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CURRENT ECONOMIC COMMENT BY DISTRICT

Prepared for the
Federal Open Market Committee
by the Staff

March 23, 1983

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SUMMARY*

Overview

District reports are nearly uniform in the suggestion that an economic recovery began shortly after the first of the year. In most areas the recovery is being led, in many cases exclusively, by personal consumption expenditures and residential real estate sales and construction. Automobile sales are generally improved relative to year earlier levels, but are not consistently sustaining the levels reached in January of this year. The manufacturing sector remains spotty. Housing and auto related industries are improving. Capital goods, on the other hand, remain severely depressed in most areas. Inventories are generally characterized as light to moderate but there is no clear pattern of intentions with respect to changes over the near term. Despite the improvement in business activity the employment picture seems to have improved little, if at all. Banks and thrifts continued to experience strong deposit inflows, primarily into MMDAs. Loan activity is essentially flat with modest gains in real estate and consumer lending about offsetting declines in business loans.

The Manufacturing Sector

Manufacturing activity is mixed both nationally and in most districts. Generally speaking, consumer, automobile, and housing related industries are showing marked signs of recovery. Building materials, in particular, are buoyant and upward pressures on their prices are developing.

*Prepared at the Federal Reserve Bank of Richmond.

Minneapolis, Dallas, and San Francisco all indicated that their lumber and forest products industries are strengthening. Chicago reports some gypsum plants operating six days a week with output above rated capacity. In the Boston District, housing activity is boosting production of roofing materials, building parts, wiring, electrical devices, and appliances.

In the Philadelphia and Richmond Districts the strength in manufacturing activity is more broadly based. New orders and shipments have zoomed according to Philadelphia, while in Richmond's area there has been broad improvement in shipments, orders, and order backlogs.

In other areas developments are less encouraging. Cleveland notes little change on balance, although steel orders are responding to increased auto production. Mills are operating at 50 percent of capacity as compared to 30 percent some months ago, and the price of scrap is up sharply. Industrial production remains depressed in the St. Louis District where several large plant closings are reported. Energy related industries also remain weak, and in Chicago's words, "machine tool order backlogs have evaporated."

Consumer Spending

Consumer spending appears to be strengthening on balance, but the improvement is spotty, both across districts and across the various segments of the retail sector. The relatively robust sales of January have moderated, in some areas because of extreme weather conditions. The composition of sales also varies from district to district. Soft goods, particularly apparel, seem to be doing well generally. Activity in durable goods is less consistent. Only Richmond, Atlanta, Dallas, and San Francisco specifically note strength in big ticket items. New York, on the other hand, reports that big ticket items remain weak.

Retailers' inventories are modest to trim over all, but there appears to be no widespread tendency or intention to add to them. Atlanta sees stocks at department stores on the rise, responding to brisk sales. Boston characterizes inventories as high but satisfactory.

New car sales, although up from recent levels, are still below expectations. Nonetheless, they are sufficient to have fostered some optimism and have encouraged production among suppliers, with the notable exception of tire manufacturers.

Construction and Real Estate

The most consistent and widespread source of strength is the residential real estate sector. Sales of existing houses are up sharply in most areas. Construction of new structures is beginning to follow, and information on applications for and issuance of building permits suggests further progress in coming months. In the Minneapolis metropolitan area, home sales for the first two months of 1983 were up 34% from a year earlier, while in the San Francisco District housing starts are running at twice the level of the comparable period in 1982. Kansas City describes the situation there as a boom in housing starts.

Commercial and industrial construction, however, is pervasively weak and, in many areas, is slowing. Only St. Louis specifically notes any strength in non-residential construction.

Banking and Finance

There has been little tendency to date for loan demand to respond to the gains in economic activity. Modest and scattered strength in real estate and consumer lending is offset by continued weakness in business lending. Even consumer lending by banks and thrifts does not appear to have matched the gains in consumption expenditures. It is conjectured that captive finance companies may be handling some of the new car financing. The low level of business lending is attributed to sounder financial positions rather than to reduced business activity.

Banks and thrifts are continuing to experience heavy inflows of funds into MMDAs. Kansas City suggests that other classes of deposits are actually declining, but that MMDA growth is so strong that it is holding the growth of total deposits up. There are indications from several areas that institutions are coming under increased pressure to find outlets for these new funds and are therefore becoming somewhat more aggressive in marketing loans, especially in the retail lines.

Agriculture

Despite some improvement, the farm sector remains troubled. Production costs are moderating and land prices have stabilized. Winter wheat conditions are good in the Kansas City District, where a mild winter and higher prices are also helping livestock producers. Bad weather has caused heavy crop losses and delays in planting in the western part of the country and is expected to lead to price increases later in the spring. Heavy participation is generally expected in the PIK program, which will result in reduced acreage in some crops and areas.

The Outlook

The outlook is generally positive. The failure of activity to match January levels is considered transitory. Many industries still languishing are expected to feel the upswing before long. There is little optimism regarding the capital goods industries, however. Further, there is little expectation of significant gains in the employment over the near term. There is some scattered concern over the potential for higher inflation rates. Recent rises in non-petroleum industrial prices are seen as omnious in some quarters.

FIRST DISTRICT - BOSTON

For retailers and manufacturers in the First District the recovery seems to have arrived at last. Retailers report that sales in the first months of 1983 were well ahead of year ago levels. Retail inventories are relatively high, but still satisfactory. Manufacturers are not as optimistic, but most have seen improvements in some facets of their business. Demand has picked up for housing-related products in particular. Exports are weaker than domestic sales, although several respondents have become more positive about prospects in Europe. Canada is a major problem area, as is South America. In contrast to the retail sector, inventories in manufacturing are low.

Retailing

Retail sales in January and February were well ahead of last year, but quite variable. Inventories are said to be relatively high yet satisfactory. Prices are much more stable than a year ago.

A building goods specialty house closed out the 1982 fiscal year in January with their strongest quarter in several years. However, a snowstorm in mid-February cut year-over-year sales growth from 24 percent in January to 6 percent in February. Even sales to contractors, which have been severely depressed for several years, have picked up in the last couple of months.

A discount department store chain reported February sales gains in New England ranging from 30 percent in Vermont to 5 percent in Rhode Island. Another department store chain, which has been upgrading its merchandise, reported strong growth "even in Rhode Island" where the recession has been most severe; for this firm fiscal year 1982 was the best year ever in terms of sales and profits.

