CONFIDENTIAL (FR)

CURRENT ECONOMIC COMMENT BY DISTRICT

Prepared for the
Federal Open Market Committee
by the Staff

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SUMMARY*

The general tone of this month's REDBOOK reports is somewhat less confident. Virtually all districts note improvement in conditions, but there are frequent mentions of unsatisfactory gains. Retail sales have increased, but mainly in soft goods with consumers showing continued caution on big-ticket purchases. Inventory adjustments are largely completed at the retail level (unless sales recede again), but many manufacturers plan further liquidations. General price inflation continues, despite weakness in some commodities, and there are fears that increases in the price level will accelerate. References to weak job markets do not seem commensurate with the substantial gains in employment reported for the nation. Unemployment remains at depressingly high levels in all districts. Reports on capital expenditures suggest further weakness, overall. Construction activity has shown no sign of revival except for single-family homes. Fears of substantial disintermediation are slowing new loan commitments by thrift institutions. Business loan demand at commercial banks remains sluggish for the most part. Harvests of major agricultural crops have been generally very good, but Hurricane Eloise caused extensive damage in some parts of the South.

Boston's report indicates widespread discouragement with economic trends and emphasizes "hazards" to business. Richmond finds the improvement "less widespread," and San Francisco says the recovery is "slower than expected." Most districts sound some notes of caution. Perhaps the strongest pictures are presented by Philadelphia, St. Louis, and Dallas.

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*Prepared at Federal Reserve Bank of Chicago.

Retail sales have improved modestly in most districts, mainly in apparel and other nondurables. Only Dallas reports a "marked pickup" in big-ticket items. However, Minneapolis, St. Louis, and Dallas find that auto dealers are pleased with the reception accorded 1976 models. Chicago and Philadelphia say that consumer credit delinquencies have been reduced.

The inventory correction continues. Most districts draw a contrast between manufacturers' continued efforts to reduce inventories and the success of retailers in bringing stocks into line with anticipated sales. Cleveland emphasizes the continued overhang of steel inventories, and Kansas City points up the recent stocking of steel to beat the October 1 price increase. Needs to replenish depleted inventories account for much of the increase in output of chemicals and textiles since last spring.

Continuing price inflation remains a major consideration almost everywhere. Cost-push inflation reflects rising labor costs, higher prices for energy, outlays to control pollution, and high interest charges. New York observers see inflation in the 6 to 8 percent range and some fear a "reacceleration." None of the districts reported views that the inflation rate would slow substantially next year.

Dallas and Philadelphia report a significant rise in manufacturing employment and in the average workweek. But Chicago finds that demand for workers continues weak, and Minneapolis says manufacturing employment declined further in the summer. The weakest job market appears to be in New England where unemployment increased to 12 percent in August.

Most districts reported that capital expenditure prospects appear soft for the next several months at least. Cleveland says capital goods orders have strengthened, but from "very low levels" last spring. Chicago says most manufacturers of capital goods and components are still cutting output, but demand for large mining and earth moving equipment remains strong. Richmond says 40 percent of manufacturers consider capacity "excessive." Dallas reports a very high level of oil and gas exploration in proven fields, but riskier ventures have been deemphasized and exploratory offshore drilling is at a "virtual standstill." San Francisco reports weak orders for commercial aircraft and reductions in investment plans for aluminum and lumber.

Sales and construction of single-family homes have improved this year throughout the nation, and added gains are expected in 1976 if credit conditions permit. But slowing inflows of funds to thrift institutions constitute a threat to further recovery. New apartment building is at very low levels. Office space is in excess supply with Atlanta reporting a vacancy rate of 20 percent. Chicago says architects have "nothing on the shelf or the boards."

Atlanta comments at length on the damage done to crops and buildings by Hurricane Eloise and the associated adverse impact on tourism. New York observers are apprehensive over the spreading impact of the financial problems of New York City. Unsettled conditions in the municipal bond markets have "virtually halted" major new commitments on government construction projects throughout the state.

FIRST DISTRICT--BOSTON

The directors of the First District are more unsettled this month. They are aware that the economy may not trace out a classic recovery; "to look around and see the wreckage, it is hard to feel cheerful." Many more problems, many more hazards seem to be plaguing business. There are suspicions that "our system doesn't work right." New England unemployment in August increased to 12 percent from 11.1 percent for July. Rhode Island's figure improved substantially, dropping to 13 percent, but significant deterioration in Massachusetts (13 percent) and Connecticut (11.4 percent) more than compensated.

Banking directors report sluggish or declining asset portfolios. All components of loan demand continue weak, and consumer credit has shown only feeble activity. Inventory liquidation seems to be reaching a nadir, but firms which are in positions to restock are proceeding extremely cautiously. Consequently, banks are improving their money market positions, unwinding liabilities and buying Treasuries. The lack of profits continues to restrict municipals investments to local issues, at best. New York City evokes divided attitudes, but none of the directors is intimately involved.

The banking directors expect short-term interest rates to remain flat for a few months. There is hope that recent money stock data may occasion a fall in the federal funds rate. "It would be regrettable if short-term rates rose."

Retail sales in the district have yet to recover convincingly. Most markets have seen only feeble increases in volume since April. One more successful retailing director reports a softening in activity for the last three weeks. He is stocking cautiously for Christmas, and business uncertainties are moderating his optimism for spring. In general, retail outlets have not begun restocking inventories. There seem to be few reported ripples from Grant. Although suppliers may have been caught, it was no surprise to our retail director. The firm had lost identity in a highly competitive market.

A director from Connecticut has become more optimistic about his state's prospects for 1977-78. Foreign companies anxious to locate in the U.S. have been impressed with Connecticut. Also, corporate headquarters of U.S. firms have been moving to the state. Defense contracting is continuing strong as well. Other New England states cannot look forward to these sources of growth at this time, and concern about long-term development is becoming substantial.

