's 1975 models.

On a more restrained line, a number of the respondents indicated that although retail sales levels appear to remain high, consumers are bargain hunting to a greater degree than before. And a senior official of a high quality New York City department store with branches in the suburbs reported that his firm had taken a gloomy view early in the year, but had been "pleasantly surprised" until September; since then, his firm's business had turned "soft," particularly with respect to durable goods and big ticket items.

Concerning supply conditions, the president of a multinational chemical firm reported some easing in certain lines of chemicals and in packaging products, while the chairman of a major oil company characterized the supply picture in the petroleum industry as quite strong, with substantially higher inventories of fuel and heating oil. The president of an upstate bank stated that supply conditions in general had eased somewhat, a sentiment expressed by several other respondents. The retailers that were contacted reported some easing in textile products and another observer reported a greater availability of certain lumber products. The Buffalo Directors, however, stated that supply conditions remained tight for critical items used in manufacturing such as stainless steel, zinc, paper products, metal casing and welding rods, and noted that in general delivery times for manufactured goods were much longer than last year. A Director closely associated with New York State agriculture reported that fertilizer and box material remained in tight supply and that rapidly rising prices as yet had not dampened the demand for these products.

Respondents expressing an opinion on the price situation did not think that firms were raising prices because of fears of a return to price controls. Rather, the rapid increase in prices was attributed to higher operating costs and declining profit margins. A senior official of a large multinational firm based upstate stated that business generally recognized that if price controls were reinstated such a move might well be accompanied by mandatory price roll-backs.

Comments regarding the unemployment situation were received before the release of the September unemployment figures. At that time, the respondents attributed the continued relatively strong employment picture in the face of weakness in some other economic indicators primarily to the limited extent of the decline in industrial production and to the strong corporate profit picture, which has induced less layoffs.

Views regarding the impact on liquidity positions of the recent decline in short-term rates were best summed up by the Buffalo Directors. No significant easing of liquidity pressures was noted by these Directors. They generally felt that current short-term rates could be tolerated by large industries but that liquidity pressures continue to be particularly intense for the small businessman. Moreover, while short-term rates may have gone down, there has been little change in long-term rates, posing problems with respect to long-term financing for industry and municipalities.

THIRD DISTRICT - PHILADELPHIA

September was a slow month for most businesses in the Third Federal Reserve District. Manufacturing activity was off and employment opportunities also softened. Prices continued their inexorable rise. Area retailers reported weakness in the sales of most lines of merchandise. Most of these businesses have been unable to keep their sales volume ahead of inflation. In the construction industry strength in the public works sector has offset the weakness of residential housing. One of the few industries in the region that shows real strength is commercial banking. Virtually all of the major banks have more loan business than they can handle and, in fact, are discouraging attractive new business in an effort to reduce their reliance on money market sources of funds. The results of a survey of manufacturing executives in the District suggest further weakening of the area economy during the last month. New orders are lower for the first time in three months, and production is catching up with the order backlog. Shipments rose during the month and delivery times on orders in process were cut. For the most part, inventories were steady during the month. These businessmen also report some softening of their need for labor.

This short-term sluggishness is reflected in the outlook these businessmen hold for the months ahead. On balance, they still expect business conditions to improve by March, but the ranks of the pessimists are swelling. Most respondents expect new order activity to be holding steady in the months ahead. Unemployment will probably be up in these industries as manufacturers shrink both their workforces and their average workweeks.

Capital spending during the next six months is not expected to change very much from current levels. Retailers in the Delaware Valley are feeling the slowdown quite keenly. Only one of the four major retail chains surveyed was managing to keep its volume ahead of inflation. The concensus is that consumers are downgrading the quality of their purchases, looking for sales, and avoiding many big ticket purchases that could be deferred. The outlook is for continued weakness through the Christmas season.

Construction activity in the District is mixed but clearly on the plus side. The value of construction contracts awarded so far this year is up 40 percent over the comparable figure from last year. This is well above the national level of activity in this industry. Residential building is down dramatically, but nonresidential construction is ahead of last year's pace. However, the major factor giving the industry its current strength is public works construction. The value of local contract awards in that sector of the industry is up almost 200 percent over last year at this time.

Third District banks report that their business loan growth has slowed, but the reason has been restrictive lending policies rather than lack of demand. Virtually no new business is being accepted, and well established customers are required to show that their loans are intended for "productive" rather than speculative uses. The lending restrictions have not been directed at any one class of business borrowers.

Finally, inflation shows no sign of abating. The glimmers of hope reported last month have all but disappeared from the results of our latest outlook survey. The businessmen anticipating higher prices for both the goods they buy and the ones they sell outnumber those expecting prices to hold steady by more than two to one. Only a handful of respondents expect any reduction in prices by next March. It looks like inflation psychology is well entrenched and will not soon be dislodged.