A mail order supplier of clothing and outdoor equipment reported January and February sales 10 to 15 percent ahead of last year, considerably below the year's average growth of 30 to 40 percent. The slowdown was due to weakness in sales of outerwear caused by a very mild winter in the Northeast and poor skiing conditions. Sales of spring merchandise in the first part of March were back on budget, about 25 percent above a year ago.

These merchants attributed their recent strength to consumer optimism about the incipient national recovery, the relative health of the New England region throughout this recession, and their individual appeal to customers on price or quality grounds. Several have adjusted upward their fiscal 1983 plans and budgets, but this has not involved any net hiring.

Manufacturing

Most manufacturers contacted think they see evidence of a recovery. The evidence is strongest for such housing-related products as roofing, ready-to-install building parts, wiring, electrical devices and appliances. The pickup in other areas is much less vigorous. While several firms reported increased demand for automotive products, a major tire manufacturer has seen no increase yet in orders from the automakers. The tire-maker is confident that its competitors are in the same position. Orders have increased slightly for semiconductors and electronic components, furniture for data processing operations, strip steel, industrial wiring, some types of machine tools, and corporate aircraft.

Orders remain very depressed for commercial aircraft engines, industrial tools, and many heavy capital goods. Domestic sales are stronger than exports. However, four firms in four different product areas noted that the European situation is no longer deteriorating. Canada, on the other hand, was reported to be a major problem, as was South America. Concerns about Canada have been voiced in previous surveys, but never with such frequency.

Inventories are said to be in good to very good shape. None of the respondents plans significant inventory reductions. A couple are concerned about being ready to respond to increased orders. Two firms noted that increases in their own sales, industrial wiring and electronic components, may be attributable to their customers' restocking depleted inventories; these products usually start to pick up later in the cycle.

Until the recovery is more firmly established, manufacturers are in no hurry to call back workers. Among the firms contacted, one reported a very large layoff in January. Two others reported that work forces are continuing to fall through attrition. However, these same two firms expect to begin hiring later in the year. Most firms are meeting increases in demand by having existing staff work longer hours; in the case of the machine tool firms, an increase in hours means a return to a more normal workweek. In the housing and automotive areas, a few workers are being brought back. Almost all the current and planned hires are direct labor; some of the higher technology firms are also hiring engineers. No one plans to increase administrative and clerical personnel.

Professors Eckstein and Houthakker were available for comment this month. Eckstein believes that real growth during the first quarter may have exceeded 6 percent. With such a strong start, growth during 1983 should exceed 4 percent. "The core rate of inflation is heading downward to 5 percent." With continued good luck "the consumer price index may only increase 3 percent or less during this year, and wage inflation should continue to decelerate throughout the year." Eckstein advises the Fed "to continue to do absolutely nothing for some months." "As has been the case since last October, the Fed should devote much discussion to money aggregates and their targets, but the federal funds rate should not be changed." "It's too early to play the monetarist game for real because adherence to the targets may produce a 15 percent prime rate this year. With low inflation, real interest rates are already very high. The Fed should wait until the money numbers display some rational link to economic conditions before resuming its monetarist role."

Houthakker believes that real growth will average about 3 percent this year. The outlook for inflation this year and next is very favorable. This year, unit labor costs and prices should rise only 1 or 2 percent because of high productivity growth and decelerating wage hikes. Next year productivity growth will be much slower, but the rate of increase of labor compensation should be much slower also. Houthakker has been content with monetary policy to date, but he is concerned that rapid money growth should not be allowed to continue without explanation. Perhaps now is the time to return to money growth targets. Houthakker notes that the deteriorating current account in our balance of payments has not depressed the dollar dramatically because of strong capital inflows. A return to money growth targets will not necessarily entail rising domestic interest rates because these foreign capital flows will not allow domestic interest rates to get out of line with yields abroad.

SECOND DISTRICT--NEW YORK

Additional signs of an upturn in the Second District economy have appeared in recent weeks. Retail sales continued to exceed year-ago levels in February and showed signs of further strengthening in early March. Lower mortgage rates stimulated a decided pickup in the residential real estate market and builders anticipate a moderate recovery this spring. In the nonresidential sector, the pattern was mixed: leasing of office space grew in some areas but remained low in others. In manufacturing, rising orders spurred some firms to expand production, although many industries have not seen any improvement so far. Business leaders have become more confident that the recovery is getting underway but are unsure how quickly it will gain momentum.

Consumer Spending

During February, retail activity continued to equal or surpass year-ago levels. Heavy promotional activity continued and helped recoup the sales lost during a blizzard early in the month. Two of our contacts reported that sales improved further in early March. Consumer electronics and soft goods such as apparel moved well. Big-ticket items remained weak overall. However, one respondent noted strength in home furniture and others observed increases in installment sales. Inventories were generally at planned levels, and one department store had raised its desired stocks in anticipation of future sales growth. Other merchants also were hopeful that sales would strengthen further during the spring, but some expressed concern that renewed consumer caution would limit any gains.

Construction and Real Estate Activity

A decided pickup in the housing market occurred in recent weeks. Spurred by lower mortgage rates and a widespread concern that rates could rise again, potential homebuyers were out looking in sizable numbers. Thus far, however, there has been only a modest increase in sales of new and existing homes. Residential construction activity appeared to be heading up also. In Manhattan plans for two large luxury apartment buildings were announced and several other sites have been cleared for construction. In suburban areas builders and suppliers were reported to be very busy. Respondents anticipate further improvement through the spring but they noted that higher lumber costs could push home prices up.

The nonresidential real estate sector continued to strengthen in much of the District. A noticeable improvement occurred in the Manhattan office market where several major leasing deals were signed in the midtown area. While no major construction projects have been started in New York City since the last Redbook, construction on projects begun earlier remained strong and plans for another large office building were announced. In suburban areas, however, activity was mixed. The office markets in Long Island and Connecticut were soft while inquiries for space rose significantly in New Jersey.

Business Activity

Reports from business leaders around the District reinforced the view that manufacturing activity is beginning to turn up. A variety of firms experienced increased orders, and with inventories very low, this renewed business led to sizable backlogs in some cases. Companies ranging from electronics producers to suppliers of auto components expanded production. Some plants lengthened their workweeks, even to the point of adding overtime.

Employment finally stabilized, with recalls and new hiring at some plants sufficient to offset the workforce cuts still occurring at others. Nonetheless, our contacts emphasized that many industries have not yet benefitted from any pickup. Manufacturers of chemicals and capital equipment, for example, were noted still to be operating at very low levels, and our respondents believed it would be some time before any improvement spread to these industries.