Capital goods producers and manufacturers of intermediate goods are still working off backlogs. So far there has been little stimulus for the First District in these industries. One director has identified a "key factor syndrome." Business is paying close attention to interest rates: rising rates are depressing, a fall is encouraging. There are reports that the war against inflation is misplaced if it requires high interest rates. With sluggish business and sales uncertainty, current rates are very high in both nominal and real terms. Lower rates would be necessary to bring out investment, expand capacity, and nourish the recovery, according to this view. Financial markets are much more than a veil over the real economy, and business is not poised to spring or encouraged to do so by high interest rates, a director reports.

Professors Houthakker, Solow, and Tobin were available for comment this month. Houthakker is still comfortable with general developments, while Solow and Tobin are very concerned about the propriety of policy.

Houthakker feels that the economy and policy are on the right track. He feels that a very vigorous rate of growth will prevail for a few months driven by exports, consumers, and an end to inventory liquidation; he then looks forward to growth of about 7 percent by the end of 1976 as business investment assumes a positive role. Inflation will slow to 4 percent at that time. He cautions against rapid money growth, and hopes that policy will favor the low end of the 5 to 7-1/2 percent range. He fears that the considerable money expansion in Europe should be discouraged, perhaps through official discussions: such

European policy will present some danger that the dollar will become unduly strong, or that domestic monetary policy may be unfavorably undermined.

Solow is not impressed with Ford's proposed fiscal program, but he also believes the Fed need not be too concerned since there is little chance of enactment. He expects rates of growth of 8 to 10 percent for the near future which is not out of line with a natural rebound--especially given the foregoing collapse. Such rates of growth need not imply that a sustaining drive for recovery has surfaced, so he remarks that the Fed need not feel tempted to lean against the wind. He notes that most optimistic forecasters have assumed money growth in excess of 7-1/2 percent. Policy is not doing its part: "I have seen no calculation of cyclical increases in velocity that would make 7 to 7-1/2 percent money growth appropriate in this economic situation. It is an empty belief that this time will be different."

Tobin emphasizes that velocity increase is related to money growth. Low money growth and high interest rates tend to cause a more sluggish expansion of GNP (or even a stalling of growth) which yields slow velocity expansion, at best. Tobin also stresses that high long-term interest rates reflect market expectations of rising future rates of interest, coupled with risk. There is a positive relationship between inflation and interest rates because the market has learned that price increases entail tight policy. The Fed should permit money growth to exceed 8-1/2 percent and explain that such a policy does not include a compensating stringency in the future. A temporary increase in money growth is appropriate for recovery; in fact, a recovery without big U.S. budget deficits requires this policy.

SECOND DISTRICT--NEW YORK

According to Second District directors and other business leaders, consumer demand should continue to provide the major near-term impetus to the business recovery. Respondents at the retail level sensed rising consumer confidence, and they generally expected a better Christmas season than last year. However, a strong upturn in residential construction and capital spending does not appear imminent. Despite continued industrial slack, most of those questioned foresaw inflation in the 6 to 8 percent range because of underlying cost pressures. Some respondents felt that New York's financial plight might have some impact on the business recovery.

Prospects appeared good for further improvement in retail sales. The Buffalo branch directors cited higher personal savings and less indebtedness as strengthening the financial position of households and consumer confidence. Expectations were for a better Christmas season than a year ago. Some respondents reported good gains in apparel, but the chairman of a New York City-based department store chain did note that furniture sales had been lagging. However, the department store chairman foresaw a strong near-term profit performance for the retail industry.

Outside of the retail area the outlook was not so optimistic. No one expected any quick and marked improvement in business fixed investment or in residential construction. A number of respondents from industrial establishments mentioned present price-cost margins as unfavorable to a rapid resurgence of investment. The president of a large multinational oil company was pessimistic with respect to the petroleum industry's ability to finance the capital expenditures required to meet the nation's energy needs. He regarded higher prices for domestic petroleum products as a necessary but not sufficient condition for generating needed cash flows. The chairman of a large concern manufacturing capital goods had yet to see any signs of recovery as bookings were still quite weak. No futher recovery in residential construction was forseen by the directors of the Buffalo branch because of such factors as previous overbuilding and high construction costs. However, an economist for a New York City brokerage firm expected declines in both inflation and long-term interest rates to provide an eventual uplift to the housing sector.

Despite the presence of forces which might ease price pressures, a number of respondents were uneasy with the prevailing degree of inflation, and some feared an eventual reacceleration of inflation. Among the factors cited as dampening price rises were continued slack in productive facilities, increased price competitiveness of foreign goods in industries such as chemicals, and competition among petroleum refiners faced with low capacity utilization. On the other hand, some respondents were concerned that a steady rise in wages, energy costs, and environmental control costs could push inflation upward. One New York City-based clothing manufacturer said that textile prices had started to recover toward last year's high levels and that delivery lead times were lengthening as some suppliers were unprepared for the quick turnaround in the apparel sector. Although not particularly fearful of a marked reacceleration of inflation, the Buffalo branch directors generally expected a 7 to 8 percent rate of price rise. While there was no expectation that price controls would soon be imposed, a few respondents feared that discussion of price control might trigger widespread anticipatory price rises.

A number of respondents felt that the New York financial crisis did pose some risk to the economy. However, most of those questioned did not think that the crisis would totally undermine the recovery. The Buffalo directors thought that the recovery might be temporarily delayed but expressed more concern with the probable reallocation of funds away from municipal securities. On the other hand, they felt that the longer-run implications could be favorable if the current crisis prompted greater financial responsibility at all levels of government. There were reports of concern expressed by some European foreign exchange dealers that default could have an unfavorable psychological impact on the dollar. A quite pessimistic note was sounded by the president of a large New York City-based construction firm specializing in government sponsored construction through New York State. He offered a bleak outlook for area public construction as unsettled conditions in the municipal bond market had virtually halted major new commitments.

THIRD DISTRICT--PHILADELPHIA

Economic recovery is taking hold in the Third District. For the third month in a row, area manufacturers report that business conditions have improved. New orders and shipments continue to increase, and there are additional declines in inventories. At the same time, employment has increased and the manufacturing workweek has lengthened. However, prices paid for supplies as well as those received for finished products are both higher. The outlook for the next two quarters is for the expansion to continue. Manufacturers expect new orders and shipments to be higher, and no further cuts in inventories are anticipated. In addition, these businessmen expect both work forces and the average workweek to expand. But it's anticipated that prices will continue to climb and capital spending will rise only slightly. Area retailers report increased sales and look for an upward trend through the spring. Bankers report that deposits are level or off slightly, while loans remain flat.