FOURTH DISTRICT - CLEVELAND

There are signs of some slowing in the pace of District manufacturing activity, an easing in supply conditions for many items, and a moderate reduction in the pervasiveness of industrial price increases. Machine tool orders remain strong, although below the peak reached earlier this year. The domestic steel market continues to be tight, but world steel demand is easing. Banks report strong loan demand and increasingly stringent loan policies. S&L's generally continued to lose deposits in September and early October; few mortgage loans are being made.

Early returns from our monthly survey of manufacturers indicate some weakening in new orders and backlogs during September. Production apparently continued to rise moderately, while inventory accumulation remained large. Firms note an easing in delivery schedules and in labor utilization. Inflationary pressures continue to be extremely pervasive, although the proportion of firms paying higher prices has declined slightly in recent months from the peak levels reached in the spring and early summer. Recent reports of purchasing agents in the Cleveland area mention signs of price resistance on the part of industrial buyers and a gradual slowing in the percent of companies paying higher prices.

Among the industries showing current weakness are building materials firms and consumer goods producers. Several major glass producers have cut output and employment. Two large appliance firms in the District are laying off workers as a result of sluggish sales. A major tire firm reports excessive inventories of tires. Unless new car sales strengthen, it is likely that output and employment will be cut later in the year. (Auto dealers in northern Ohio say 1975 new car sales are off to a slow start with consumers interested mainly in the 1974 models.)

Executives from three large machine tool firms in the Ohio area say that new orders are still strong, although somewhat below the peak levels reached last March and April. Ordering by heavy equipment producers, especially mining and earthmoving machinery, continues to be high. Machinery firms report the high cost of money is affecting the ability to increase production. Shipments can be increased, builders complain, only by borrowing money at interest rates around 15% to build component inventories.

Steel industry sources report no slackening to date in the demand for U.S. steel. Order books are solid through 1974. The tight steel market has caused customers to be less demanding with regard to quality; and with less steel rejected at the mills, finished steel output has been running at a higher percentage of capacity. The tight market also has forced steel customers to carry their own inventories rather than have the mills hold them. Contrary to the domestic situation, steel industry economists report an easing in world steel demand and a recent surge in steel imports. Expectations are that foreign steel prices (now at a premium) will drop next year to whatever level is necessary to sell steel in the U.S. One economist predicts an end to domestic steel shortages in the second quarter of 1975.

Steel mills continue to be hampered by shortages of coking coal. Two major steel firms both said that in the event of a coal miners' strike they would begin cutting production immediately unless the government gives indications of ordering the miners back to work. An executive with a large coal company confirmed reports that a coal strike would have immediate repercussions on steel output. Utilities have almost normal inventories of coal--between two and three months supply. The spokesman estimated that the utilities could withstand a four-week coal strike.

In the financial area, bankers report that tighter loan policies are being applied to all types of borrowers, and few new customers are being accepted. Utilities are borrowing to the maximum of their credit lines and are expected to continue so until other markets improve. REITs are said to have all they are going to get. Banks notice weakness in loan demand from housing-related customers such as furniture and appliance dealers. Strong credit demand from manufacturers is anticipated during the current quarter.

Spot checks with S&L's in the Cleveland area generally reveal sizable losses in deposits during late September and early October. One of the area's largest S&L's, however, has been a net gainer in deposits thus far in October, following extremely heavy losses in September. The recent improvement was attributed to a heavy promotional campaign to attract deposits. Other S&L executives do not expect an improvement in their deposit flows until the yield on T-bills falls below 7 percent. They are prepared for a massive advertising campaign when rates are at or below that figure. Presidents of four local S&L's all remarked that demand for mortgage loans is still high, despite lending rates in the 10 to 11 percent range (with a third down). No one is encouraging loans, and loans are made selectively only on the basis of past customer relationship of a high recommendation.

FIFTH DISTRICT - RICHMOND

The September survey of Fifth District businesses reveals a continued slowing in most sectors of the District economy, with the manufacturing sector showing the greatest decline. This decline seems to be centered in a few industries, but they are industries which contribute significantly to the Fifth District economy, including the textile and furniture industries. Construction, particularly residential construction, continues in a slump, and the effects are beginning to ripple throughout the District economy, impacting on employment and production in several important industries. New orders declined almost across the manufacturing sector, while inventories of finished goods continued to accumulate. The six months expectations of manufacturing firms turned decidedly pessimistic. In the banking sector, reduced demand and restrictive bank lending policies have slowed the growth of business loans relative to the first half of the year. The personal savings situation shows continued weakness.

