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CURRENT ECONOMIC COMMENT BY DISTRICT

Prepared for the
Federal Open Market Committee
by the Staff

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SUMMARY*

The general thrust of this month's comments is that the economic situation has deteriorated and further weakening is in store. Unemployment seems likely to rise again in February, on the basis of widespread reports of more layoffs since early January. Slackening conditions in the labor market, however, have done little thus far to curb wage demands, according to New York and Chicago. On the other hand, the recession appears to be having a depressing effect on prices, perhaps even more than the indexes suggest. The overall impression of the District reports is that the recession has become more pervasive but there are regional and industry sources of strength in the nation's economy. Reduced natural gas supplies, mentioned by Cleveland and Richmond, have contributed to cutbacks in industrial production and employment. Housing remains in the doldrums throughout the nation, retail trade generally continues to be sluggish except for a pickup in new car sales, the capital goods sector is showing signs of further weakness, and excessive inventories remain a problem for many firms. A number of Districts report instances of inventory liquidation underway. At the moment there seems to be little optimism regarding prospects for an early recovery. In one of the more bearish reports, for example, Boston points to growing fear of a "second tier" in the recession; its academic correspondents are particularly concerned over the state of the economy. Alternatively, there are some encouraging items. Philadelphia reports that more than half the manufacturers in its survey are optimistic for the outlook six months ahead. Richmond says there seems to have been a break in the mood of pessimism which has prevailed over the past few months, with an increase in the proportion of their survey respondents expecting an improvement

* Prepared by the Federal Reserve Bank of Cleveland.

in business activity in the next six months. Atlanta mentions a rebound in tourism in Central and South Florida, and that businessmen seem to have a renewed air of optimism since the first of the year.

In the consumer sector, heavy sales promotions and price-cutting have had limited success stimulating retail trade. Sales are described as weak or sluggish in virtually every District. The auto manufacturers' rebate program has made new car sales an exception, but as Chicago notes, has not brought about a boom. Atlanta adds that some dealers worry about what will happen when the rebate program ends. Philadelphia says retailers are pessimistic about the near-term outlook, and Boston reports that retailers are growing more cautious in their ordering. New York and Richmond say some progress has been made reducing excessive retail inventories.

In the capital goods sector, several industries are still operating at a high level. Chicago says large order backlogs are maintaining output of equipment for coal mining, oil well drilling, rail transport, ore boats, heavy agricultural operations, and chemical processing. Orders for many other types of capital goods have dropped sharply, however. Philadelphia reports that capital spending plans have been cut back in the retail sector, but are holding firm in manufacturing. New York and Cleveland see signs of weakening in capital spending. Richmond and Atlanta mention little scaling down or retrenchment in spending plans. In New England, firms say most investments are planned for such purposes as cost reduction, replacement, and compliance; plans for expansion are nil. San Francisco commented that an increase in the investment tax credit would not help capital spending until late 1975.

The agricultural outlook for soybeans and feed grains appears to be encouraging, according to Dallas, St. Louis, and Richmond. Despite recent declines in crop prices, there is still enough incentive to increase production plans. The sharp drop in cotton prices is causing a switch from cotton to soybean production. Kansas City, Dallas, Minneapolis, and San Francisco all comment on the difficulties of livestock producers, many of whom have gone bankrupt.

Among Districts commenting on banking developments, Philadelphia says prospects of large defaults in loans are concerning bankers. Dallas says that most banks have increased reserves for loan defaults. It also reports that delinquencies on farm loans have risen. No District reported any strength in business or consumer loan demand. Demand deposits have declined generally.

Thrift institutions continue to have net savings inflows, according to Dallas, St. Louis, Atlanta, and Cleveland. Chicago notes a dropoff in savings inflows in late January.

FIRST DISTRICT - BOSTON

The outlook is unsettled. Previously, our directors felt comfortable in attempting to fix the timing of the 1975 economic rebound; now they are more insecure and uncertainties cause them to dwell on short-term developments. In December, the New England unemployment rate moved up by .7 percent from the previous month to 9 percent; a year earlier, 6.5 percent of the labor force was unemployed. The Massachusetts unemployment rate was 9.9 percent in December.

Retail sales in the region are not reassuring the directors. In some markets, inventories are very heavy, according to year-end statements. Those firms which were able to report higher revenues note that they were reasonably successful in selling their way out of stock. However, their fortunes are attributed to capturing a larger share of their specific markets, declining auto sales, their offering good values (very aggressive promotions and liquidations by manufacturers are critical here), and, possibly, trading against spring sales. These factors do not contribute to sanguine forecasts. As the unemployment figures are released and as major local manufacturers continue to announce extensions of furloughs, cutbacks, and layoffs, the retailers are growing even more cautious in ordering and planning.

The directors report that most investment in the region is tied to things one "must" do: cost reduction, replacement, compliance. Expansion is nil, and there is worry that today's musts could be tomorrow's luxuries.

A major national firm was recently required to face red tape to get a $1 million loan at an aggressive regional bank. Previously, the red carpet would have been shown. Now, the bank is not sure it wants the business.

There is a growing fear of realizing a "second tier" in the recession. The directors are attempting to determine whether this recent experience is a "flushing of the pipelines or a snowball." Continuation of dreary prospects may lead to further substantial reductions in growth targets for firms and banks introducing another drop in economic activity. Desirable or not, much business is looking to Washington to lead the economy from the slump: a helpless passive attitude is gaining ground.

Our academic correspondants, Professors Samuelson, Solow, Eckstein, Tobin, and Duesenberry, all agreed on three points: 1. The economy is in a serious downward spiral, 2. The proposed tax cuts are insufficient to ensure a recovery, and 3. The Federal Reserve must pursue a more aggressive expansionary policy. Several economists also predicted restrictive monetary policies would unleash a strong political backlash against the System.

All the economists emphasized the severity of the current recession. Eckstein said that for the first time since the 1930's, we are in a pure Keynsian spiral of falling incomes and employment. There is no certainty, he concluded, that the economy will generate an upturn. Tobin characterized the economy as in an "emergency situation". Solow believes that all the current forecasts are too optimistic. Samuelson said that the economy is giving only one signal: it needs strong fiscal and monetary stimulus.