Manufacturers in the Third District, responding to this month's business outlook survey, report a higher level of economic activity compared to last month. This is the third consecutive month in which 35 percent or more of the respondents have indicated an improved business climate.

In fact, none of this month's respondents reports a decline in economic activity. More than one-fourth report higher levels of new orders, and shipments are up for a similar proportion of the respondents. Inventories are down, on balance, but the cutbacks are smaller than those reported in the previous few months. Of the manufacturers surveyed this month, the proportion reporting lower stocks exceeded those reporting higher ones by only 7 percentage points.

In July, by comparison, declines exceeded additions by 43 percentage points. The current expansion in manufacturing is also reflected in employment, which is up again this month, and in the average workweek, which is longer.

The outlook for the next six months remains optimistic. More than 80 percent of the executives polled look for an increase in overall business activity. Seventy percent expect new orders to be higher by April, while 68 percent anticipate an increase in shipments. Inventories are expected to stabilize over the period. In addition, almost 40 percent plan to add to their work forces, and there are plans to lengthen the workweek further. Modest increases in capital spending are also expected, but plans are still cautious with almost two-thirds of the manufacturers polled planning to maintain current levels.

Retail executives report increases in sales after adjusting for seasonal factors. Apparel and fashion items are reported to be selling well and one contact indicates very good sales of hard goods. These executives look for a strong Christmas season and most expect sales to trend upward through the spring. Most of the merchants contacted feel that consumers are more price conscious than in the past and one notes, "as a result, it becomes more difficult to maintain profit margins, let alone increase them." All of the retailers indicate that their inventory-sales ratios are at desired levels, but one anticipates some supply problems by year-end because manufacturers aren't building inventories fast enough. Most of the merchants report that in terms of credit collections they see signs that consumers are finding it easier to pay bills on time.

On the price scene, manufacturers report that prices they pay for their supplies, as well as prices they charge for their finished products, are up from last month. Prices paid are decidedly higher with none of the respondents reporting lower prices and close to 60 percent paying higher ones. Prices charged are up somewhat as well with a little over one-fourth reporting increases. The outlook for the next six months is for additional increases. More than three-fourths of the manufacturers surveyed expect to be paying higher prices by April, and 70 percent expect to be receiving higher prices for the products they sell. Retail executives report that, in general, the prices they pay and charge continue to move up.

Area bankers report that, after adjusting for seasonal factors, demand deposits are level or down slightly and savings accounts are flat. Most of the financial executives contacted report that they lost deposits to the Treasury during the latest offering, with one banker indicating a gross outflow of at least $15 million. All of the bankers surveyed are aware of California Federal S&L's offering of mortgage-backed bonds last month, and the majority report that they're looking into it as a possible way of circumventing Regulation Q ceilings and of achieving a better alignment of maturities. Loan volume is reported to be level or down somewhat, and the outlook is for it to pick up as recovery continues. One banker reports a slight pickup in consumer lending, and he looks for a further increase of 10 percent next year. These bankers look for short-term interest rates to rise gradually, and they expect inflation to be in the 6 to 7 percent range through next year. The majority of those contacted feel that if prices climb at a faster pace while M_1 grows at 7-1/2 percent or less, the chances of the recovery aborting will increase. There is general agreement that the tax cut in effect now should not be allowed to lapse, at least until the economy expands further.

FOURTH DISTRICT--CLEVELAND

Recovery in the Fourth District seems to be proceeding slowly. Manufacturing activity has been improving from its early spring low; but as in recent previous recoveries, the upturn is slower here than for the United States. Liquidation of steel inventories is not expected to be completed for several months, and capital goods producers report strengthening from very low levels last spring. Retailers report consumers are still cautious. Mortgage lenders are apprehensive over prospects for residential construction mainly because of last month's slowdown in deposit inflows.

Recovery in manufacturing has been under way for several months but is still relatively slow. This bank's index of manufacturing activity shows a pick-up since the March low that is somewhat slower than for a comparable period of recovery from the 1970 recession. Most of the strength in the present recovery in manufacturing is coming from nondurable goods producers. Tire production picked up sharply in response to a pickup in sales as well as smaller declines in inventories. Chemical and plastics firms, where inventories have been cut to desired levels, also report a gradual pickup in orders and output from early 1975 levels. A large supplier to the auto industry reports medium-sized trucks are beginning to sell well and that car frame orders have picked up. Steel orders have weakened sharply in recent weeks, and economists with three major producers expect little real improvement until early next year. Orders and shipments bulged in September to beat the October 1st price increases. One economist expects orders and production are at the low point of the year because inventories will have to be liquidated at the same high rate as last quarter. They expect that the October price increases will hold, despite a $30 to $50 per ton advantage foreign producers have over domestic prices. Orders from capital goods producers remain weak.

A recovery in capital goods typically lags an overall recovery and latest reports from capital goods firms in the district suggest no significant upturn until next year. A large machine tool builder notes that incoming orders have risen moderately from a trough in the first quarter of 1975, and he expects a 50 percent increase in new orders for 1976. A manufacturer of printing presses reports an increasing number of inquiries in recent weeks that he expects will result in a rising trend in new orders. Several tool and die producers note a small but definite upswing in orders since June, mainly from appliance and farm implement producers. A financial officer of a major firm that produces material handling equipment, auto parts, and trucks reports that its business low occurred early last spring. He does not expect much improvement in its automotive products until next year. A heavy duty truck producer reports production and orders have been climbing slowly from a low in March, while its construction machinery remains on a high plateau.