Survey responses from the manufacturing sector indicate broad and, in many areas, steep declines in the level of activity. Some decline in shipments was indicated, but a more accurate assessment of the trend might be based on the volume of new orders and the backlog of orders. Thirty-seven percent of the manufacturing respondents indicated declines in shipments while only 28 percent indicated increases. On the other hand, 58 percent reported a decrease in the volume of new orders and 51 percent reported a reduced backlog of orders. The last six months have shown a consistent, or perhaps accelerating, decline in new orders while the volume of shipments has generally remained firm. September represents only the second month since March in which shipments, orders, and backlogs each showed a general weakness. Additionally, there was some further inventory accumulation in the finished goods area. Forty-eight percent of the manufacturers surveyed now feel inventory levels are excessive. More than twice as many manufacturers reported reductions than reported increases in the number of hours worked per week.

Although there are indications of a general weakening in the District economy, a review of the individual industries represented in the survey shows a few large industries are greatly influencing the overall picture. In the textile industry, shipments, orders, and backlogs were all off sharply, inventory levels were considered excessive and expectations were generally pessimistic. During September, there were scattered reports of textile firms slowing or ceasing production. Recent announcements include one-week closings of six plants by one firm and the dropping of a product line by another.

Similar conditions are reported by survey respondents in the furniture and fixtures industry where shipments, orders, and backlogs were down sharply and current inventory levels are considered excessive. Expectations among furniture manufacturers surveyed were decidedly negative, with one respondent feeling there is "no improvement in sight." Conditions in the furniture and fixtures industry are, of course, closely related to conditions in the depressed residential construction industry. Various reports show continuing declines in building permits issued and high and rising unemployment among residential construction workers. Cutbacks in other industries are also being tied to the current housing market. For the second consecutive month, a major sheet glass producer has closed a production facility in the Fifth District. The lumber and wood products industry reports conditions very similar to those reported by the textile and furniture industries.

Several factors, such as rising prices, tight credit conditions, and delays in obtaining materials, are having a depressing effect on the expectations of those manufacturers surveyed. Sixty-five percent now expect national business conditions to worsen over the next six months and almost as many, 58 percent, foresee a similar decline in their respective market areas. Perhaps more indicative of the general mood, the number expecting their own level of production to decrease now exceeds the number expecting it to increase over that period.

Retailers responding to the September survey present a somewhat more optimistic picture, although the responses are difficult to interpret. Sales are generally reported to be increasing but it is not clear whether this indicates a real increase or merely increases in dollar volume. Sales of big ticket items relative to total sales continued to decline during September. There is some indication that inventories are accumulating beyond desired levels although this condition may not yet be widespread.

In the banking sector, the efforts of banks to restrict business loan activity are having some impact as aggregate business loan expansion slowed relative to the first half of the year. There are also some indications that business loan demand is slowing as well. Commercial and industrial loans outstanding at District weekly reporting banks have shown essentially no growth over the past four months. Consumer savings deposits at commercial banks remain weak, having declined through September. Final July data for S&L deposit activity in the Fifth District (excluding West Virginia) shows a net decline in savings of \$49.8 million. Preliminary data for August indicate a net savings drop of \$77.2 million.

Realized net farm income rose an unprecedented 68 percent in 1973. But District bank agricultural specialists, in a recent opinion survey, indicated a belief that net farm income will decline this year because soaring farm production costs will more than offset the slight gain in gross farm income.

SIXTH DISTRICT - ATLANTA

Inflation continues to concern most area businessmen, but fears of recession are becoming more widespread. While the region's crop outlook is good, Hurricane Carmen destroyed part of Louisiana's sugar cane crop. Mobile home plants in the District are closing or laying off workers. While new commercial projects and industrial plants continue to be announced, several cutbacks and delays have been reported. Foreign trade in the region appears to be booming.

Florida Directors are pessimistic, largely because of the depressed conditions in housing. In south Florida, it would take about two years to fill up vacant condominiums and housing coming on the market. The slump in housing is now spreading to other sectors of the economy. Directors in Birmingham, Nashville, and New Orleans expressed growing concern over a possible recession. One New Orleans businessman summed up this feeling by stating that although people in this region were more concerned with problems of inflation than recession or depression, there is growing concern that a further wringing out of the economy will cause undue hardship to the small businessman and the average income citizen.

Hurricane Carmen, which hit along the Louisiana coast, destroyed an estimated $100 million--about 20 percent--of the states sugar cane crop. The unharvested rice crop was also damaged. The soybean crop is very good in Louisiana this year. The Florida citrus industry is pleased with its near-bumper crop and reports the fruit is in excellent condition. Georgia's tobacco and corn crops may turn out to be the best in several years. Georgia's peanut crop is also excellent: the harvest should be 10 percent more than last year. Tennessee's crops have generally done much better than nationally; only soybean production appears to be down.