Outlook

Business leaders are becoming increasingly confident that a recovery is getting underway. Their main concern now is that the initial upswing may be too gradual to generate momentum for the longer run because manufacturers are reluctant to expand until they are sure the recovery is sustainable. Our contacts expect many firms to wait for a substantial accumulation of orders before committing themselves to rehiring workers, rebuilding inventories, or investing in new equipment.

Financial Panel

This month we have comments from Donald Riefler (Morgan Guaranty Trust), Francis Schott (Equitable Life Assurance Society), and Robert Stone (Irving Trust):*

Riefler: The recent firming of interest rates is a normal reaction to the improving economy. However, the resurrection of M-1 as a policy concern has raised the level of uncertainty in the market about the future direction and level of interest rates. In view of the unusual relationship of M-1 to GNP in the last 12 to 18 months and the virtual impossibility of predicting with any certainty the impact of "Super Now Accounts" on M-1, the de-emphasis of this aggregate as a policy guide should be reiterated.

* Their views of course are personal, not institutional.

Schott: There has been a major easing of cash flow at thrifts and life insurance companies. Funds for medium-term bonds and mortgages are readily available. Lenders are still extremely reluctant to make long-term fixed-rate commitments. A clash between Federal deficit financing needs and rising private credit demand is foreseen, perhaps by early or mid-1984. It is feared that either inflation will return or else interest rates escalate again. An attack on the structural part of the Federal deficit appears to be the only way to assure a steady supply of long-term funds for private capital formation.

Stone: Whatever it is the Fed has been doing, it ought to continue to do it. No reduction in the discount rate seems warranted since recovery is getting under way without it and since given the concern that some people have over the aggregates, the reaction could turn out to be perverse. My own view of the aggregates is that their significance is still not sufficiently clear to warrant taking any action to rein them in at a time when the recovery is still in its early stages. Should the pace of recovery accelerate, and should aggregate growth remain high, the Fed may at some point have to take action that would lead to higher interest rates. But it would be very premature to do that now. Hence I repeat the opening sentence: whatever the Fed has been doing, it ought to continue to do it.

THIRD DISTRICT - PHILADELPHIA

Reports from the Third District in March indicate the local economy is expanding. Manufacturing activity has surged ahead substantially since January. Retail sales rebounded strongly from a disastrous February snowstorm and are quite strong in early March. Loan activity at area banks is unchanged but deposit levels are up. In the real estate market, home sales continue to increase and housing starts are slowly coming to life.

Third District businessmen predict further recovery for area business over the next six months. Manufacturing contacts are planning for substantially improved activity by September. Retailers say sales should stay strong through the summer. Bankers are forecasting minor gains for consumer lending, but stable demand for business loans.

REAL ESTATE AND CONSTRUCTION

The housing market in the Third District has entered the spring buying season by gaining dramatically since January. Brokers report sales volumes up 30 percent to 90 percent over year-ago figures. Mortgage rates are now in the area of 12.50 percent to 13.50 percent. Realtors note, however, that it is still tough for first time buyers to qualify for the lower rates, keeping an upper limit on sales activity. While most of the activity is still in previously owned houses, new homes are finally beginning to sell also. Prices of new homes have firmed up a bit and, although the stock of unsold units is still somewhat heavy, Third District builders are slowly starting new construction.

MANUFACTURING

Manufacturers responding to the Business Outlook Survey say Third District industrial activity climbed sharply both this month and in February. A robust recovery for local industry finally seems to be taking hold. New orders and shipments zoomed upward, halting the deterioration of producer backlogs and slowing inventory decumulation. Employee ranks held steady in March (the first month since September 1981 without a drop), as did the length of the average workweek.

Manufacturing activity is widely expected to pick up steam over the next six months, pushing the present expansion further along. Area businessmen predict that new orders will continue to soar between now and September causing a widespread buildup in producers' backlogs. In addition, survey respondents say that by early fall, stock levels should have turned the corner and begun growing. Plans for stepped-up production include enlarging payrolls, extending working hours and, reflecting renewed confidence, increasing capital expenditures in the next six months.

Industrial prices are mixed in March. Prices received for final products have held steady again this month but, after four months of stability, the cost of inputs has crept upward. A return to higher price inflation as business improves is projected, but not to the levels observed in the late 70s.

RETAIL

Sales growth at Third District department stores has dipped slightly since the last Redbook, slowing from its fast start this year. The east coast's "Blizzard of '83" virtually halted sales for several days in early February, forcing many store closings and countless transportation problems. The weather, however, has turned very favorable since then, and sales in the last four weeks, aided by larger than expected tax refunds, have recouped most of the early February losses. Current dollar volume is ahead of last March by 10 to 12 percent, down from January's huge year-over-year gains but in line with retailers' forecasts. Most lines are moving well, with activity centered, as expected, in apparel and other soft goods.

Merchants are counting on a buildup in consumer confidence to keep sales moving through the summer. With the economy rebounding and shoppers' balance sheets in good order, and likely to improve with more tax refunds and a mid-summer tax cut on the way, retail contacts project year-over-year gains of about ten percent by September. Store operators, however, are planning to keep inventories in check at least until consistent sales growth is obvious. Stock levels are presently very trim.

FINANCE

Third District bankers report little change in loan activity in March. Commercial loan volume, in line with lenders' plans, is about where it was in January, ranging from even-with to nine percent ahead of a year ago. Contacts report some recent cooling of C&I loan demand, however, as rebuilding area businesses cut down on distress borrowing. Retail loan activity remains above last March's levels as well, but, in spite of declining interest rates, consumer caution has kept the demand for loans below bankers' expectations. Banking contacts are forecasting continued sluggishness in overall loan demand for at least the next six months. Unlike retailers, they project a slow recovery, and expect the demand for business loans to be flat. In addition, consumer confidence will be slower in developing than previously expected, they contend, providing only a modest boost for consumer loans by September.

The prime rate at banks in the Third District is currently 10.5 percent, having dropped 50 basis points since the last Redbook. Interest rates have been firming recently with upward pressure coming mainly from worries about the federal deficit and Fed policies, according to banking contacts. Nevertheless, bankers are predicting the prime will slide another 50 basis points by the third quarter, but caution that some temporary upward movement is possible before then.