Consumers remain cautious, especially with respect to durable goods. According to a major chain headquartered in the district, real sales of soft goods have risen 4 to 5 percent since the spring of 1975. Sales of major appliances are still weak, although the decline from 1974 levels will narrow to 1 or 2 percent in the present quarter, and sales are expected to exceed year-earlier performance in the first quarter of 1976. Retail stocks of major appliances were brought into balance by midsummer, and retailers have begun to place orders for early 1976 sales. Markdowns over the next several months are unlikely to be as prevalent as they were during most of 1975. An executive with a major discount chain also reported that soft goods and home improvement products have picked up in recent months. An economist with a national food chain in the district noted customers are still very selective and cost conscious. Consumers will pay high prices for quality food and meat but are buying less.

Residential construction awards in the district rose at about the rate they rose in the United States in the first eight months of 1975, but mortgage lenders are apprehensive over prospects because of the net outflows of savings experienced by some savings and loans. Of the four S&Ls contacted, two reported net outflows of funds in September (both have had net gains so far in October), one reported net inflows, and one reported net inflows only because of successful promotional programs for opening of a branch. One of the largest S&Ls in the district reported net outflows of $1.0 million, in contrast to a $1.7 million increase in August and a recent high of $6.0 million in March. Liquidity in each of these associations has been cut from an 11 to 12.5 percent range during the summer to as low as 7.5 percent. These associations expect to take on new commitments cautiously, and generally expect that mortgage rates will rise another 1/4 point within the next few weeks. Bankers contacted also expect another rise in mortgage rates shortly after usury rate ceilings are raised. Several banks expect heavier mortgage loan demand in coming months as S&Ls cautiously take on new commitments, but these same bankers state that restricted portfolios may hold down their mortgage lending.

FIFTH DISTRICT--RICHMOND

The October survey of Fifth District business conditions suggests a continuation of the recent pace of recovery. Manufacturers continue to report increases in shipments and new orders, although improvement in the orders picture was apparently less widespread than a month ago. Inventories continue to decline, and there is some indication that they are coming into line with desired levels. The number of manufacturers reporting inventories as excessive is the smallest in over a year, although it still amounts to one-third of the respondents. Some improvement in unemployment rates is reported, but it is not clear that increases in employment are the primary factor in this improvement. Our survey of retailers suggests further general improvement in sales, while sales of big-ticket items relative to total sales seem to have stablized. In the banking sector consumer and real estate loans have continued to post modest but steady gains. Business loans, however, continue sluggish in most parts of the district. In agriculture, lower prices and a smaller volume of sales of flue-cured tobacco have combined to reduce the value of marketings some 12 percent, or over $100 million, from a year earlier.

Manufacturing respondents to our October survey report continued increases in shipments and in volume of new orders. Increases in new orders, however, were not quite so widespread as in the previous month and backlogs showed little change. The diffusion of survey responses this month suggests the greatest, or at least the broadest, inventory liquidation of the year. Over 45 percent of the manufacturers surveyed report declines in materials and almost 40 percent report declines in finished goods inventories. One respondent stated explicitly that his firm is shipping from inventories.

This widespread inventory runoff has now continued for six months and may be tapering off. One-third of our respondents, the smallest number in over a year, still view current inventory levels as excessive. About one-sixth report current levels as too low.

While little change in manufacturing employment during September is reported, there does seem to have been some increase in hours worked per week. Respondents reporting increases outnumber those reporting decreases by three to one. Employee compensation and prices continued to move up across a broad range although only one-fourth of the manufacturers reported receiving higher prices during the month of September. Approximately 40 percent of the manufacturers believe that current plant and equipment capacity is excessive, but almost 90 percent feel current expansion plans are about right.

Concerning the outlook for the next six months, there persists a basic mood of optimism although it is not as pervasive as in some recent months, and there is actually less optimism expressed in the outlook for the respondents' respective industries. Fewer than half of those responding expect the level of production in their own firms to improve during the next six months.

The October survey of retailers suggests improved sales during September but sales of big-ticket items relative to total sales were apparently unchanged. The prolonged relative decline in sales of big-ticket items would suggest that although such sales may have stabilized, they continue at a very low level. Inventories at the retail level declined further during the month and have apparently been brought into line with desired levels. The number of retail employees appears to have declined somewhat, while our survey respondents were unanimous in reporting increases in employee compensation. All respondents reported paying and receiving higher prices. There also appears to have been some deterioration in the outlook as 80 percent of our retail respondents now expect the level of business activity and of sales in their respective firms to be unchanged over the next six months.

Asset expansion among Fifth District banks has followed an irregular pattern in recent weeks, with advances in some loan categories offset by weakness in other areas. Bank interest in investments has also weakened. Consumer instalment loan volume at weekly reporting banks continued to show strength in September as compared to earlier months. Real estate loans also expanded in September and are running about 7-1/2 percent above a year earlier. Contrary to expectations expressed in August, and again as recently as mid-September, business loan volume has been weak. The notable exceptions are loans to the retail trade and tobacco industries, where seasonal influences have resulted in strong gains. Demand deposit growth has continued but the rate of inflow of consumer time deposits has fallen and savings deposits have suffered an absolute decline. Rate competition is also affecting S&L deposits. CD attrition continues. Average daily member bank borrowings increased in September to their highest level since January, but net federal funds purchases of member banks fell by about one-third from the August level.

District cash farm income for the January to July period was up about 1 percent over a year ago. The seven-month figure represented the first year-to-date period which showed an increase over the comparable period in 1974. Flue-cured tobacco prices have improved in recent weeks, but the season average price as of October 2 was still running 6 percent under last year's level. September 1 estimates indicate that the district's 1975 production of field crops, with the exception of tobacco, soybeans, and sweet potatoes, will be under 1974 levels.

SIXTH DISTRICT--ATLANTA

Retail sales, hampered by adverse weather associated with Hurricane Eloise, made slow improvement. Signs of renewed single-family residential construction activity appeared in some areas, while nonresidential and multi-family residenti construction remained largely dormant. A potential for renewed inventory adjustments continues to exist. Layoffs and wage disputes created crosscurrents in labor markets. Coal has stimulated business activity in the district.