One large Georgia-based mobile home firm, which had four operations in Florida, has filed bankruptcy. Mobile home plants in south Georgia and in Mississippi have been laying off large portions of their labor force, and at least one plant has closed down operations entirely. A Tennessee appliance manufacturer announced a production cutback and layoffs as a result of the decline in residential construction and mobile home sales. A downturn in the retail fabric market has resulted in a general slowdown in Georgia's large textile industry. Heavy layoffs have not as yet been announced, but companies have reduced operations. The workweek has been cut back from six to five days. Buyers are ordering on a short-term basis and in smaller quantities than normal. Orlando, Florida's Martin-Marietta Corporation recently announced a large layoff; it is the second large layoff at the defense plant this year. The only industry which seems to be booming is Alabama's steel fabricating manufacturing. Reports indicate that profits and order backlogs are well above normal. The Lockheed-Georgia Company also received some good news; it has been awarded an additional $150 million order for 48 more C130H transport planes.

Announcements of new commercial and industrial projects continue. The largest is a new chemical plant for the Baton Rouge, Louisiana area, which will employ some 2,000 workers when completed. Once again this month, several previously announced projects have been cut back or postponed. Southern Company, parent company of Georgia Power and Alabama Power, has suspended plans for construction in both states. This will cut Southern's building program in the next three years by $1.7 billion. Florida Power and Gulf Power Company of Florida are also reducing and postponing construction. In New Orleans, the Pan American Life Insurance Company has postponed indefinitely the previously announced $26 million office building-hotel-shopping complex. New and expanded industry projects have been delayed in the Huntsville, Alabama area because of the slowing in the economy.

Rumors about the stability of one of the Alabama savings and loan associations were rampant--so widespread that a public statement was made by the association's chairman, the district attorney, and the president of the Federal Home Loan Bank to reassure public confidence. Even though all deposits were covered by the Federal Savings & Loan Insurance Corporation, people were lined up to withdraw their funds.

Foreign trade in and out of Florida ports has taken a 50 percent jump over last year. The port of New Orleans also handled more ocean-going cargo in July than a year ago. In August, a Liberian freighter left Mobile, Alabama headed for Saudi Arabia loaded with southern pine lumber products. Lumbermen hope this is a start of lumber exports, since the industry has suffered from the decline in residential construction.

SEVENTH DISTRICT - CHICAGO

The economic situation in the Seventh District has weakened in the past month. Shortages of purchased materials and supplies are much less significant, and in some cases the change has been dramatic. A concerted effort is being made by many firms to reduce inventories or, at least, restrict further expansion. Consumer demand for discretionary items has slowed, especially for appliances and furniture. Some softness has been noted in certain, but by no means all, capital goods. Housing activity remains at "crisis levels," and a distinct cutback is underway in commercial and public construction. Price inflation in the nonfarm sector has slowed, at least for raw materials. Announced wage settlements cluster in the area of 12 percent per year. Corn, soybeans, fruits, and vegetables have been hard hit by early frosts. Attitudes, generally, have become much more pessimistic, and many firms have "contingency" plans to be effected if prospects deteriorate further.

In the manufacturing sector, the most significant development has been the easing of shortages. Improvement is noted in fuel, paper, industrial chemicals, most nonferrous metals, and of course, residential building materials. Purchasing departments have been deferring deliveries in some cases. Some price softness is reported in fuel, chemicals, and fibers.

Very high interest rates and limited supplies of funds, coupled with reduced demand for some finished goods and ready availability of purchased supplies, have created pressures to reduce inventories, even though inventories are not generally excessive, relative to current activity.

Despite easing in some sectors, supply constraints are still severe in many areas, particularly those related to capital goods. Iron ore, coke, structural steel, steel plates, aluminum, nickel, diesel engines, electric motors, castings, forgings, bearings, hydraulic components, hoists, axles, transmissions, and fasteners remain very tight--many say "as bad as ever."

Consumer purchases of major appliances and furniture dropped off significantly in recent months, partly because of the decline in residential building. Sales of 1975 car models have been below expectations, with sharply higher prices a factor. Airline travel has only equaled year-earlier levels, also with sharply higher prices. Consumers appear to be conserving their resources for necessities and contractual obligations.

Fuel supplies, including natural gas, appear to be comfortable in this District. Major oil companies have followed independents in cutting gasoline prices. Electric utilities say their "send out" has been below forecasted levels.

Current high prices for materials in ample supply are soft and could be vulnerable to significant declines, such as those that have already occurred in the spot commodity market. Finished goods prices remain under upward pressures because of large increases in wages and other costs.