Deposit growth in the Third District has been substantial over the past six weeks. Demand deposits are currently running as high as seven percent above year-ago levels; bankers cite approaching corporate taxes and an increased precautionary demand for money as contributing to the surprising strength in demand balances. The money market account continues to attract large amounts of new money and keep time deposit levels high, as well. Current estimates put time deposits 16 percent to 40 percent ahead on a year-to-year basis.

FOURTH DISTRICT - CLEVELAND

Summary. Forecasters in this District expect a moderate national recovery with unemployment falling slowly and the inflation rate rising by year-end. Personal consumption expenditure is improving slowly. Employment fell and unemployment rates continue to rise in this District but leading indicators suggest the bottom is near. Manufacturers in general expect little change in activity in March. Automobile production is expected to rise substantially this year. Steel producers had sharp order increases in February but expect no profits until late this year. Machine tool orders are improving but shipments and backlogs are still deteriorating. Loan demand is generally flat with a few indications of improvement.

National Outlook. Economists who attended the Fourth District Roundtable Meeting on March 11 at this Bank scaled up their forecasts of economic activity from their October forecasts. The median of 27 forecasts now shows a 4.3% annual rate of increase in real GNP this quarter, 2.9%, 4.5%, and 5.0%, respectively, in the second, third and fourth quarters and 4.3% in the first half of 1984. None of the 27 forecasts shows negative figures for any of the next six quarters. Industrial production is forecast to rise 8.2% this year (IVQ to IVQ). The median forecast shows the implicit price deflator rising at a rate of 4.6% this quarter, slowing slightly for two quarters, and then accelerating to 5.6% in the fourth quarter. The median forecast has the unemployment rate averaging 10.5% this quarter and falling steadily to 10.0% in the fourth quarter.

Consumer Spending. Personal consumption expenditure is improving slowly. Spending growth on consumer durables this year is expected to be retarded by high unemployment, reduced unemployment benefits, and high real interest rates, but boosted by the rise in stock prices and consumers' improved ability to service debt. Car and truck sales are not expected to rebound as sharply as usual for the first year of a recovery, because sales incentives provided support during the bottom of the cycle. Also customers are reported to be hesitant about purchases because of uncertainty about changes in gasoline prices. One automotive industry economist expects sales incentives to be continued after March 31 only for small cars, because large cars are selling well.

An economist with a major producer of consumer nondurables reports nondurable goods expenditures are well on the road to recovery. The improvement seems fairly widespread across the major components of nondurable goods and he expects the first quarter to show a 3% real year-over-year gain in expenditures, the largest since mid-1981. He also notes some return by consumers from generic and lower-priced brands to higher-priced brands. A major petroleum company expects very little near-term sales response to the drop in oil prices. Expenditures on services in the first quarter will be held down because of the mild winter's impact on sales of natural gas and electricity.

<u>District Labor Market Conditions</u>. Employment fell and unemployment rates in this District rose again in January but leading indicators suggest the bottom is near. Unemployment rates reached 13.2% (nsa) in Wheeling, 17.6% in Pittsburgh, and 18.1% in Erie. Twenty of 88 Ohio counties have unemployment rates that exceed 20% and the state average is 14.9%. However, factory employment, particularly in the automotive industry, is rising slowly and announcements of factory layoffs are less frequent than three months ago.

Leading indicators for Cleveland and Pittsburgh rose in December and January, indicating that the bottom is near in those SMSAs.

Manufacturing. Results of the March survey of Fourth District manufacturers indicate little change in activity from the previous month. Shipments are expected to rise in March, but backlogs, orders, and inventories are expected to show little change. Employment and hours worked are expected to remain at February's level.

The median of ten automotive industry forecasts at this Bank's Roundtable Meeting shows domestic production of automobiles rising 28% to 6.5 million units in 1983. Automobile inventories are reported to be low and, considering current rates of sales and production, are unlikely to rise excessively. Dealer stocks, which fell by 360 thousand units last year, are expected to increase by 150 thousand units in 1983.

Steel-making firms see some improvement in orders and production but are unlikely to earn a profit until late this year. Major steel producers expect domestic consumption of steel to fall by 1% from last year. One major producer notes that since 1948 domestic steel consumption generally has risen only in years when real GNP growth has exceeded 2.7%. Nevertheless, major firms expect industry shipments to rise by 20% and production to rise by 35% as both users and producers partially reverse their sharp inventory declines of last year. However, producers are likely to suffer losses again this year as transactions prices remain well below published prices and recent labor concessions reduce costs by only $15 per ton.

Steel firms had sharp increases in orders in February, mainly from the automotive sector, and expect further increases in March, but order levels remain low relative to capacity. Mills currently are operating at about 50% of capacity versus the 30% low during the 1981-82 recession. Order backlogs are rising but producers are cautious about recalling workers and restarting idled facilities. The price of steel scrap is reported to be up sharply.

The machine tool industry remains depressed with shipments expected to deteriorate further in 1983 although orders should turn up. Order backlogs at current shipping rates are only five months, the lowest in the post-World War II period. Backlogs are low more because of the record length (14 quarters) of the industry's order downturn than because of its depth (87% decline). One firm forecasts no recovery in the industry's shipments in 1983 and only a small recovery in orders.

A major producer of materials for the construction, automotive, and general industrial sectors whose output tends to be coincident with the economy reports sales were up in January but were flat in February, except for February sales gains in fiberglass for the automotive and construction industries.

Bank Lending. Bank loan demand is generally flat with some pockets of strength. Business loan demand has been generally flat this year but is showing some signs of strengthening in March. One banker reports little borrowing thus far to rebuild inventories. Some consumer lending rates have been lowered a little in the past 30 days. Some banks note no strength in demand for new car loans and presume the financing is being done by the manufacturers' credit companies at incentive rates. Residential mortgage lending continues flat, except for strength in Cleveland. A Cleveland bank reports some strength in home improvement loans, only part of which is believed to be a response to unseasonally mild weather. Other consumer lending in the District is generally flat.

FIFTH DISTRICT - RICHMOND

Overview

Most available indicators of economic and business activity in the Fifth District appear to have turned positive in recent weeks. At a sample of manufacturing establishments new orders, shipments, and order backlogs have all improved. The residential real estate sector is also beginning to move with both sales and construction having recently begun to show some vigor. Modest increases in retail sales and in extensions of consumer installment credit are also evident. Labor markets have generally firmed with strength in manufacturing, construction, and agriculture overcoming the seasonal weakness in the trade sector. Prices seem generally to have remained stable. Expectations have improved dramatically since our last survey.