The impact of Hurricane Eloise on the regional economy has been considerable. Substantial wind and water damage to tourist accommodations occurred in coastal Florida. Foul weather diminished tourist traffic and limited the growth of retail sales, particularly in coastal areas. Substantial damage to corn and peanut crops, pecan groves, farm buildings, and homes occurred in rural Alabama. Mid-Louisiana reports a disappointing soybean crop because of heavy rains; however, the sugar cane crop is reportedly the largest ever. Excessive moisture has also hampered corn and soybean yields in Tennessee.

Despite the hurricane's effects, directors report slow improvement in retail sales in many areas. However, sales in many localities remain below 1974 levels. Scattered reports are received of renewed reluctance to buy. The strongest recovery in sales appears to be in Tennessee, where gains in relation to 1974 levels are indicated.

The torpor of the construction industry continues, except for scattered reports from directors and lenders of renewed activity in the single-family residential sector, particularly in the state of Tennessee. A scarcity of mortgage funds is a recurrent theme in assessments of construction activity. Concerning the nonresidential sector, the latest survey of office space in Atlanta finds a vacancy rate of 20 percent, with continuing increases in store as additional structures are completed. Excessive stocks of commercial, office, and warehouse space are noted in reports from Florida. In Louisiana and Mississippi improvement is noted in building permits granted, but much of this activity is governmental. Large electrical generating plant construction projects are reported in both Louisiana and Alabama. The multi-family residential market remains depressed, with sales of condominiums during August in the Miami area 69 percent below the 1974 level. In Jacksonville, although condominium sales were the best this year, only 4.3 percent of the 1,500 units in inventory was sold.

Two reports emphasize a continuing potential for renewed inventory reductions, should demand fail to increase as expected. Customers of an iron foundry, thinking that their inventory adjustments were complete, had increased their orders. Now sales of fabricated metal products have failed to meet expectations, and a hold has been placed on foundry shipments scheduled for late September. In addition, although a large retailer notes lengthening delivery times and short supplies of piece goods, he states that insufficient increases of demand could cause a stock liquidation similar to that in 1974.

A membership survey by a purchasing managers association in Georgia found the following trends: lead times are lengthening on goods ordered; higher prices are reported by 40 percent, as in the previous month; 55 percent report prices unchanged; three-quarters anticipated higher prices over the next three months, compared to two-thirds in the previous month; reductions in inventories are indicated by about one-third and unchanged stocks by about 60 percent.

District labor markets were buffeted by strikes and layoffs but benefited from rehiring in certain industries. The strike by flight attendants against National Airlines, which began September 1, still continues. The central issue is comparability of wages with those of other carriers. Proposals for a five-year, no strike agreement are being considered by seven unions which represent National Airlines employees. An indefinite layoff of 500 workers, in addition to the 750 furloughed in March, began October 6 at the Ford Motor Company assembly plant near Atlanta. These additional layoffs during a period of the year in which production is usually high are explained by weak demand for the intermediate-sized models manufactured at the plant. Near Birmingham, a lack of orders for steel has caused the shutdown of a U.S. Steel Corporation plant which employs 700 to 800 workers. A Georgia chemical manufacturer has recalled 600 workers after a shutdown which lasted for six months, following settlement of a dispute concerning terms for extending a labor contract. A Florida iron foundry has recalled its second shift for molding of heavy castings. These employees were laid off in April. In Tennessee 300 workers have been recalled by a manufacturer of baseboard electric heaters and electric can openers. An additional 200 employees are expected to be recalled within four to six weeks when production of portable electric fans resumes. In Alabama depletion of the state's unemployment conpensation pension funds has necessitated a deduction, beginning October 1, of one-half of 1 percent from workers' paychecks in order to fund unemployment compensation payments. This is the first time in the history of the state program that such contributions have been necessary. Borrowing from the federal government will also supplement the fund.

Coal is creating significant business activity in the district. Two deep shaft coal mines are to be sunk near Birmingham at a cost of about $50 million each. Production is expected to begin in 1978. Coal will be furnished under a long-term contract to six Japanese steel companies. In Mobile, Alabama, the prospective increase in coal exports has resulted in an effort to expand port facilities to accommodate increased shipments of coal. Construction of additional coal-powered electrical generating plants has led to an announcement by Southern Railway of plans to build facilities for coal loading, storage, and blending at an Alabama location. Following its completion in 1977, this plant will receive coal from barges on the Mississippi River and then distribute it to trains for transportation to generating plants.

SEVENTH DISTRICT--CHICAGO

Observers in the Seventh District agree that an upturn in the general economy has been under way since the spring. The expansion is expected to continue, probably through 1976, with total output and the average price level both up about 5 to 6 percent year-to-year. Many important district manufacturers of capital goods and components are still cutting output or at least have noted no improvement in demand. Large retailers report that consumers are still cautious. Nevertheless, there is little concern among informed observers in the district that the upturn will "abort," as expressed elsewhere. Demand for workers continues relatively weak. Virtually all goods and supplies are readily available. Inventories are generally in line at the retail level and manufacturers increasingly are achieving a desired balance. Some types of equipment are being offered at "discounts from list," but underlying pressures to raise prices as and if markets permit are strong. Construction prospects remain very poor. Harvesting of generally excellent crops is proceeding at a faster-than-normal pace. Commercial bank loan demand remains slow.

It appears that executives are less convinced of the durability of the uptrend than their forecasting teams. Market analysts for certain firms producing both business equipment and consumer goods say that operating managers are "scared" and are tending to under-schedule production, despite possible lost sales. This caution reverses the pre-recession exuberance that resulted in excessive inventories.

The preponderance of producer equipment manufacturing in this district accounts for the less pronounced recovery here. Demand for materials handling equipment, logging equipment, and lighter construction and farm equipment, and machine tools is still sliding. Producers of certain large equipment for mining and earth moving continue to operate at the limits of their capacity. Overall, producers of equipment in this district, however, appear to be reducing output. Analysts expressed surprise at the increase reported for the business equipment component of the FRB index for August. Heavy truck sales remain at a very depressed level, but there are early signs that a revival is under way because of continuing gains in highway freight. Increases in sales of all classes of trucks are expected for 1976, but not to the peak levels of 1973-74.