The proposed tax cuts were viewed as inadequate. Tobin pointed out that fiscal policy will be snarled up in Congress for some time, while the need for stimulus is immediate. Like Duesenberry, who argued for $30 billion in tax cuts, Tobin felt that a $16 billion cut was not enough. Samuelson felt that Ford had a minimal program and that the $7 billion tariff would do more for depression than the tax cuts would do for recovery. Solow felt that the budget was inadequately expansionary and that expenditures should be increased.

The long lead time on expenditures would be no problem, he noted, since we are at least 3 years away from full employment.

On monetary policy, the call was for expansion. None of the economists were impressed with the fourth quarter reserve growth as a reason for not pushing harder to get interest rates down and money supply growth up. Tobin argued that if it is true that demand is not out there, then it cannot do any harm to push reserves out. There is plenty of time to sop up any reserves during a recovery. While he would not be upset by 12 percent growth in M_1, if that is what is required to keep interest rates from creeping up, he is personally skeptical that the federal deficit will require it. He thinks the problem has been blown out of all proportion. He sees corporate borrowing as refinancing, not as an additional drain on savings.

Samuelson echoed the same theme. He argued that getting reserves out isn't the job. One cannot take the multiplier as given. If the multiplier is low because demand is weak, the Fed has to push out even more reserves. He noted that Friedman's criticism about Fed actions during the depression was not that we did not get the reserve out. The Fed did, but it did not push out enough, given a falling multiplier. The real question is whether we forsee too much demand in 8 months. If not, he argued, we can not effectively say that by doing too much now, then the money will be out there to haunt us. When velocity picks up, we should take the money out. The worst of all possible worlds is for the Fed to stick to one policy too long.

Duesenberry thought that financing the deficit might cause a temporary spurt in money supply growth, but that we should not let this be an excuse for letting rates creep up. He believes open market rates should be down a bit more and kept there.

Eckstein argued that it was foolish for the Fed to delay in getting rates down. Eckstein agreed with Tobin that the Fed needed to do something dramatic and immediate. Eckstein said the Fed should stop decrying the deficit and should say straight out that the economy is in danger of a depression and that the Fed will do whatever it can to prevent it. He felt that at this time, it was not constructive for the Fed to be concerned about banks' capital adequacy. Our concern should be to help businesses re-establish their liquidity. Both he and Solow thought it was time for the Fed to begin buying long-term securities--either agency issues or corporate bonds--as a means of helping business liquidity and reviving investment.

SECOND DISTRICT - NEW YORK

The picture that emerges from the views expressed by Second District directors and other business leaders who were contacted recently is one of further declines in economic activity. Consumer demand has been generally sluggish, although aggressive sales promotions and cutbacks in purchases from suppliers have enabled some merchants to reduce inventories. Business capital spending plans are being scaled down. Unemployment is rising rapidly, but most respondents have observed little or no moderation in wage demands. They did note, however, some indications of a slowing of the rate of price increases.

Concerning consumer spending, District retail sales appear to have been running below the nationwide average, with the New York City retail sales picture showing particular weakness. An official of a trade association thus reported that business at the City's department stores was about 4 percent lower in dollar terms this January than in January 1974. He stated that traffic at the major stores was down significantly, and that there seems to be considerably less "impulse" buying. Similarly, an executive of a high quality New York City department store with branches in the suburbs reported that sales by his firm have been running behind last year in real terms and have been "struggling" along to maintain the same level in dollar terms. He noted, however, that business was somewhat better at the firm's suburban branches. Some New York City retail merchants did report that sales and promotions have been fairly successful in attracting business. These sales have covered a much wider range of merchandise than usual, including goods that normally would not be placed on sale until spring, and have involved significantly greater price concessions than usual, with a resulting decline in profit margins. At the same time, the respondents reported that merchants have significantly cut their own purchases from their suppliers and that these cutbacks have helped to reduce retail inventories. Similarly, the Buffalo branch directors observed that merchants in Western New York have met with success in moving goods and in reducing inventories to manageable levels. This has been achieved, however, only through sharp markdowns with correspondingly adverse effects on profitability.

Reduced demand, according to a number of respondents, appears to be putting some downward pressure on prices. Among others, the president of a large nationwide retail organization stated that prices of basic raw materials and of some intermediate goods have softened considerably and that, while posted prices of most finished consumer goods were holding firm, consumers were benefitting from the sales promotion programs mentioned above. The chairman of a large New York City bank stated that there was growing evidence that prices were now rising much less rapidly, and that in view of sales promotions and discounting the official price indices were probably overstating the rate of inflation. A number of top officials of industrial firms mentioned price reductions in their industries, including textiles, wood products, and some metal products. It was also noted, however, that prices of other products, including auto parts, paper and certain chemicals, were remaining firm.

Concerning capital spending, the respondents in general agreed that the outlook had weakened significantly in recent months. Among others, the New York City banker mentioned above looked for further cutbacks, especially in consumer goods industries. Another director felt that while many businesses are committed to capital programs for 1975 and 1976, they are hesitating to make commitments beyond 1976 at this time. The Buffalo directors in general agreed that 1975 capital spending plans were sharply cut in the latter part of 1974.

In their views, firms experiencing drastically reduced sales have no alternative but to further cut back from their planned capital spending during 1975 in order to cope with worsening liquidity problems.

Unemployment in the Second District has continued to rise rapidly. New York City, northern New Jersey, and Buffalo have been especially hard hit, with unemployment rates well above the national average. In the view of most respondents, however, the rise in unemployment has thus far exerted little moderating influence on wage demands. This view was summed up by the Buffalo branch directors who felt that while rising unemployment may be having a moderating effect on upward wage pressures in nonunionized small to medium sized firms, there was no evidence of a less aggressive posture by the large unions representing workers in major industries. Indeed, it was noted that some union leaders are "preparing for battle" and likely to accuse management of using the current economic slump as the basis for harsh negotiations affording labor less than acceptable contract settlements.