Manufacturing

There was broad improvement in business activity among District manufacturers judging from our latest survey. Orders, order backlogs, and shipments all rose across a wide range of firms and industries. There were very few reports of declining activity. Inventories were nearly flat as a slight increase in materials about offset a minor decline in finished goods. A majority of respondents find current stocks near appropriate levels, although total responses suggest that, on balance, current stock remain somewhat above desired levels.

Survey responses further suggest a turnaround in the manufacturing employment picture over the month. Both employment and the length of the average work week rose since the last survey, although more narrowly than orders and shipments. Several Richmond and branch directors noted instances of recalls or increases in new hirings in their respective areas. Current plant and equipment capacity remains well in excess of present needs, but there is little sentiment for changing existing expansion plans.

The strength described above appears to be developing rather generally across industries. To the extent that differences exist, primary metals and machinery and equipment are among the strongest with textiles not far behind. Paper producers appear to be among the least affected.

Consumption

The evidence from the consumer side is also positive. General merchandise sales have continued to firm and apparently have begun to get support from big ticket items. Retailers surveyed report a relative increase in big ticket item sales and our directors associated with financial institutions have noted an increase in consumer installment loans over the past few weeks. Retailers further report inventories little changed and employment down slightly over the month. Inventories are essentially in line with desired levels, however, and the employment decline is largely seasonal.

Real Estate and Housing

Most indications are that in the residential real estate sector activity is picking up rapidly in many areas of the District. Sales of existing houses began improving shortly after year end and, judging from reports on mortgage credit extensions, that improvement is continuing. In addition, reports on construction employment and building permits substantiate these recent gains.

Agriculture

Fifth District farm credit conditions in the fourth quarter of 1982 were highlighted by the continuing decline in interest rates and a further rise in the availability of loan funds at banks. Farm loan demand generally remained soft, and requests for loan renewals and extensions increased. Farm loan repayment rates continued at a slow pace, despite a modest improvement over a year ago. While liquidity pressures on rural banks eased further, bankers maintained stiff collateral requirements. Meanwhile, farmland values rose slightly but remained well below year-earlier levels.

The Outlook

Perhaps the most noteworthy result of our latest survey concerns the respondents' expectations. Respondents in both the retail and manufacturing sectors are nearly unanimous in the expectation that the level of business activity will improve over the next six months. Higher levels of activity are expected at the national level as well as at the respondents respective market and establishment levels. There is apparently some concern within the business community over the prospect of rising inflation, however.

SIXTH DISTRICT - ATLANTA

Evidence of recovery has become more widespread and consistent since January, and respondents expect this trend to accelerate in most sectors. Previously reported improvements in construction and auto sales are triggering inventory and employment expansion in related industries. Mortgage rates have resumed a downward trend after rising earlier this year. Retail sales growth has tapered somewhat, but many merchants are expanding inventories in anticipation of a resurgence in consumer spending. Savings deposits at banks and thrifts continue to expand although less rapidly, and consumer lending has picked up slightly for the first time in months. The upturn in tourism is extending to more areas and markets. Farm lenders are less pessimistic than when previously polled, even though delinquencies and foreclosures are still mounting.

Employment and Industry. More signs of recovery are appearing in manufacturing. Local orders for auto parts are rising substantially in response to increasing auto sales. The upturn in construction is stimulating lumber yards to rebuild inventories and building materials manufacturers to recall workers. Even heavy industries are beginning to report increases in orders and expansion plans. A sharp drop in Florida's February unemployment rate to the single-digit level strongly signals the end of recession since Florida's cycle lags that of other states. Oil, petrochemicals, shipping, and aluminum remain depressed, however. A survey of Louisiana petrochemical plants reveals no significant change in production levels or capacity utilization, but hope remains that lower costs for petroleum-based raw materials will boost the industry. Reduced oil prices should also aid Louisiana's Offshore Oil Port, which is now handling one-third of break-even volume, but they would adversely affect regional synfuel projects, such as coal gasification.

Consumer Spending. Retailers report that the upward trend in consumer spending is continuing but at a slower rate than in January. They cite atypically mild weather as the reason that the Southeast fared better than the nation in February. A poll of regional department store officials indicates that most are building "heavier-than-usual" stocks of apparel and appliances, which are moving well. Ordering for most other merchandise, however, remains cautious. Car dealerships report increased floor traffic this month and reviving demand, although sales at Ford's regional dealerships fell almost 5 percent last month from year-ago levels. Because of customers' recent responses to lower interest rates and falling gasoline prices, dealers are expanding inventories, particularly of large models carrying high profit margins.

Construction. A poll of realtors reveals high optimism. March sales are running even with or above February levels. Most respondents expect the progressive improvements of the past months to continue. A survey of building permit departments indicates that applications appear to be coming in at a faster rate than last month. Even more depressed cities, such as Birmingham and Chattanooga, are beginning to report a quickened pace. Conventional mortgage rates continue to ease after edging back up in January and early February. By mid-March the rate structure in Atlanta drifted down from early February's range of 12 to 13 5/8 percent, with most lenders at 13 1/4, to a range of 12 to 13 percent, with most lenders at 12 3/4 percent. Discount points on FHA and VA loans firmed slightly the second week of March. As many as 6 3/4 points are being charged on some mortgages.

Finance. Total deposits at large commercial banks fell slightly last month relative to the previous month for the first time since last August. However, buoyed by money market deposit accounts (MMDAs), savings deposits at banks and thrifts continued to grow, albeit more slowly than the 26-36 percent rates prevalent at year-end. Commercial banks report continued uncertainty about the maturity of assets against which to match this new instrument. Investments, particularly treasuries, are currently favored. Construction and commercial loans should receive a large portion of these funds once their stability is determined. Growth in corporate and real estate loans moderated last month after jumping sharply in January. Consumer loans grew slowly for the second successive month after a quarter of decline. District banks are pioneering innovation in financial services. Next month a bankers' bank, offering correspondent services to 50 independent banks, will begin business in Florida. Two southeastern banks have entered a joint venture with two other financial firms and a major publisher to offer national financial services, including home banking and cash management, through a videotex system. A Georgia bank will offer banking, insurance, and travel agency services in three Atlanta supermarkets by May.