Large retailers report some gradual improvement in sales in recent months, both from catalogs and at stores, but physical volume is still below last year. Gains are reported for all regions, but the north central area remains relatively weak. Credit sales volume has increased relative to total sales and delinquency experience has improved. A Chicago-area department store chain has begun to honor both major bank credit cards, the first full-line department store in the area to do so. Reports of changes in sales by product line are quite mixed, although auto parts and related maintenance are strong everywhere. Outlets for furs, jewelry, expensive cars, and other luxuries report that sales remained strong throughout the recession.

Unemployment remains at high levels in the district and appears to be rising further, especially in Illinois. Increasingly, manufacturing operations are being shifted to other areas, mainly the South, where compensation scales may be only half as great. Only in rare cases is organized labor prepared to make concessions on existing contracts. Teachers and other public employees have been successful in forcing substantial advances in compensation despite budget stringencies. Unexpectedly heavy enrollments at large public colleges, attributed to weak job markets, have overloaded facilities and some schools will not accept new applications for the spring.

Virtually all materials and finished goods are readily available. (Oil and natural gas will not cause problems in the district this winter.) Price concessions are reported in some markets, but virtually all manufacturers expect to increase prices further as demand improves.

Steel executives are indignant over the recent CWPS report which they believe understates future demand and drastically underestimates the industry's needs for capital. The October 1 price increases for steel seem to be holding up. Steel imports are running at a lower rate than expected. Steel consumption is expected to be up 6 to 7 percent next year, which could mean a 15 percent rise in shipments because user inventories have been reduced this year. By year-end 1976 shortages could be a problem again.

Construction activity has not improved, except for some rise in single-family housing. The recent trend toward disintermediation has caused S&Ls to closely restrict new commitments. In the Chicago area single-family home permits have increased this year, but are almost 40 percent below the average for 1971-73. Permits for apartments are down sharply from last year's low level to a rate only one-fourth as great as in the good years. Architects for residential, commercial, and industrial projects have "nothing on the shelf or on the boards." A large surplus of office and store space exists in all major centers. Mobile home shipments are expected to total only 220,000 units for 1975. A pickup in both conventional housing and mobile homes is expected for 1976, but a significant rise for both sectors depends on availability of credit which is increasingly uncertain.

EIGHTH DISTRICT--ST. LOUIS

Business activity in the Eighth District continues to increase somewhat according to recent reports of area businessmen. The recovery, although relatively slow, appears to be fairly broadly based. Manufacturing continues to expand; several firms report production near capacity levels. Consumer durables production is reported to be up from the rate of earlier months. Retail sales are increasing somewhat on a seasonally adjusted basis. Residential construction is increasing, but nonresidential construction remains generally at a low ebb. Savings inflows at thrift institutions have slowed considerably in recent months, and mortgage rates have been rising. Commercial and industrial loans at large district banks have increased somewhat in recent weeks.

Manufacturing continues the improvement noted in previous months, although activity is still well below year-ago levels. Respondents report an upturn in production of consumer durables. Appliance sales are also up, spurred by increased residential construction. St. Louis area manufacturers of clothing, lubrication and welding equipment, and materials used in construction report production at near capacity levels; some have recently added additional shifts.

Employment has increased somewhat, according to the latest available data. In some states and metropolitan areas, however, there has been little or no gain. A similarly mixed picture is presented by unemployment; but the rate of unemployment in the St. Louis area has declined somewhat from the 9 percent peak in the summer.

Retail sales are increasing, with many firms indicating the real volume of sales at about last year's rate following a seasonally adjusted low near the end of the year. Automobile sales are reported to be less than in the same period last year, but new model sales are reported to be off to a good start. Sales of foreign cars appear especially strong.

In the agricultural sector, prices of meat and feed grains remain relatively high. Demand for pork is expected to remain relatively strong and pork prices relatively high through most of the next year, but some short-term weakness is expected in broiler prices. Most of the Kentucky tobacco crop was cut and housed early because of drought, but the crop is reported to be good. A good soybean crop also appears in prospect, but the cotton crop in west Tennessee is characterized as a "disaster."

Many parts of the district report rising activity in residential construction, but little or no recovery in nonresidential construction. The apartment vacancy rate in the St. Louis area is reported to have fallen from 14 percent last year to only 2 percent now. The industry representatives believe that such a low vacancy rate will provide incentive for a sharp increase in construction of new apartments.

Mortgage rates in the district have risen and lenders anticipate further increases. Withdrawals from passbook accounts are reported at both thrift institutions and commercial banks. Thrifts report a new inflow of funds, although not at the rapid rate experienced in earlier months. Total time deposits at large district banks have shown little change over the last few months. Total loans at these large banks have increased somewhat in recent weeks, paced by increases in commercial and industrial loans. This increased loan demand appears to be more from intermediate-sized firms than from large ones. Some banks report rising credit demands for plant expansion and for building inventories. Consumer instalment loans have shown little change in recent weeks.

NINTH DISTRICT--MINNEAPOLIS

Entering the final months of 1975, the district's economy appears to be improving, despite continuing poor performance in a few key sectors. Retail spending picked up markedly in early summer. Farm income prospects have been fair to good, and labor market conditions have stabilized. Bank loan growth has recently improved, but savings deposit growth at district commercial banks and savings and loan associations slowed somewhat during the third quarter. Construction and manufacturing activity, however, have not yet begun to recover.

Minnesota retail sales rose sharply in May and remained at high levels through July. According to retailers' reports this sales upturn continued at a slower rate into August and September. Home appliances have been selling, and clothing sales have been good. Back-to-school promotions did extremely well in some stores, depleting inventories, while promotions in other stores were disappointing. Inventories are being kept in close check, and retailers generally expect sales to continue to increase this fall.

Although still down from a year ago, recent district automobile sales have continued stronger than national sales. However, this region's share of the national market has dropped from last year's peak and is approaching the traditional level. Last year at this time the price increase on 1975 models spurred very strong sales of the remaining 1974 models. This year dealers reported generally weak sales of the remaining 1975 models. Dealers attributed this to the fact that the price increases this year are not as large as last year and that there is a substantial increase in gasoline mileage on the 1976 models.