THIRD DISTRICT - PHILADELPHIA

Economic activity in the Third District continues its slowdown. Manufacturers report declines in new orders and unfilled orders in February, but over half are optimistic for the outlook 6 months ahead. The labor force, too, is feeling the effects of a declining regional economy. And, with the size of the labor force continuing to grow, an even higher level of unemployment in the region can be expected in the months ahead. Area retail sales also were severely damaged in January, and appear to be equally hard hit in February. Capital spending plans in the retail sector have been cutback as a result, but in manufacturing, most executives don't plan to alter current spending plans for the next 6 months. The outlook for prices remains bleak this month, as manufacturers post additional price hikes with expectations that this trend will continue for the next 6 months. And, area bankers are feeling the pinch, as loan levels and deposits drop off.

Manufacturers in the Third District responding to this month's business outlook survey report that business activity is continuing to slow down in the regional economy. Almost half of the respondents report a general decline in business activity in February. And, in their own firms, this condition is repeated. Two out of five businessmen report declines in new orders, and two out of three are posting decreases in unfilled orders. However, these manufacturers are more bullish on the future outlook. Well over half of the executives polled expect the general level of business activity to pick up by August. And, an equal number expect this general increase in the region to translate into an increase in both new orders and shipments for their own firms. Manufacturers remain mixed in their outlook for any increase in capital investment plans 6 months out, with nearly half of the respondents content to let their spending plans remain the same.

This general slowdown in the manufacturing sector is also have an effect on the labor force in the Third District. While 60 percent of the executives are maintaining a stable workforce and workweek, almost a third of the respondents report a decrease in the average number of employees and the average length of the workweek. On balance, slightly more manufacturers expect to increase their employment levels by August than expect to decrease them, but over half anticipate no change in these key employment indicators. With a new crop of graduates moving into the labor force in late spring, the regional economy will likely experience higher unemployment in the months ahead.

Our retailers too, are experiencing the effects of the declining regional economy, although the number of transactions had fallen below the level of a year ago January, retail executives have reported that the dollar volume of sales has been keeping pace with previous years. However, as of February, department store sales as measured in dollars as well as in the number of transactions, fell significantly below last year's level. And, the large discount stores, such as Sears and Penneys, were especially hard hit as they were caught with large inventories on hand. One major retailer in the area reports a policy decision to decrease employment levels in its stores through attrition, with several others hinting at similar plans. And, all retailers report that capital expenditure plans have been severely cut back. As for spring sales and the outlook for the next several months, retailers expect ever softening sales as prices continue to rise and the general level of the economy continues to decline.

Prices in the manufacturing sector, too, increased in February. Over one third of the executives polled are facing higher prices on raw materials this month than they experienced last month. And 50 percent expect to be paying even higher prices by August.

Loans at most banks are below last year's level. And, the larger Philadelphia banks report a slight softening in demand. Although most banks are generally moving to a less restrictive loan policy than they have followed in the last several months, they are moving cautiously. The prospects of large defaults coupled with difficulty in collections in a declining economy are weighing heavily in their decision. Demand deposit growth is generally disappointing and only savings instruments guaranteeing 7 percent interest or better are attracting new time deposits.

FOURTH DISTRICT - CLEVELAND

Economic conditions in the District deteriorated significantly last month, and further weakness is expected. Layoffs and shortened workweeks are widespread. It appears many industries are liquidating inventories, although some steel and machine tool firms say they need to rebuild stocks. Signs of weakness are spreading in the capital goods sector, and demand for steel is softening. S&Ls continue to have savings inflows, but mortgage loan demand is weak and housing is still declining.

Early returns from our monthly survey of District manufacturers indicate a further sharp deterioration in business during January. Many companies reported declines in new orders, shipments, and backlogs; and inventory liquidation, underway last month, apparently continued. The proportion of firms paying higher prices eased for the fourth consecutive month. One clothing manufacturer said sales and new orders are so low, and inventories so high, that it is not purchasing and therefore cannot take advantage of lower prices quoted by its suppliers.

Employment and hours worked continued to drop in January, and unemployment seems likely to rise further in February. Several large firms announced temporary or indefinite layoffs beginning in late January or February. In the Pittsburgh area, a 40 percent reduction in the amount of natural gas available for industrial use (effective January 1) has caused some layoffs--concentrated in the stone, clay and glass industries. Other firms are shortening workweeks. In the Akron area, for example, many tire company employees who usually work a 6-day week of 6-hour days have gone to a 5-day week and some to 4-day and even 3-day weeks.

An economist for a major tire company reports that further weakened sales have lifted inventories of tires to a 9-month supply compared with 6 months recently. Production has finally been cut below sales and additional layoffs are likely, although the worst seems to be over. Demand for chemical products has dropped sharply since November, resulting in a rapid buildup of stocks. Production has been cut in line with reduced sales and output appears to be leveling off. One firm intends to reduce planned 1975 capital spending by stretching out some programs. The firm wants to avoid any further depression of its debt-equity ratio.

Signs of weakening in the capital goods sector are spreading. A major heavy-duty truck manufacturer in Cleveland recently closed its plant for a week, and reopened with operations reduced by one-third. Truck suppliers and some machinery firms are laying off workers. A major machine tool company in Cleveland said cancelled machine tool orders exceeded new orders in January for the third consecutive month. The firm's economist noted that backlogs through mid-1976 and the need for inventory rebuilding preclude any decline in employment. This economist, a highly regarded analyst of capital spending, added that he expects the rate of decline in real capital spending to continue during the first half and to increase in the second half.

Another major machine tool producer reported that new orders have weakened recently but are still running close to the firm's shipping rate. Although cancellations have increased, back orders stand at 15 to 18 months. The firm has not changed its capital spending plans. Its inventories have improved but are still unbalanced, partly because of continued shortages of some materials, notably castings. This firm is still hiring and working a 48-hour week.

A major electronic and printing press producer reports orders for presses fell sharply in January following a strong volume of bookings throughout the second half of 1974. The decline was attributed to uncertainties over the investment tax credit. Demand for the firm's electronics products, such as radio and TV broadcasting equipment and computer components, is still strong, with January bookings 10 percent above December 1974 levels. Capital spending plans for 1975 have not been curtailed because of the recession, although the firm may stretch out as much as $1 million of its $16 million increase planned for this year. Stocks are being reduced gradually and are in better balance than they were at the end of the third quarter. No drastic cutbacks in stocks are anticipated because order backlog is 15-20 percent higher than last year.