Orders for capital goods have slowed in some categories, mainly because of postponements or cancellations by public utilities and auto producers. Demand for equipment for mining, heavy construction, transportation (highway, rail, and water), chemical processing, oil exploration, pollution control, steel production, and for manufacture of machinery remains very strong

Many smaller commercial and industrial construction projects have been postponed or cancelled because of financing problems. Some very large residential developments have been abandoned, with no plans for revival.

Steel output is expected to be near capacity throughout 1975, despite an expected 10 percent drop in shipments. Mill inventories of steel are badly depleted and must be rebuilt, and imports are expected to rise.

Although steel order books are full, overall, auto industry demand is off, and appliance manufacturers have been cancelling, not merely postponing, orders.

Frosts, two to three weeks ahead of normal, have dealt a severe blow to corn, soybean, fruit, and vegetable crops--especially in Illinois and Wisconsin. Prices of canned goods are likely to rise substantially further. Early frosts came on top of heavy spring rains followed by serious drought. Uncertainties facing crop and livestock producers have been increased by the recent government moves to cut exports. High feed prices are leading to a sharp reduction in production of hogs and poultry.

EIGHTH DISTRICT - ST. LOUIS

Economic activity in the Eighth District generally remains strong. Manufacturing output continues to increase with the exception of housing-related products. The supply situation for most raw materials appears to have eased with the removal of wage and price controls. Little change was reported in the dollar amount of retail sales, except for appliances which were down somewhat. Employment is little changed from the beginning of the year, and the unemployment rate in the Eighth District remains well below the national rate. The agricultural situation is somewhat mixed, with the effect of recent cold weather not yet known.

Manufacturing firms in the capital goods and heavy equipment industries report strong demand for their products. The demand for steel continues especially strong, although part of the demand may be transitory, reflecting the expectations of a coal strike and higher steel prices following the settlement. Many firms are apparently stockpiling steel, and long delays for delivery are reported. The only major weaknesses in manufacturing appear to be those industries which are housing-related, such as lumber and appliances.

Raw materials shortages have generally eased in recent weeks. Wood and lumber shortages have disappeared as a result of the removal of price controls and the slackened demand in the housing industry. Fewer shortages were also reported in the paper and paperboard industries. Some shortages are still reported in chemicals, especially petrochemicals, and in the steel and aluminum industries, but the supply situation in other metals such as brass and copper appears to be easing.

Major retailers report that sales in dollars have in general not changed significantly in recent weeks, although appliance and wholesale clothing sales are down, and shoe sales apparently have leveled off after slowing in the early months of the year.

Employment in the District continues at a generally high level. Employment has shown some recent upturn, partly as a result of strike settlements, and no widespread layoffs are reported. The unemployment rate in the District remains relatively low, well below the national rate.

The agricultural situation is not clear. The effect of early frosts in the northern parts of the District has not been fully assessed, while in the southern parts of the District, harvests have been delayed by heavier than usual fall rains. Yield prospects for rice, cotton, and tobacco are good, while corn and soybeans yields will fall below levels of recent years due to the drought during the summer months.

The demand for business loans has apparently leveled off following a sharp uptrend in the early months of the year. One large bank reported no increase in business loans for several weeks. Savings and loan associations generally report that they are able to meet previous commitments but are not making new home loans. The associations have recently experienced a net outflow of savings, although some report that the runoff was less than expected. The movement from passbook accounts into four-year certificates at thrift institutions was reported to be continuing.

NINTH DISTRICT - MINNEAPOLIS

Although District business activity is currently stronger than in the nation, signs of weakness are emerging. The livestock industry's depressed condition combined with poor weather which has significantly cut crop production has made the prospects for farm income a primary concern. District retail sales so far this year have increased at faster rates than nationally, but retailers are uncertain about the future. However, District resort operators look for good business this winter. A lack of mortgage funds nationally has also hurt District homebuilding, but not as severely as in the nation. Business loan demand continues strong at District banks with no letup foreseen.

After increasing very sharply in 1973 and 1974 the outlook for District farm income is not very encouraging. Early frosts in September combined with a wet spring and a dry summer have significantly reduced District crop yields. Although higher prices will offset part of the production decline, gross receipts from the District's 1974 harvest will probably be down slightly from 1973's level. Gross receipts from District livestock sales are also expected to be down from a year ago. The marketing of livestock this year will not be off significantly but prices are down considerably from a year ago. This softening in gross farm income comes at a time when farmers' production costs have been rising rapidly. Consequently, District net farm income is expected to weaken considerably in the last half of 1974 and into 1975.