The district's summer tourist business was excellent. The number of tourists was up throughout the district, and many resort owners reported improved profits. Expectations for winter business are good: advance reservations at some resorts are already ahead of a year earlier.

Total district cash farm receipts for the first half of 1975 were down sharply from 1974 but remained above 1973 levels. Future receipts from crop marketing should remain fairly high since prices have been strong and district prospects have indicated improved harvests over last year. On the livestock side, feedlot operators remain hesitant to expand, though the third quarter did see a modest increase in the number of cattle on feed.

The sharp rise in district unemployment earlier this year appears to be ending. In July-August the district's unemployment rate, seasonally adjusted, was 6.8 percent and was up only 0.1 percent from the second quarter. This contrasted to 0.6 and 1.1 percent increases in the first and second quarters. This summer's marked increase in district "Help Wanted" advertising reflected the recent improvement in district labor market conditions. Manufacturing employment continued to decline this summer, though at a slower rate, and initial claims remained substantially above a year ago.

The second-quarter pickup in homebuilding was not sustained in the third quarter. Housing unit authorizations in July-August only matched second-quarter levels. Recent figures, though improved from the beginning of this year, were well below the numbers issued in the early 1970s. Also, district nonresidential building spending remained down from a year ago.

Savings deposit growth at district commercial banks and savings and loan associations slowed somewhat in the third quarter, following rapid growth during the first half of 1975. The slowdown largely reflected the growing attractiveness of U.S. Government Securities, whose yields have risen above the highest rates that savings institutions are permitted to pay.

Mortgage loans closed and mortgage loan commitments by district S&Ls continued to climb rapidly in the third quarter. However, if past relationships prevail, S&Ls will soon be scaling back the volume of new loan commitments to match the slower savings growth. Loan growth at district commercial banks strengthened substantially in September from the weak pattern that had existed during 1975.

TENTH DISTRICT--KANSAS CITY

The signs of economic recovery are confirmed by increased manufacturing activity in the Tenth District. Manufacturers' inventories as a whole apparently are still higher than desired, with stock runoffs proceeding and expected to continue until the end of 1975. Materials prices are viewed as bound to rise. Despite record or near-record crops of wheat, corn, and soybeans, farm prices in the aggregate have posted firm gains. This increase in farm prices is attributable to reduced supplies of pork and to grain exports. Bank loan demand is weak, except for a small increase in consumer instalment credit (primarily auto loans). The weakness in commercial loans reflects both inventory liquidation and little construction activity.

Inventory liquidation by district manufacturers appears likely to continue until year-end. While some purchasing agents say that they have completed their reductions in inventories, most want to reduce their stocks some more. Inventory levels of certain materials, notably steel, reflect recent stockpiling, rather than unintentional accumulation. Agents welcome improving business as an aid in getting inventories down to desirable levels quickly, not as a reason for ending the liquidation. Buyers are now able to get what they need, but several expect shortages to develop as things tighten up in the months ahead. Many agents report recent price increases by their suppliers; all expect prices to go up in the near future.

Although August beef production was 6 percent above a year ago, total red meat output actually fell 5 percent for the month due largely to a 28 percent decline in pork production. However, the record high hog prices that farmers are presently receiving are expected to foster larger farrowings in the near future. The recent hog and pig report indicated that farrowings may rise 6 percent above year-earlier levels in the December-February quarter. Meanwhile, cattlemen are continuing to reduce inventories, with the August 1975 cattle-kill 9 percent over last year and 29 percent over August 1973. These cutbacks in meat production, together with the bright prospects for grain exports, have bolstered farm prices. The index of prices received by farmers rose 3 percent in the month ending September 15, and now stands 18 percent over the 1975 low reached in March.

Corn and soybean harvest is progressing rapidly in most areas. The U.S. Department of Agriculture now estimates corn and soybean production at 5.74 billion bushels (a record) and 1.47 billion bushels (second highest on record), respectively. Rapid harvesting may result in some price softening in the near term as the trade nervously awaits removal of an export embargo to the USSR. The Russian sunflower seed harvest is now anticipated to be even worse than had been expected and this may increase U.S. soybean exports, providing export bans are lifted before Russian needs for vegetable oil have been filled from alternative sources.

Wheat seeding is progressing on schedule in the Tenth District except for delayed planting in southwestern Kansas and western Oklahoma due to lack of moisture. The general concensus is that winter wheat acreage in 1975-76 will be about the same as 1974-75 acreage in the district. However, it is expected that more fertilizer will be applied this year than last, reflecting lower fertilizer prices as well as the general optimism of farmers on wheat prices.

Tenth District banks continue to report that loan demand is generally weak and few bankers expect significant improvement by year-end. Business loan demand is strong only in energy-related businesses. Caution on the part of businesses in rebuilding inventories and in expanding capacity is holding down loan demand. Construction lending for one- to four-family structures has increased somewhat, but lending for multi-family structures is still very low. Large inventories, along with high construction and financing costs, are depressing the demand for construction loans. Consumer instalment lending has increased slightly in recent weeks. Several banks reported a small pick-up in auto loans, while others reported above seasonal use of credit cards.

ELEVENTH DISTRICT--DALLAS

Despite the suspension of the oil depletion allowance, drilling activity in Texas continues at a rate nearly 20 percent ahead of a year ago. Higher prices for new oil and natural gas sold in the intrastate market account for most of the 7,855 wells drilled so far this year. Most efforts, however, are concentrated on developmental drilling--recovering more oil from proven fields--while riskier exploratory drilling has been deemphasized. Lack of a national energy policy is cited as the major factor that has led oilmen to steer away from high-risk ventures. Exploratory drilling offshore, for example, has come to a virtual standstill.

Increased drilling activity worldwide has continued to fuel the demand for oil field equipment. The state's largest manufacturer of oil field equipment estimates demand is running 25 percent ahead of a year ago. Several producers report a year's production of unfilled orders on their books. Industry suppliers are also experiencing brisk sales. Some steel fabricators, for example, have been able to sustain high production levels by shifting resources to their oil field equipment business and away from construction-related products.