The treasurer of a multinational firm that produces office equipment reported orders have fallen sharply recently, from both domestic and foreign sources. The firm has laid off about 1,000 of its 16,000 workers since December 1 because of declining sales and large inventories. Inventories are considered excessive, but production is thought to be near the bottom of a "U"-shaped pattern.

Demand for steel is weakening, according to three major steel firms. Customers are cancelling or deferring delivery on old orders, and pushing back delivery on new orders. However, there is still substantial strength in the steel industry stemming largely from oil, coal mining, railroad, and farm equipment producers. One steel firm heavily dependent on the automotive and appliance industries has begun laying off workers and reducing the workweek. Steel output in Cleveland has declined recently because a blast furnace at one mill cracked last month. It will probably be March before repairs are completed. The firm is receiving poor quality metallurgical coal resulting in production inefficiencies. Another large steel firm reports bottlenecks in production because of natural gas shortages and because they have operated at full capacity for 2 years without sufficient maintenance.

Demand for mortgage loans is seasonally weak, according to some banks and S&Ls in Cleveland. Officers attribute weak loan demand in part to a lack of consumer confidence but also apparently to little easing in mortgage terms. One major bank requires 40 percent down on a 20-year loan, with an interest rate of 9 1/4 percent. Loans with less than 40 percent down are not encouraged. In contrast, some S&Ls are actively soliciting mortgage loans, following 3 successive months of net deposit growth. A $150 million deposit institution that offers a variable rate mortgage is actively seeking loans but has found fewer takers than it wants. Housing starts continue to plummet.

FIFTH DISTRICT - RICHMOND

The January survey of Fifth District businesses reveals further deterioration of business conditions. Reports from across the District indicate continued economic weakness exacerbated by spot shortages of critical energy supplies. Unemployment has reached or is approaching record levels in many areas and pockets of severe unemployment are becoming more common. The responses of manufacturing concerns show continued weakness in new orders and further declines in shipments and backlogs of orders. Reports of plant closings and layoffs continue across a broad range of manufacturers. Survey responses indicate a further accumulation of finished goods inventories and growing concern over present levels. Commercial and industrial loans at District weekly reporting banks declined sharply in January; real estate loans are exhibiting a gentle but persistent rise while consumer loans remain sluggish. In the agricultural sector, changes in relative prices during 1974 appear to be altering the prospective crop mix for the coming planting season, with major shifts from cotton to soybeans and feed grains.

Manufacturers' responses to our latest survey reveal the continuation of several presistent trends. Over 70 percent indicate further declines in backlogs of orders and almost as many report reductions in the volume of new orders. Meanwhile, over 50 percent report a decline in the number of employees. The volume of shipments continues weak and although the number of employees and hours worked per week are down, inventories of finished goods remain firm. Over 60 percent of the manufacturing respondents view current inventory levels as excessive, compared to about 50 percent a month earlier. Almost half of the manufacturers surveyed consider current plant and equipment capacity excessive, but fewer than 10 percent feel current expansion plans should be cut back.

From around the District reports of plant closings and layoffs continue across a broad range of industries. Recent announcements involve such industries as printing, chemicals, shipbuilding, electrical equipment, and rubber. Meanwhile, actual and potential disruptions of natural gas supplies are contributing to uncertainties in parts of the District.

Our survey of District retailers yields much the same picture. Sales declined in January following an increase in December, while sales of big ticket items continue weak. Responses indicate a reduction in retail inventories for the first time in 7 months, although 50 percent of the retailers still view current levels as excessive. An exception to this situation seems to have developed with regard to sales of new automobiles. The sales policies initiated by the manufacturers have given a significant boost to sales in this sector.

Although no trend is discernible at this time, there is some indication of a slowing of price increases. Of the manufacturers surveyed, 35 percent report paying higher prices, down substantially from recent months. At the same time, over 30 percent received lower prices during January. Retailers report paying and receiving higher prices generally, but such reports are not nearly so common as in recent months, indicating a significant improvement over the last half of 1974. In addition, there seems to have been a break in the mood of pessimism which has prevailed over the past few months. The diffusion of responses reveals some cautious optimism, as more respondents than in recent surveys see an improvement in business activity over the next 6 months.

Lending activity at Fifth District banks appears to have stabilized in January, while interest in investments increased. The level of seasonally adjusted loans at District member banks was almost unchanged from the December 1974 level. Seasonally adjusted bank credit at District member banks showed a net increase after declining in December. The unadjusted data for weekly reporting banks show that commercial and industrial loans have declined at a fairly rapid pace since the beginning of the year. Bankers' acceptances, however, have resisted the general decline, increasing about 100 percent over the month. Real estate loans at weekly reporting banks continue a gentle but persistent rise while consumer loans remain sluggish. Member bank borrowings were at the lowest level since January 1973 following the seventh consecutive month of decline. Savings at District banks seem to have slacked off in January following increases in December.

By and large, last year turned out to be a fairly good crop year but not an exceptional one. Output of some of the major crops was below the record levels a year earlier. But crop prices were generally higher, and value of production of all District crops totaled $3.5 billion--23 percent above 1973. Farm real estate values per acre continued to advance during the year ended November 1, 1974, with increases in District states ranging from 14 to 32 percent. The rate of increase in each state, especially in Virginia and West Virginia, slowed substantially after March 1, however. District cotton producers, reacting to the sharp drop in market prices last year, have indicated that they will plant only about half as much acreage in cotton in 1975 as they did a year ago. Growers' plans to increase soybean plantings 8 percent and feed grain acreage 2 percent will more than offset the severe cut back in cotton, however.

SIXTH DISTRICT - ATLANTA

Economic prospects in the Sixth District economy appear to be turning cautiously optimistic. Layoffs are still being reported but not of the magnitude of the past few months. Local area businessmen and directors' opinions are mixed concerning the impact of automobile price rebates and post holiday retail sales. Generally, sales seem to be holding up better than previously expected. Besides auto rebates, several other instances of price cutting were reported again this month. Industrial and commercial investment plans, despite some retrenchment, remain reasonably strong in the face of last year's weak economy and little improvement yet this year.