Relative gains in District retail sales have outpaced comparable increases in the nation so far this year, but retailers are concerned about the future. Much of the strength in District retail sales can be traced to large farm increases in 1973 and early 1974 which have spurred retail spending outside of the Minneapolis-St. Paul Metropolitan Area. Discussions with District retailers have revealed that sales this summer were good. However, most admitted that higher prices accounted for a major part of their recent sales gains. Our contacts reported good sales of apparel and home improvement items and declines in big ticket merchandise such as furniture and major appliances. Freezers and similar items are in great demand and in very short supply. District retailers are cautious in assessing their fourth quarter sales outlook and some fear was expressed that this year's short Christmas shopping season might cut into their business.

Automobile sales in July, August, and early September were exceptionally good, according to a survey of regional sales managers. Despite large sales in the last two months, cumulative sales for 1974 are still below those for 1973, however. On the other hand, truck sales continue to run well ahead of last year. The supplies of large luxury cars are very low in the District. Current inventories of smaller cars are greater than normal, but dealers say they are confident of selling them once the higher priced 1975 models are on the market. Automobile dealers are worried about the impact of the 1975 model prices on their sales and that current high sales of 1974 models might cut into their future sales.

District resorts reported a very good summer and look for business to remain good. An increase in business by local people and group vacationers this summer was noted by several resorts. They also reported that family groups stayed longer than in the past. With regard to their winter recreational business, resort owners are anticipating a very strong winter season and report that reservations are well ahead of last year's at this time.

Residential construction is off in the District but not as severely as in the nation. The number of housing units authorized in the District for the seven-month period ending in July was 9.5 percent lower than those for the same period a year ago, as compared to a 38.4 percent decline nationally. Savings inflows have been off at District thrift institutions, and mortgage lending has declined. Mortgage loans made by Minneapolis and St. Paul S&L's in August were 41 percent below the August 1973 level. Interest rates and nonprice terms of mortgage loans made by Twin Cities financial institutions have stiffened during the past three months. Despite a substantial cutback in recent months, outstanding loan commitments at District S&L's are at a high level due to the large volume of commitments made in early 1974 when savings inflows were unusually heavy and were expected to continue at a higher rate.

Business loan demand continues strong at District banks and no letup is foreseen. Discussions with the three largest banks in the Minneapolis/St. Paul area indicate that they consider their loan demand strong and foresee no change over the near term. Consequently, these banks are raising interest rates and tightening other terms and conditions on new commitments. The outlook for loan demand at District rural areas will be largely influenced by farm income developments. Because of lower net incomes, spending on capital items and consumer durables will fall, resulting in lower loan demand for such purposes. However, refinancing needs will increase to cover production costs not met by the year's income. In addition, feeder cattle loans will be soft for some time, but ranchers may demand more credit to cover holding their cattle over the winter months.

TENTH DISTRICT - KANSAS CITY

Tenth District firms are now facing less of a "sellers' market" for materials inputs than they did only a few months ago. Supplies are more readily available, and price increases are moderating somewhat. With business weakening, inventory growth is being watched more carefully and purchasing policy is becoming less aggressive. In agriculture, concern over frost-damaged crops and the possibility of export controls have created uncertainty over future feed costs, but the picture for profits in the livestock industry and for food prices remains gloomy. Loan demand at Tenth District commercial banks is holding up fairly well, with business and consumer instalment loans up, and farm loans and loans to financial institutions down.

Results of a survey of purchasing managers in the Tenth District suggest some easing in both the availability and prices of materials. These tendencies are not evident across the board, as some industries and some commodities are still faced with short supplies. The contrast with only a few months ago is evident, however, with a significant number of respondents now reporting shortening lead times, improved availability, some moderating in the number and degree of price increases, and a lessening in the use of allocations. As a result, several firms report that they are pursuing a less aggressive purchasing policy. Inventory accumulation targets are also being reduced in some instances. There is a definite indication that part of the change is due to current and anticipated slowdowns in demand for these firms' output.

Textiles, corrugated paper, and some chemicals were specifically listed as being more readily available to purchasers. The supply situation for iron and steel does not show as much improvement as for other goods. A major manufacturer of offroad vehicles reports very little improvement in either availability or lead times of many important items. Other firms, however, do report some slight easing in steel with allocations larger and lead times down a little. One respondent reported that reinforcing bars and mesh have become much easier to get.

With certain exceptions--mainly in metals--the purchasing managers are leaning toward a less aggressive purchasing policy. For example, one respondent said his firm was no longer "taking everything we can get, as was the case six months ago." All of them seem to be keeping a close watch on their inventories, with an eye to paring them down in light of a weakening business situation. At the same time, the experience with shortages and allocations appears to be pushing up the level of what is viewed as "normal" real accumulation. Inventory reductions will be selective and cautious; one respondent says his firm is "comfortable with most of the excess."