Tourism. Although improvements in travel and tourism remain concentrated geographically, reports of nascent recovery come from a widening arc. For the first time in months, business travel has begun to pick up, according to industry representatives polled. EPCOT is filling central Florida hotels to capacity, and bookings are "solid" through Easter. Even south Florida's hotels are experiencing rising occupancies relative to last year, but international tourism remains off. A strike by Eastern Airlines, Miami's largest private employer, would exacerbate the area's woes. It might also temporarily reverse the growth in passenger traffic at Atlanta's Hartsfield Airport, which has finally reported the first monthly increase from year-ago levels since September 1981. Only in Tennessee and Louisiana have respondents yet to perceive harbingers of an upturn. Certain markets, such as family tourism and conventions, also remain soft.

Agriculture. A survey of farm lenders reveals a continuing climb in liquidations and bankruptcies relative to a survey taken last fall and to historical norms. Nonetheless, only a minor portion of the District's farmers face severe insolvency.

Lenders believe less than 10 percent of farmers are undergoing partial liquidation and less than 3 percent, complete liquidation. Only one-fifth of farm lenders surveyed anticipate worsening farm financial conditions in the coming two quarters, whereas last autumn a clear majority expected deteriorating conditions. Produce prices are rising. Excess rains have caused a temporary shortfall in shipments of vegetables, and two years of freezes have reduced yields and raised costs for citrus growers. However, new duties should prevent foreign producers from making serious inroads into Florida's orange juice market.

Panel of Economists. Most of the bank, business, and academic economists polled believe the FOMC's monetary policy is consistent with the goals of recovery and nonaccelerating inflation, but business economists regard money supply growth as too rapid for the continued restraint of inflation. No consensus exists regarding the optimal monetary aggregate on which to focus attention. The majority of economists are more optimistic about the strength of national recovery than they were in January, and state forecasters have made upward revisions in their predictions of state recovery. However, most bank economists hold the same views about local recovery as in January. New signs of regional improvement noticed since our last survey are in the areas of disinflation, business services, consumer spending, and housing- and auto-related industry and some light manufacturing. In addition, more respondents see amelioration in construction and auto sales. Economists expect consumer durables, basic manufacturing, and migration to begin reviving in the next phase of recovery. Most panelists see no signs of rekindling inflation, but a few discern such a trend in housing and building supplies.

SEVENTH DISTRICT--CHICAGO

Summary. The economic atmosphere in the Seventh District has improved substantially since the turn of the year. This is the first time such a statement could be made unequivocally since the region's deep problems became manifest in the spring of 1979. Virtually all sectors have seen improvement or at least an end to the declines of the past year and a half. Orders have increased for building materials, steel, nonferrous metals, appliances, paper, paperboard, and various components. Retail sales of general merchandise have improved moderately and airline traffic is booming in response to bargain fares. Order leadtimes have lengthened and wholesale prices have increased for a broad range of hard and soft goods. However, demand for capital equipment remains very slow. Employment, overall, appears to have stabilized, but there is little hope for a significant near-term increase.

Caution Remains. Signs of better times should be kept in perspective. Improved sentiment largely reflects a feeling of relief that the long decline has halted, and perhaps reversed, without the wholesale bankruptcies that some had feared. The entire region remains very depressed. The view is spreading that the problems of the Midwest are chronic, not just the result of another "cycle." Moreover, aside from residential construction and defense (a minor factor here), much of the improvement since December is associated with the aftermath of the rapid inventory liquidation of 1982, especially the fourth quarter. No general resurgence in final demand is anticipated in the near future.

Business Confidence. Various surveys of business sentiment indicate improvement, but this may reflect more a feeling of relief that "we made it" through the crises than renewed confidence. Strength in the stock and bond markets has permitted many companies to greatly improve their balance sheets, and ruthless cost cutting has lowered breakeven points. But debt burdens remain high and most executives are very hesitant in making commitments. An "aversion to risk taking" is evident, to a degree unknown since World War II.

Purchasing Managers' Reports Favorable. In their February reports, purchasing managers' associations in Chicago and Milwaukee showed gains in orders and output for the first time since the spring of 1981. Also, voluntary inventory liquidation appeared to have ended. However, reports of declining employment continued to outnumber reports of increases. Perhaps the most striking development was a sudden surge in prices paid. Since early 1982 these reports had shown prices declining on balance, an unprecedented development since World War II.

Wholesale Prices. Increases in prices are reported for steel, steel scrap, aluminum, copper, brass, nickel, silver, gypsum board, cement, lumber, building hardware, paper, and paperboard. Only oil products and petrochemicals have continued to decline. In many cases, earlier declines in prices and recent increases were effected by adjustments of discounts from list that will not be recognized fully in official indexes. Fierce price competition and very short leadtimes have reflected excess capacity and very low order books. Inventory policies, geared to immediate availability of goods and soft prices, are being modified as these conditions are reversed.

Consumer Purchases. A very large general merchandise chain reports a modest improvement in demand. Inventories are somewhat slim. Retail prices average only 2.5 percent above the year-earlier level, but may be firming. Airline travel in February and early March was at least 10 percent above the year-earlier level, and at a new seasonally-adjusted high. The surge in air travel was encouraged by bargain fares, 12 percent below last year in February.

Employment. In January, payroll employment in the district was 9 percent below January 1979. Nationally, employment was about the same as four years earlier. In the same comparison, manufacturing employment was down 27 percent in the district, about twice the deficit nationally. It is unlikely that job markets will improve significantly in the months ahead. Help-wanted ad volume in Chicago in February and early March was 25 percent below the year-earlier level, and 60 percent below the 1960 base. Conditions in other large district centers are similar. Many employers will attempt to handle any improvement in business without new hirings. Severance of newly hired workers can be costly, especially if government regulators or private litigation become involved.

Capital Goods. The outlook for capital equipment produced in the district remains bleak. A slight rise in sales of small backhoes used in homebuilding is the only improvement in the construction equipment sector. Logging equipment is also up modestly. If the Caterpillar strike (now almost six months old) is settled, output of earthmoving equipment and related components will rise. Large inventories on hand when the strike began have been depleted. Hopes for a revival in farm equipment have been dashed by the government's acreage reduction programs. Rail equipment demand has dropped to the levels of the 1930s. Some orders for trucks and trailers were placed to beat the April 1 tax hike. Machine tool order backlogs have virtually evaporated. This industry, described by its leaders as "severely crippled", is seeking protection from imports. Contracts for factories, warehouses, and commercial structures indicate a further decline in nonresidential construction.

Autos. Sales of auto this year have not been strong enough to justify planned production schedules, which may have to be cut back. However, some analysts point out that a growing share of auto output is for individual orders. Orders are not counted in reported sales data until deliveries are made to customers.