Unemployment in the District continues on the rise, as it does nationally, but the extent of the rise varies throughout the region. Florida and Georgia have been hardest hit, and unemployment rates in these states are higher than the nation's. Both states are typically well below the national unemployment rate. Alabama and Mississippi, though showing some increases in unemployment, seem to be holding their own. For example, Alabama steel producers are turning their backs on new customers; producers indicate that their books are full through 1975. Union Carbide Corporation announced a large expansion ($9 million) at its steel mill in Gadsden, Alabama. Bessemer freight car building plant, the world's largest and most diversified facility of its type, is booked solid with orders through this year. Reports of job layoffs are fewer and more scattered than in the previous 2 or 3 months. South Central Bell will lay off 250 employees in Alabama and will trim capital spending by $82 million. A large Florida truck-trailer company has laid off one-half its work force. Three hundred workers will be furloughed by the Tennessee Valley Authority. A Louisiana paper mill which makes liner board used by many national companies has closed down, idling 335 workers. A large plywood manufacturer has also recently shut down its facilities. North Georgia's carpet industry has recently predicted that 1975 will be a better year than previous bleak forecasts have indicated. At a recent carpet industry meeting, an industry representative reported that January 1975 sales surpassed those of a year ago. Alabama's textile industry is also expecting a good year.

Regional auto dealers are reporting improvement in sales as a result of the rebate programs. Florida directors indicated that sales are up from previous months but still below year-ago levels. Sales are restrained, however, by the availability of credit. Showroom traffic has been very heavy. However, heavy-duty truck sales have fallen to the lowest point in many years in Central Florida. New Orleans directors report mixed responses to rebates. A New Orleans area director noted that the rebates have materially enhanced showroom traffic but not new car sales. A Mobile, Alabama director reports that the rebate has boosted sales significantly and that dealers are very enthusiastic. Three Baton Rouge, Louisiana car dealers indicated that the rebates were responsible for 50- to 100-percent sales increases. But it was interesting to note that each of the three dealers stated that they are now worried about what will happen to auto sales when the rebate program ends. A survey of Alabama auto dealers indicates that rebates have caused great increases in showroom traffic and substantial increases in sales, in some cases over 100 percent at 23 major dealers around the state. It was also reported that several large Alabama industries with ties to the auto industry were giving $100 rebates to employees who purchased new cars.

Retail sales seem to have held up fairly well in January. Directors' responses to questions regarding the extent preholiday sales campaigns siphoned off January sales were mixed. At least two reports of strong January sales were received. One indicated that retail stocks were the lowest in years, creating a problem until spring delivery of merchandise. A Central Florida retailer, however, believes that December sales promotions did eat into January sales. Louisiana directors reported that retailers were satisfied with January sales levels. Apparently, December promotions did not drain January sales. A report from the Alexandria, Louisiana area, however, indicates that retail sales are sluggish and not responding to intense price promotions.

Last month we reported a surge in holiday tourist traffic in Florida. In early January, tourist activity fell off drastically but has rebounded again, at least in Central and South Florida. One director reports that businessmen in central Florida seem to have a renewed air of optimism since the first of the year.

Besides the car rebates, several instances of price cutting were noted. A South Florida area retailer indicates that at present inflation is dead in soft goods. He notes that there is weakness in both apparel and textile goods prices. An Alabama apparel retailer indicates that while leisure wear is selling well, men's clothing is one area where inventories remain abnormally high. He notes that they are now in a whole new ball game for clothing manufacturers; they have adjusted their thinking, and it appears now that prices for fall 1975 will be reduced from fall 1974 prices. There is considerable price cutting on Florida's housing, condominium, and rental-unit markets. Direct cuts have appeared in resale markets, while discounts, "free gifts," no leases, no deposits, and low early-months' rent are being offered on new home and rental housing. One Florida director reports that 55 townhouses previously priced in the $55,000-range were reduced to $36,000; within a week they were all sold.

Savings inflows continue at savings and loans throughout the District. These institutions, particularly in Florida and the Atlanta area, are now beginning to seek new mortgage commitments. Rates have been reported in the 8 3/4- to 9-percent range by some savings and loans.

SEVENTH DISTRICT - CHICAGO

The general business decline in the Seventh District continues with no reversal in sight. Virtually all industries, with producers of heavy capital goods still an exception, are laying off workers, cutting production schedules, and reducing inventories. Pessimism among consumers, businessmen, and lenders is deep and almost universal. A general realization exists that this decline is far more pervasive than earlier postwar downturns. Mortgage funds are now more available, but there is no indication, as yet, of a revival in residental construction.

Large order backlogs are maintaining output of equipment for coal mining, oil well drilling, rail transport, Great Lakes shipping (mainly large ore boats), steel mills, agriculture (at least heavy equipment), and chemical processing. On the other hand, output of some equipment has been reduced sharply, including lighter farm and construction equipment and heavy trucks. These sectors had been strong until the fourth quarter. Orders for many types of equipment components (e.g., mechanical controls, small motors, axles, and transmissions), which had presented bottlenecks through much of 1973 and 1974, have dropped very sharply in recent months.

Shortages of certain types of bearings and hydraulic and electrical components continue, and steel plates and structurals are still on allocation, but such reports are much less frequent. Prices of some industrial supplies, including specialty steels and fuel have softened--especially in the brokered markets. Overall price inflation apparently continues, however. A large producer of farm equipment says the average prices it pays for supplies and components rose significantly in December and January, although at a slower pace. Average prices paid by this firm in early February were one-third higher than a year earlier. Net new orders for steel have declined substantially, with cancellations playing a larger role. Demand for packaging materials has dropped sharply, partly as a result of inventory reductions.

Although oil and gas exploration continues at a pace limited only by capacity, oil firms say that they are scaling down future plans. The threat of an excess profits tax is said to be a factor, although demand for oil products has been weaker than expected. Prices of gasoline and some other petroleum products have been under downward pressure as a result of sizable inventories.

Electric and telephone utilities report demand to be below expectations. New installations of telephone and message volume have declined, a new phenomenon since World War II. Most telephone companies have laid off workers. One company has relied on attrition, but says layoffs are likely.