The majority of respondents believe themselves to be facing less of a "sellers' market" than in the recent past. Although prices generally are still rising, increases apparently are somewhat smaller and less frequent and cover fewer items. (Two makers of steel products noted that prices in the "gray" market have fallen sharply.) A firmer stand by purchasing agents is credited with having some effect on the price situation. Yet price at time of shipment seems to be more the rule than the exception. Moderation in price increases is not universally reported, however. A tire manufacturer reports "terrible price increases (for materials) in the past 90 days," with more expected to come.

Reversing a recent trend, farm prices declined 2 percent for the month ended September 15, with cattle, hogs, soybeans, and corn contributing most to the decrease. However, growing concern over the frost-damaged crops in much of the corn belt has resulted in significantly stronger grain prices since mid-September, portending another year of high feed costs for livestock producers and rising food prices for the consumer unless various measures are taken to slow export demand.

Even assuming export controls and a decline in grain prices, profits in the livestock industry will likely remain small for the next several months. Hog producers are responding by reducing farrowings and liquidating brood-sows while cattle feeders are increasing the culling rates for cows. Since adjustments proceed more slowly in the cattle industry, beef supplies should remain adequate through 1975, but pork supplies are likely to be off substantially, pushing prices up.

In the District, the planting of the new winter wheat crop is progressing well. Most of the seeded acreage in the southern half of the region has germinated and is growing. Moisture conditions are generally excellent, although parts of western and central Kansas, where some wheat was "planted in the dust," need rain to assure a stand. Rain also is needed in Nebraska where the wheat is now being seeded.

Tenth District bankers contacted this month were divided in their opinions about the strength of loan demand but in general they thought demand was holding up fairly well. Reports indicate that consumer instalment and business loans continue to increase, but farm loans and loans to financial institutions have declined. Some of the decline in farm loan demand is due to liquidation of inventories by cattlemen.

Many of the bankers surveyed indicated there has been some tightening of loan policies, such as a reluctance to make term loans. It appears that tighter loan policies have been selectively applied. Loans to new customers have been discouraged. Also, term loans are being discouraged to avoid being locked into present interest rates in case interest rates should rise in the future.

ELEVENTH DISTRICT - DALLAS

Growth in business loans at commercial banks in the Eleventh District has abated since midsummer as bankers reportedly have tightened lending policies in an effort to avoid further reducing their liquidity positions. Nonetheless, loan officers report demand has remained strong, and they have encountered only minimal resistance to high interest rates, mostly by smaller borrowers. Tight conditions in capital markets have resulted in considerable demand pressures on banks as companies have relied more heavily on bank credit lines for capital expansion. Much of this borrowing was originated on a short-term basis, and these loans have been rolled over as customers have been unable to secure long-term funds in the bond and equity markets. In addition, high prices for some raw materials have also contributed to a greater loan demand as businesses have tried to build up inventories of scarce materials.

Lenders are relying on greater selectivity in granting loans rather than raising interest rates to hold down borrowing. Bankers report they are closely screening loan applications, and typically only requests by old customers are considered. Moreover, all "speculative type" loans, particularly construction loans, are being discouraged.

All of the bankers surveyed said they are not actively seeking new consumer loans because of the low profit margin available under state interest ceilings. They are, however, attempting to accommodate their old customers. Much of the recent strength in consumer borrowing reflects personal loans to maintain current living standards, including the greater use of bank credit cards. However, automobile loans are up substantially, and some bankers report a rise in borrowing to purchase recreational vehicles.

Commercial builders in the District warn of a severe curtailment in nonresidential construction activity in coming months. Most builders interviewed feel commercial construction has held up fairly well because of the long completion time required for most projects--typically more than a year. But as jobs are completed, builders are finding little new work--as evidenced by the 50 percent drop in nonresidential building permits in the past three months.

Real estate loan officers at leading District banks generally agree that the outlook for commercial building is bleak. Obtaining interim financing is "nearly impossible" according to contractors, although some long-term financing is believed to be available. But the increased restrictions on loan requirements have sharply reduced the number of all loans granted. None of the bank loan officers interviewed will make interim loans unless builders have an "ironclad" commitment for long-term financing that completely covers the cost of construction. As a result, new commitments are reported to be at less than half the level of a year ago. But some banks have experienced much sharper declines and claim new commitments are at a "standstill." For example, a large bank in Houston has made only one new commitment in the last month.