Steel. Orders for steel have risen sharply since year-end, but only for lighter products required for autos, appliances, and housing. Heavy structurals and plates remain very weak. Order leadtimes on sheet steel, near zero in January, are now out three months, a situation that may cause some users to order still further ahead.

Housing. The housing upswing has considerable momentum. Large district realtors report that transactions for existing homes in January and February set all-time highs for those months. Contracts for new residential construction in January in the Chicago area were almost double the low level of last year. Repair and remodel work may be at new peaks. Some gypsum plants are operating six-day weeks with output above rated capacity.

EIGHTH DISTRICT - ST. LOUIS

The economic recovery in the Eighth District, which began around the turn of the year, strengthened in February and early March. Favorable weather contributed to greater retail sales and robust construction activity. Orders for manufactured goods have been rising, and shipments of goods have been inching up. Inventories are relatively low, a positive sign for future production. Total District employment, however, has changed little from January levels, and, although the price level has been increasing only moderately, a few respondents are concerned that the oil price decline is concealing an ominous rise in other prices. Expectations are that sales, production and employment will rise in the spring and early summer, but capital spending plans have changed little.

Sales at department stores in the District averaged nearly 10 percent more in February and early March than in the corresponding period in 1982, a gain of about 7 percent after adjusting for merchandise price increases. Most merchandise sold well, particularly "large ticket" items. Weather was exceptionally good for shopping this year, unlike last year when much of the area was blanketed with deep snow. Merchants also noted that some customers had received large tax refunds as a result of overwithholding after the July tax cut. Automobile sales in the District, after rising sharply in January, changed little in February and early March. Five dealers reported slight increases in sales, while four experienced declines.

New and existing homes sold well in February and early March. More sales of new homes were made in February in the St. Louis area than in any other month in three years, and sales continued at that pace in early March, according to the St. Louis Homebuilders' Association. Favorable reports also were received from other parts of the District.

Residential and commercial construction in most areas of the District has been relatively strong. The average size of new homes has declined, however, reflecting high prices of construction, high mortgage rates, and a sharp rise in gas heating prices. Reflecting the pace of construction activity, lumber sales in the mid-south region have risen, causing an increase in the price of standing timber. Several contractors voiced concern over costs of materials, noting that since last October board lumber has gone up 20 percent; brick 9, percent; concrete, 7 percent; and heating and air conditioning equipment, 4 percent.

Industrial production in the District remained depressed during February and early March, and several large operations were closed, including a tire plant, a foundry, a farm equipment plant and a lead mining facility. However, most industrial firms, other than those producing business equipment and farm machinery, reported increases in new orders and shipments. Total District employment changed little, since most output gains were accomplished by improved productivity, and over two thousand employees were idled by the plant closings. Managers claim that a tight rein has been kept on inventories.

Although shipments from many industrial firms are expanding, reports from transportation companies still present a mixed picture. River traffic at the Memphis harbor declined in February. District rail and trucking activity reportedly was little changed for most products, although an increase was noted in grain and lumber shipments.

It appears that many District farmers will participate in the PIK (payment-in-kind) program of the government. Farmers believe it is favorable for them, and it is expected to reduce inventories of agricultural commodities significantly. Prices of most crops, however, are not expected to rise much above support levels. The sales outlook for farm equipment and seed is bleak with the PIK program.

The financial condition of savings and loan associations in the District is improving, although one large association and several others have been liquidated since January. With the new money market deposit accounts, the associations are able to attract funds, and, with the decline in interest rates since last summer, the associations are now operating at a profit or much smaller loss. Reflecting a substantial inflow of money market deposits in February and early March, the associations have increased their liquidity, reduced average rates on money market deposit accounts from 11 percent to 8.5 percent, made and acquired a greater volume of mortgage loans, and extended more loan commitments. A survey of 14 financial institutions indicates that check withdrawals from the money deposit accounts has averaged less than one a month per account.

NINTH DISTRICT-MINNEAPOLIS

The Ninth District's recovery continues to gain momentum. The directors' reports at our March meeting were unanimously optimistic, probably the most optimistic in several years. Our directors do not appear to share some national analysts' view that the February statistics denote a relapse in the economy. January and February advances in retail, home, and manufacturing sales were stronger than the increases that occurred late last year. The recovery has also begun to reach the district's two weakest industries--metal mining and agriculture. Seven out of Minnesota's eight taconite plants have scheduled some production this spring, and the new Payment-in-Kind Program has engendered some optimism in agriculture. The recovery would have even more momentum if auto sales hadn't eased and falling oil prices hadn't further curbed petroleum exploration in the western part of the district. Furthermore, district state governments' struggles to balance their budgets suggest that considerable weakness persists even though the district economy has started to recuperate. Lending remains lackluster at district banks.

Consumer Spending

As noted in previous Redbooks, the district's recovery has been led by consumer spending. It continues to strengthen. The largest retailer in the Minneapolis-St. Paul area reports a definite pickup in department store sales in January and February and indicates that they were in fact better than expected. Bank directors also report improving retail sales. In South Dakota, for example, some retailers' sales have recently been up as much as 40 to 50 percent from a year ago. Home sales have also continued to gain momentum. According to the Minneapolis Board of Realtors, January and February home sales in Minneapolis and its suburbs were up 34 percent from a year ago compared with a 16 percent year-to-year gain in the fourth quarter.

In contrast to retail and home sales, auto sales appear to have weakened in early 1983. Although several bank directors report that car sales in their immediate areas have been good, regional sales managers for the nation's two largest automobile manufacturers indicate that sales in January and February were down from a year earlier (after being up in late 1982). They view this easing as temporary, however, because consumers have been showing considerable interest in purchasing cars. Early attendance at the Greater St. Paul and Minneapolis Auto Show in mid-March, for example, was at record levels.

Industrial Activity

Manufacturing, like consumer spending, has continued to gain momentum. According to a University of Minnesota survey of Minnesota manufacturers, 38 percent of the respondents reported increases in new orders in February compared with 27 percent reporting increases last November. While the percentage of manufacturers reporting increases rose, the percentage reporting declines dropped to 24 percent in February from 46 percent in November.

Much of this pickup in manufacturing has come from the forest products industries. The revival in home construction continues to result in Montana lumber mills stepping up operations and Minnesota waferboard plants adding shifts. One new waferboard plant in Minnesota, which was completed last year but never opened, now plans to start operations this spring. In addition, a director with the paper industry indicates that Minnesota paper plants are now operating continuously instead of intermittently as they were last year.