The job market continues to deteriorate. New claims for unemployment compensation have been running about double last year's increased level throughout the District. Unfilled requisitions at the Federal Reserve Bank are at the lowest level in memory of some old timers. Newspapers carry frequent stories of white collar workers, including executive and technical types, who are unemployed for the first time in their working lives with no early prospects for employment. Chrysler's SUB fund for nonunion workers is said to have been exhausted. In the Chicago area, the truck drivers union has ordered a maximum 50-hour week and a 10-hour day to spread available work, involving a seldom-used contract clause. Relatively few jobs are open and then mainly for such specialties as chemical engineers, draftsmen, accountants, commission salesmen, and telephone solicitors. Despite weak job markets, low-paid, menial, and dirty jobs are hard to fill. Moreover, most labor groups negotiating new contracts are militant in demanding increases in compensation of 10-12 percent or more.

Reports indicate a dropoff in savings inflows to S&Ls in late January. Nevertheless, most major associations have resumed lending to non-customers, with rates cut to 9 percent. There seems to be no surplus of housing in the District. Net new construction probably is well below household formation. Rent hikes on "better units" in the Chicago area are expected to average 10-15 percent on leases renewed this year.

Consumers are buying very cautiously despite price reductions and heavy promotions. Retailers appear to be closing marginal outlets more frequently, even in modern shopping centers. Rebates on some car models have not brought a boom in new car sales. Aside from the recession, car buyers are said to be deterred by price increases (about $1,000 per car), by the presence of the new features required to promote safety and control pollution, and by uncertainties as to the functioning of catalytic converters and the availability of lead-free gas.

EIGHTH DISTRICT - ST. LOUIS

Eighth District businessmen generally report a slackening in economic activity in recent weeks. Growth of retail sales has apparently slowed further, although some improvement in auto sales has been reported. Manufacturing output and total employment have declined and construction activity remains at a very low level. Some acceleration in the growth of deposits at savings and loan institutions was reported. Farmers are currently planning acreage increases for most crops this spring.

Large retailers reported poor sales in January, and excessive inventories have triggered considerable price cutting and promotional activity. Although automobile dealers report some recent improvement in car sales as a result of the rebate programs, such sales are still well below levels of a year ago. With the large inventory of cars, increased sales will have to continue for some time to have a major impact on manufacturing.

Manufacturing activity is in a slump throughout most of the District. More layoffs have been announced since last month in the automobile, textile, appliance, boxboard and paper products industries. Many firms have curtailed operations by shortening the work week and eliminating overtime. However, in a few cases, including the television and automobile industries, some previously laid off workers have been recalled.

A number of manufacturing firms continue to report fairly high levels of business activity. These include capital goods, steel, and chemicals. A manufacturer of towboat, barge, and dredging equipment reports backlogs of 2 years at the present time. One steel manufacturer reported backlogs have dwindled in recent months but unfilled orders are still higher than a year ago.

Some chemicals, including fertilizers, remain in short supply.

Nonmanufacturing employment, which declined in the District in the first half of last year, has picked up slightly since July. Construction employment has generally remained at a relatively low level, but increases have occurred in other activities including health care and government.

The increase in deposits at savings and loan institutions reported last month apparently continued in January. Savings flows into commercial banks have leveled off, however, and demand deposits have declined sharply in recent weeks. Loan demand at banks continues weak as both interest rates and loan volume have declined.

While construction activity continues in a slump, the increase in mortgage money has been filtering into the used home market at somewhat lower interest rates. One building representative in the St. Louis area predicts a worse year in 1975 than in 1974 for construction of single family dwellings; however, other reporters expect some slow improvement in home building throughout 1975, leading to an upturn in demand for appliances and other items.

Although most crop prices have declined recently, they are still believed to be sufficiently high to provide incentive for increased production plans next year. Some cotton producers, after a dismal season in 1974, are planning to substitute soybean for cotton acreage. Part of the 1974 cotton crop may remain in the fields due to a combination of poor quality, low prices, and wet field conditions. Although some farmers who experienced poor crops and financial losses last year may find financing more difficult this year, banks currently anticipate being able to meet their customers' demands for credit at competitive rates.

NINTH DISTRICT - MINNEAPOLIS

Reports continue to indicate a slowing in District economic activity. Even though the District has so far avoided large layoffs, labor market conditions have softened, and unemployment was expected to rise. Economic developments have also made District consumers hesitant to spend, and in January, many retailers had to cut prices to stimulate sales. Rebates have helped to spur District auto sales, and several directors felt tax rebates would help promote consumer spending. In general, business activity has been somewhat better in the District's rural areas than in the Minneapolis/St. Paul metropolitan area. The District's farm economy, however, is not as strong as a year ago. Bank directors cited several reasons for the recent declines in grain and soybean prices.

Although the District has escaped large layoffs, labor market conditions have undergone some softening. After the burst of layoffs reported in January's Redbook, no significant layoffs have occurred in the Minneapolis/St. Paul metropolitan area. However, help wanted advertising has fallen in the Twin Cities, and hiring has slowed. The policy of Twin Cities area businessmen was described as running a "tight ship" with a willingness to let work forces decline gradually. Also some shrinkage in middle management employment has occurred at some large firms which had laid off shop workers earlier.

Outside of the Minneapolis/St. Paul metropolitan area, several directors reported only seasonal unemployment increases. However, a Western Montana director stated that a third of his state's workers in the forest products industry were out of work. Layoffs have also occurred in the forest products industry in the Upper Peninsula of Michigan, but these employment declines are being offset by strength in that area's mining industry. In general, bank directors were looking for further weakening in District labor market conditions and additional rises in unemployment.

District retail sales in January reflected the weakening in District business activity. One director associated with the retail trade industry termed consumer spending in January as "soft." Another report indicated that Minneapolis/St. Paul area retailers have had to engage in price cutting and sales promotions in order to attract business. Promotions have helped to reduce inventories but have hurt retailers' profits. Retail spending has held up somewhat better outside of the Minneapolis/St. Paul metropolitan area. In the Upper Peninsula of Michigan, for example, tourist spending was up in January, and retail spending was quite good. Several other directors from rural areas also indicated that consumer spending had held up quite well in their areas. However, a Western Montana director described January retail spending in his area as "sad." With regard to the future, several directors indicated that a tax rebate would help to stimulate retail spending.