Even when funds are available, the cost of borrowing is often prohibitive. Larger banks in the District are currently charging 14 to 15 percent on interim loans plus a 1 percent a year fee. And most builders cannot make a profit on these terms. Even the cost of the available supply of long-term funds has rendered many projects economically infeasible. In El Paso, for example, two development projects were canceled because permanent financing was so expensive that construction could no longer be justified.

Manufacturers of chemicals and plastics report no letup in the heavy demand for their products. Because production is running at full capacity, unfilled orders have reached the highest level in the history of many of the firms contacted. Most manufacturers have been forced to allocate their output among old customers and are not taking orders from new buyers. Shortages of raw materials for industrial chemicals and plastics have eased somewhat, and some leveling off in prices was reported. Fertilizer production, on the other hand, is still hampered by shortages of nitrogen and phosphate. Capital spending plans remain strong in these industries with only minor revisions due to high financial costs.

Steel producers report that while overall demand is heavy, there has been a letup recently in new orders for reinforcing steel rods and oil field pipe. The decline in construction activity, first in residential building and then in commercial building, accounts for the softening in the demand for reinforcing rods. However, the big accumulation of field pipe inventories represents months of overbuying by the petroleum industry to hedge against possible shortages of drill pipe. However, even in these product lines, steel manufacturers plan no letup in production this year in order to rebuild badly depleted stocks of their own inventories of finished goods. Therefore, faced with capacity limitations and improved availability of scrap metal, firms are going ahead with ambitious expansion programs despite tight capital markets.

TWELFTH DISTRICT - SAN FRANCISCO

Our Directors report continued concern over the inability of government to control inflation. The general trend of economic activity exhibits little change from recent months. Housing construction remains weak and the lumber and plywood industry is cutting employment. Agriculture in the District, except for beef, is experiencing an excellent year. Business investment remains heavy although some planned expenditures may be revised downwards. Banking conditions reflect the economy and are basically unchanged with good loan demand but little change in deposits.

The difficulty of controlling inflation remains the major policy concern of our Directors; there is a need for more strenuous efforts by the Federal Government to reduce its budget deficits in order to reduce the burden on the Federal Reserve. Directors support a steady monetary policy integrated with use of all the powers of the Federal Government to control inflation. An additional concern of some Directors is the need to prevent any failures of large banks in view of a growing uncertainty about the soundness of the banking system. Failures would have a domino effect on small banks who have purchased CD's of the large banks.

General conditions in the economy do not appear to have changed. Consumer spending is reasonably good, but there are weaknesses in spending for durables and a decline is expected in automobile purchases. The weakest section remains construction. Housing construction shows no sign of recovery, and further declines in apartment construction are reported. Public construction is lower in several states because of higher interest and other costs.

Most of our Directors reported little or no change in investment plans in their regions, and overall, investment activity appears to be strong. However, instances of revisions in plans are reported by several Directors. Public utilities are having difficulties in floating issues. One large utility has made major reductions in its long-term construction budget, reportedly cutting $1 billion out of planned capital budget between now and 1985. Rising construction costs have also led other firms to revise their plans. For example, a large California dairy cancelled a project originally estimated at $3-1/2 million when the estimate was revised to $5 million. Other firms have postponed projects in expectation of lower interest rates next year.

Recent increases in capacity are beginning to reduce supply shortages. One bank reports that California electronics components manufacturers in San Mateo and Santa Clara counties have expanded capacity sufficiently so that supply now nearly matches demand. In petrochemicals, some price cuts have occurred already due to the emergence of excess supply. In the steel industry, demand is still high, but it may not remain so. The price differentials between U.S. and foreign steel prices have narrowed, and foreign competition is becoming more serious. There is still a waiting period for steel and users must accept a restricted allocation. However, some buyers have cancelled their steel order allocations, and this action often indicates a softening in demand. At the moment, the majority of our Directors think sales of automobiles in 1975 will be weak. Recent price rises have stimulated sales of leftover 1974 models, but this is expected to be at the expense of 1975 sales. In addition to higher posted prices, problems of obtaining finance and the prospects of higher gasoline prices are also discouraging buyers. Dealers are receiving requests for 48-month contracts by customers. Foreign car demand is not likely to be better either, particularly since U.S. compact car prices are reasonably competitive. Japanese cars remain in the best position in terms of sales activity, but European sales are lower; domestic truck sales, in contrast, appear to be good.

Agricultural prospects in the District are reported to be excellent. Ten percent smaller crops are reported for wheat, potatoes and apples, but price rises more than offset the lower production, and farm income continues to grow. The only exception to this picture is beef, where producers face rising costs with unchanged demand.

Bankers report loan demand is strong but deposits show only slight change. Some banks have experienced a shift from demand to time deposits, and others report a continued drain of deposits because of small investors shifting to government or government guaranteed issues.