The current upswing in the Texas industrial production index has been largely due to the recovery in petrochemicals--the biggest sector in the index. Chemical manufacturers now warn the recovery may be short-lived. The recent strength has been mainly due to a heavy influx of orders by user industries to replenish inventories. But because purchases by users are currently outpacing their sales, new orders are expected to fall once stocks have been brought up to desired levels. The upturn in chemical production, which is dependent on petroleum-based feed stocks, has stimulated much of the 10 percent increase in crude oil refining since May.

Apparel and textile manufacturers also report production continues to grow on a deluge of new orders that began last April. Clothing retailers, especially large chain stores, are rebuilding inventories. One indication of the strength of the wholesale market was the quantity of orders placed by retailers with manufacturers last summer. According to one industry spokesman, area manufacturers accepted one-third more orders than they could comfortably produce without extending delivery schedules.

Commensurate with increased manufacturing activity, the labor market for production workers in Texas continues to improve. After declining during the first half of the year, factory employment has risen since July, and the trend will likely continue. The average manufacturing workweek, seasonally adjusted, is 40.9 hours, substantially above the February low of 39.7 hours. Moreover, the layoff rates for major Texas cities have been at least halved since January, and recent gains in the quit rates suggest workers sense job prospects are improving.

A survey of new car dealers indicates consumer interest in the new models is much higher than it was a year ago. Improved gas mileage and a smaller increase in sticker prices were cited for the more favorable reception of the 1976 models. In addition, buyers appear more willing to accept the added expense of optional equipment. (It must be remembered, however, that this year's models come stripped down, and the back seat in one car is optional.) A Fort Worth dealer feels buyers plan to keep their new cars longer and are willing to spend more for a model equipped for their individual needs. Several dealers warn that sales this year may be slowed by a shortage of new cars. Auto workers appear reluctant to work overtime this fall and heavy demands for some smaller models are expected to keep dealer inventories below desired levels.

Since April, sales at Eleventh District department stores have been increasing at a brisk pace. Over the past 60 days, however, the composition of sales has changed somewhat as there has been a marked pickup in purchases of durable goods, especially big-ticket items. Executives with the leading stores attribute much of the increase to greater response to a normal level of promotional activity. The manager of a Dallas store points out that recent big-ticket purchases were being made by customers who differ from the typical buyer two or three years ago. Then, customers were predominantly interested in buying "the top of the line," with prices playing a secondary role. Today's buyers, on the other hand, are extremely price conscious and are trading down in their purchases.

Agricultural conditions in the Eleventh District remain generally favorable. Harvests of corn and grain sorghum are about two-thirds complete and ahead of last year's pace. The cotton harvest is on schedule but only one-fourth finished. Cold, wet weather on the High and Low Plains of Texas late last month has substantially reduced the expected yield of cotton from September 1 estimates. Wheat seeding is progressing well, but much of the dryland crop needs rain to establish a stand.

Livestock are in good condition. However, top soil moisture is limited, and fall grazing prospects are deteriorating. Heavy marketing of livestock continues as ranchers closely cull herds in anticipation of high feed costs this winter. The number of cattle and calves slaughtered in Texas through August of this year is 42 percent larger than in the same period of 1974 and compares with only a 16 percent increase for the nation.

TWELFTH DISTRICT--SAN FRANCISCO

Our directors view the recovery as slower than anticipated. Business investment plans are cautious and inventories continue to be held down to levels matching orders. Residential construction activity shows mixed trends in this district but on balance is recovering despite some problems associated with higher interest rates. Demand for loans is described by banks as being steady rather than strong, with the greatest weakness being in industrial or national accounts.

The pace of economic recovery is slow and business conditions reflect that situation. Few of our directors report any major change in their investment plans. They regard plant capacity as adequate to meet existing demand, and in industries such as aluminum and lumber investment levels have been reduced somewhat. Businesses also appear to be keeping inventories in line with sales, and no directors report any significant increase in order backlogs. Firms are experiencing a major reduction in estimated delivery times and report no shortages.

Orders for commercial aircraft remain weak, but orders for electronic equipment have increased. The lumber industry faces both lower volume and prices, while prices for pulp and paper remain steady. No recovery is expected for lumber until construction activity recovers. In contrast, demand for corrugated paper products is stronger, reflecting increased consumer demand. Generally, retail sales appear to be a major source of strength in the recovery, and retailers appear to be reasonably optimistic about sales over the rest of the year.

Residential housing activity is improving, but there remains considerable variation across the district. Construction expenditure increases as high as 40 percent above last year are reported in the Seattle area. Vacancy rates are low--less than 5 percent--and home prices have been pushed up accordingly. In California most of the activity appears to be centered in the north. Usually southern California accounts for 60 percent of the housing starts, but currently 68 percent are in the northern half of the state. The Bank of America expects that there will be a modest uptrend for the state as a whole over the next six months, despite this weakness in southern California. Some directors think that higher interest rates, in part caused by Treasury borrowings, may restrain the housing industry until 1976, when lower rates are expected. In Oregon the recent rise in interest rates has pushed mortgage rates close to the state's 10 percent ceiling on loans under $50,000. Further increases would cut real estate financing in that state.

Agricultural prospects in this district appear to be good. Farmers continue to expand acreage under cultivation and they are encouraged by reductions in some costs. For example, nitrogen-forming fertilizers, which had been $220 a ton in early 1975, are now offered at $64 a ton. Farm equipment dealers have large inventories, and significantly reduced prices are being offered. The strength of Russian grain orders, however, remains an unknown factor for wheat. Storage facilities for potatoes and other crops are being increased in eastern Washington and Idaho to meet increasing demand for frozen and processed foods.

Bankers describe the demand for loans as being steady with no particularly strong sectors. Loan demand is greatest in such categories as consumer credit, small business, and retail loans. Some banks report agricultural loan demand as being somewhat weaker and they ascribe this to the increased liquidity of farmers. Over the past few months there has been a strengthening of loan demand in California from utilities, areospace, and retail industries. General manufacturing, transportation, aluminum and forest products are weak. Several banks commented on the lack of demand from their national accounts and heavy industry.