Auto rebates have helped to offset recent declines in District automobile sales. One major car manufacturer's sales in the Minneapolis/St. Paul metropolitan area during the last 2 weeks of January were up 85 percent from those reported in the previous 2 weeks. In addition, several directors stated that the rebates have stimulated auto sales in their areas. One interesting observation by two directors was that the rebates have helped to promote the sales of autos not eligible for rebates. Dealers in the Minneapolis/St. Paul metropolitan area hope that the rebates will bring their car inventories down to desired levels by the end of February. On the negative side there is a feeling that many car buyers are customers who would have bought in any case and are merely accelerating their purchases to take advantage of the cash rebate.

Bankers responding to our latest agricultural credit conditions survey reported that the District's farm economy was not as strong as a year ago. Bankers reported that some customers may be getting "into difficulty," but there were no reports of widespread bankruptcies. Many bankers stressed, though, that another year like 1974 could be disastrous. Although recent declines in grain and soybean prices have helped, livestock producers are still in a cost-price squeeze. Also, the early January blizzard caused heavy livestock losses in Minnesota and Eastern South Dakota. For many farmers, however, sales of 1974 crops will help bolster farm receipts in early 1975. Many bankers anticipate strong loan demand in 1975 to help cover farm operating costs. But increased deposit flow, primarily from crop sales, should provide the funds needed to meet loan demand, at least through the first quarter. Conditions will likely be tighter in the spring as seasonal borrowing needs pick up.

Grain and soybean prices have declined markedly, and bank directors cited several reasons for the falling prices. First, the cancellation of Russian and Chinese orders have lessened export demand for grain. Second, cattle feeders have cut back on their demand for feed grains. A Montana director, for example, indicated that many livestock producers are doing without feed grains. Third, recent price declines were attributed to larger January 1, 1975 carryovers than anticipated by market participants. Finally, users of grain products have reduced their buying in order to cut down accumulated inventories. These price developments have brought some relief to the District's livestock producing industry but imply some income reduction for those farmers still holding 1974 crops.

TENTH DISTRICT - KANSAS CITY

A number of Tenth District retailers report disappointing Christmas and January sales and express rather muted prospects for any significant improvement in the immediate months ahead. The auto market, however, has responded to the rebate program with dealers reporting sharply increased floor traffic and sales. For District farmers, both total cash receipts and realized net income were down for the year 1974. In addition, the bankruptcy of American Beef Packers has caused some financial ripples in the District. Reflecting the general weakness in the economy, a number of large District banks report a decline in total loans during recent weeks, with weakness in consumer, farm, and business categories. During this same period, deposits also moved sharply downward.

In a follow-up to our pre-Christmas survey of department store sales expectations, a number of the District's large retailers reported that sales had generally fallen short, with durables particularly weak. This pattern has continued into January, and sales forecasts for the months ahead have been trimmed back. At the same time, auto dealers report very good response to the current rebate program. Floor traffic is up sharply, and sales have responded, particularly for the rebated models. Many dealers report that sales of non-rebated models, including full size autos, have also picked up noticeably. Dealers express the view that the likelihood of higher fuel prices should sustain interest in the smaller cars, but would still like to see the rebate program continued.

Although farm prices trended downward in 1974 (the December average was 4 percent below the year-earlier figure), the average for the entire year was 6 percent above 1973's average. These higher average price levels generated an increase in farm income of about 7 percent for the nation in 1974. Crop receipts were up nearly 25 percent, but livestock receipts--reflecting the sharp drop in prices--fell 8.5 percent. In the District, total cash receipts declined about 2 percent in 1974 because of the relative importance of livestock as a source of income. A 15 percent drop in livestock sales more than offset a 20 percent gain in crop receipts. Due to lower government payments and sharply higher production costs, realized net income for both the Nation and the District also was down rather significantly in 1974.

The bankruptcy of American Beef Packers (ABP) has caused some financial ripples in the District. Several cattle feeders have not been able to meet their financial obligations with credit institutions because ABP's outstanding bank drafts have been frozen until the company's difficulties are resolved. One slaughter plant has been allowed to resume operations on a custom basis, and it is hoped that once the firm is reorganized all outstanding commitments will be honored in full.

A survey of large Tenth District banks reveals a decline in total loans during recent weeks substantially below the expected seasonal rate, with weaknesses reported in business, farm, and consumer loans. The decline in business loan demand is attributed to an overall sluggish economy and to a reduced demand for inventory loans as firms attempt to avoid undesired inventory accumulations. Although total farm loans are down throughout the District, Nebraska banks report a strong demand for grain, fertilizer, and feed loans. The impact of automobile rebates on consumer instalment credit is negligible, but many banks feel the impact is too early to properly assess. Real estate portfolios remain relatively inactive. On the supply side, some banks now feel they are in a position to accomodate high-quality loan requests--especially from established customers.

Deposits moved sharply downward over the last few weeks. Corporate demand deposits have declined considerably, in part reflecting a runoff of deposits built up at year-end for window-dressing purposes. Some banks attributed the decline to the payment of current tax liabilities. In addition, interbank balances have fallen due also to an unwinding of year-end window-dressing. Time deposits increased sharply in response to growth in large nonnegotiable CD's. Oklahoma banks, which issued a sizable volume of CD's to local governmental depositors, are apparently encouraging their customers to take the nonnegotiable issues. The Oklahoma banks indicated that, since their nonnegotiable CD's have 365-day maturities instead of 360-day maturities for negotiable CD's, they can reduce their effective interest costs by issuing the nonnegotiable CD's.

ELEVENTH DISTRICT - DALLAS

The volume of loans outstanding at Eleventh District banks has fallen sharply since the first of the year. Business loans have experienced the steepest decline, but real estate loans, loans to nonbank financial institutions, and consumer loans have all been reduced substantially. District bankers report the decline in business lending is primarily due to reduced loan demand. But apparently loan officers are being more selective, also. For example, marginal loan requests, which would have been accepted a year ago, are now being turned down.

Inventory loans have fallen sharply as many firms have successfully drawn down materials stocks in line with lower sales. Demand for accounts receivable financing has also declined with sales. Even loans for petroleum and gas operations, which had increased nearly a third in the past year, have dropped. However, rather than reflecting reduced oil field activity, lower loan demand by oil companies has been a result of higher profits, allowing these firms to finance a larger portion of their explorations internally.

Business demand for term financing, on the other hand, is up substantially. Many companies that financed capital expansions partially with short-term loans last year are now trying to refinance these outlays on a long-term basis. In addition, bankers report heavy demand from durable goods manufacturers for term loans needed to finance replacement equipment. However, most requests to refinance existing loans are being rejected becuase bankers are reluctant to commit funds to long-term obligations.

Demand for real estate loans remains weak. In fact, as described by one banker, demand for interim construction financing is "virtually nonexistent." Meanwhile, an increased flow of funds to thrift institutions has resulted in reduced borrowing by nonbank financial institutions. Requests for consumer loans have also declined substantially as households are deferring purchases of many big ticket items.

Loan renewals at District banks have risen sharply. Renewals by commercial real estate companies have been particularly large. Many of these firms are "totally illiquid," according to one banker, since they have been unable to resell large holdings of nonincome producing land. In manufacturing, loan renewals are most common in construction-related industries and among firms engaged in supplying producers of consumer durables. In an attempt to hedge against shortages and rising prices last year, many of these companies stockpiled inventories. But because sales fell sharply, they have been unable to liquidate inventories and pay out existing obligations. Heavy renewals of loans to individuals for purchase of stock have also been reported.

A survey of large commercial banks in the District reveals that most lenders have recently increased reserves for covering loan defaults. Higher profits earned last year provided the chief source of funds to increase loss reserves. And bankers admit that the economic outlook for 1975 practically ensures higher loan losses.

A downturn in business activity in the District has caused a rapid deterioration in the labor market. Growth in total employment has come to a virtual standstill, while the labor force continues to expand. The result has been a sharp rise in unemployment--25 percent in 2 months. And the unemployment rate stands at 6.2 percent, up from 4.7 percent last fall.

Layoffs in manufacturing, particularly in durable goods industries, account for much of the increase in unemployment. And barometers of future labor market strength indicate this downward trend will continue. In Texas, the average workweek in manufacturing has fallen to 40.2 hours, after remaining at 40.6 hours for 6 months. Moreover, initial claims for unemployment insurance have doubled since last fall.

Grain and soybean production is expected to rise substantially this year in the Eleventh District states. An increase in acreage planted will help boost winter wheat production nearly 50 percent over last year. Because of low cotton prices, farms will reduce total cotton acreage by 25 percent, and most of this land will be put into the production of soybeans and grain sorghum. As a result, total soybean acreage will increase 28 percent, while grain sorghum acreage will be up 18 percent. The amount of land planted in rice will be essentially unchanged.

Cattle producers continue to face a bleak profit picture. Ranchers, reluctant to cull their herds at depressed market prices, are finding it unprofitable to winter a large number of cattle. The number of cattle on feed in District feedlots continues to fall, down 40 percent from a year ago. Consequently, most feedlots are operating well below their break-even level of production, and several of the largest feedlots have gone into bankruptcy.

While bankers generally report no serious financial difficulties due to the write-off of farm loans, they indicate the number of delinquent loans has risen. Renewals of loans to livestock producers are common, and referrals to the Farmers Home Administration have increased. Bankers are reviewing agricultural loan requests closely with the view that livestock loans will continue to be risky in 1975. And with grain markets weakening, bankers are very concerned that crop farmers may experience a severe cost-price squeeze by harvest season.

TWELFTH DISTRICT - SAN FRANCISCO

In the opinion of our directors, there was a sharp deterioration in the economic climate in January, after employment and income in this region had held up relatively well through the end of 1974. Many of the directors still expect a pick-up toward the end of this year. The weakest sectors are housing, lumber and aerospace. The agricultural sector is still strong, and retail sales are holding up except for autos.

The directors feel that we are in for a period of belt-tightening and emphasis is being placed on controlling costs and productivity improvement programs. The concensus is that the recession will be short but sharp. Material shortages have practically disappeared and there is now fear of rapidly developing excess inventories. The rate of inflation is expected to decline to 6 percent by year-end because of excess supplies and low utilization rates.

In response to a question regarding the outlook for employment in their own industries, no director anticipated increases. In Utah, a very strong end 1974 showing was marred by the recent announcement of layoffs at Kennecott Copper Corporation. About 1,200 employees are involved and it has been estimated that each layoff would create a further 2 1/2 percent unemployed in secondary industry. The Boeing Company anticipates a decline of 1,500 employees, 2.5 percent of its work force, in the first half of 1975 as a result of delays and reductions in the level of commercial aircraft orders.

The agricultural sector, although generally strong, is beginning to develop cracks. High costs have depressed the cattle-feeding industry to the point where feed lots are being shut down and bankruptcies are being reported. Producers claim that along with the high feed costs they are suffering from political pressure and consumer activism. On the other hand, grains and most other crops continue to earn a good return and farmers are continuing efforts to expand acreage. One exception is cotton where growers are feeling the pinch of lower prices.

Our directors do not foresee any growth in nonresidential building activity over the next 6 months. They believe that passage of the investment tax credit would not translate to increased capital expenditures until year-end. The Seattle area, however, expects increased activity in the second half of 1975 due to such special factors as the Alaskan pipeline and the Trident Missle Base Development program. There appears to be some demand for small industrial buildings. This is being handled by a new type of financing in which developers are selling industrial condominiums. In the current financial climate, this enables the smaller businessman to put his financial package together.

Residential housing construction is still viewed as the disaster area of the current recession and its impact on the lumber industry in the Pacific Northwest is severe. Nevertheless, one director reports that his lumber firm anticipates "full production again within the next 6 months and heavy reemployment within the wood products industry as a whole."

Retail sales declines so far appear to be concentrated on durable goods. In Southern California retail sales of nondurables held up well until just after Christmas, but have slowed considerably in January. The rebates being offered on automobiles are helping the small car lines, but are not stimulating sales of medium-priced cars. Luxury automobile lines continue to sell well.

Among District states, the impact of the current recession is varied. With its prosperous agricultural sector, Idaho is faring better than the national average, and Utah is benefiting from strong demand for coal and fertilizer products. The strongest areas of California are those with an energy or agricultural base. The slowdown in general business activity is most apparent in the Pacific Northwest and Southern California, areas dependent on lumber, electronics and aerospace.