At our last writing, the recovery in industrial activity had been confined to manufacturing. It is now spreading to metal mining. Seven out of Minnesota's eight taconite plants are scheduled to be operating in April. All but one plant had been shut down for extended periods since last spring. Many of the plants' operations will remain far below historical norms, however, and their employment levels in April are projected to be down 50 percent from last April.

While metal mining has started to show signs of reviving, petroleum exploration has declined. In February, 64 oil rigs were operating in Montana and North Dakota, down from 75 in December and 159 a year ago. With the recent oil price declines, the number of active rigs is almost sure to fall further.

Agricultural Conditions

The district's farm sector has also begun to show the first distant glimmerings of recovery. Ag analysts in the district confirm our observation in the last Redbook that the new Payment-in-Kind (PIK) Program should bring some relief to district farmers. They feel that the worst may be over and report that farmers are more optimistic about the future than they were prior to PIK. Several ag bankers support that contention, stating that land prices appear to have stopped falling and, in a few isolated instances, have even increased. An economist with a farm supply company also reports that its dealers appear less worried about credit problems than several months ago. The executive secretary of the Retail Farm Equipment Association of Minnesota and South Dakota states that farmers have started to show more interest in purchasing farm equipment. Attendance at his organization's Northern Farm Show in January was up considerably from a year ago. Although these developments suggest that some relief is in sight, these individuals caution that the road back to farm prosperity could be "long and bumpy."

State Governments

Despite signs of a strengthening recovery, district state governments are struggling to obtain funds to maintain public services. The recent recession seriously eroded revenues in Minnesota, Montana, North Dakota, and South Dakota, and these states are not anticipating any marked revenue rebound during the next few years. In addition, recent declines in oil prices are expected to reduce state revenues in Montana and North Dakota during the next biennium by $24 and $35 million, respectively. To obtain revenues to fund their next biennium budgets, Minnesota and North Dakota are resorting to general tax increases. In Minnesota, the governor has asked that a temporary 10 percent income tax surcharge and a 1 percent sales tax increase be extended, and that state property tax relief be reduced. In North Dakota, the legislature has already enacted a 1 percent sales tax increase and is seeking ways to raise another $150 million. Montana and South Dakota have not had to enact any general tax increases.

In three district states, well-intentioned economic development programs are being promoted to offset the recession's severity. These initiatives will, of course, require funding--and at a time when revenues for basic public services are already tight in those states. Minnesota's governor has proposed a $75 million jobs program for those who have exhausted their unemployment benefits, a $30 million program to weatherize public buildings and develop alternative energy resources, a "New Minnesota Enterprise Fund" to finance small businesses, and a series of tax breaks to encourage small businesses to start up and stay in Minnesota. Montana's governor is pushing a "Build Montana" Program that would use 25 percent of the state's coal tax trust fund to assist local governments, build highways, increase capital assistance to business, and upgrade the state's economic development and tourist promotion efforts. South Dakota hopes to become a financial service center and has recently enacted legislation allowing outstate bank holding companies to charter South Dakota state banks so that they can go into the insurance business nationally. Governor Janklow has stated that as many as 30 outstate bank holding companies may be interested in establishing South Dakota banks for that purpose.

Financial Developments

For several months, our Redbooks have been reporting weak loan demand and this trend continues. Bank directors indicate that district bank lending has remained weak in early 1983, as it has nationally. Their comments are confirmed by loans outstanding at district county banks, which were essentially unchanged between early January and early March.

TENTH DISTRICT—KANSAS CITY

Overview. Tenth District business firms anticipate a quickening recovery in the second half of 1983. Inventories continue to be trimmed by most producers, but are satisfactory at the retail level. Mortgage lending activity is strengthening and housing starts are increasing. Winter wheat conditions are good throughout the District, and livestock prices are improving. Loan demand at commercial banks is generally unchanged, while deposit growth is strong because of the growth in money market deposit accounts.

Retail Trade. All respondents report nominal sales gains in the 5 to 10 percent range for January-February 1983 compared to January-February 1982. Retailers attribute part of the recent gains to the mild winter this year; they also indicate that sales of apparel have been strong and furniture and appliance sales have recently improved. Retail prices are stable and profit margins are improved throughout the Tenth District. Inventory levels at retail outlets appear to be satisfactory as the spring buying season approaches. Most retailers expect continued improvement in sales throughout 1983, with gains accelerating in the last half of the year.

Purchasing Agents. The outlook for manufacturers' input prices over the next few months is favorable, despite a slight rebound in steel and raw material prices. The recently announced increase in the base price of steel is not expected to stick due to weak demand, as purchasing agents anticipate continued discounting from base prices. Input prices overall are expected to rise 2 to 5 percent in 1983, mainly in the second half of the year. Inputs remain accessible and lead times short, with the exception of some lengthening of lead times for electrical components and lumber. There is some concern about input availability should the recovery be stronger than initially anticipated, especially because of existing low inventory levels. Yet almost all firms are still trimming their inventories, and intend to continue to do so.

Housing and Housing Finance. Homebuilders' associations report a boom in housing starts with the biggest increases in single-family housing. Sales of new homes are excellent, with prices generally stable. However, lumber shortages are beginning to appear in some areas, and will probably result in a gradual price rise for new homes. Although starts are not expected to maintain their January-February pace, 1983 is expected to be a much better year than 1982.

Savings and loan association officers report very high levels of savings inflows due primarily to the introduction of the money market deposit account. Most expect the positive inflow to continue, but at a somewhat slower rate. Mortgage loan activity appears to be strengthening, with increases in both applications and commitments. Long-term fixed-rate mortgages at 12 5/8 to 13 percent are more popular with consumers than adjustable rate mortgages currently offered at 11 1/4 to 11 3/4 percent.

Agriculture. Good winter wheat conditions are reported throughout the Tenth District, but there is little grazing of cattle on wheat pasture. As the signup deadline for the 1983 Payment-In-Kind program approached, District bankers expected a high percentage—more than 50 percent—of farmer participation, although a range of 40 to 90 percent was reported, depending upon the crop and the area. Wheat farmer participation is expected to average around 40 percent, while corn farmer participation is expected to average close to

80 percent. Most farmers in the Tenth District have been able to obtain credit for their spring financial needs. Livestock producers are doing better than last year due to a mild winter and higher prices. Production costs for all farmers may decline somewhat in 1983 as a result of lower inflation, declining energy costs, lower interest rates, and acreage cutbacks for major crops. However, at least 25 percent of District bankers' farm customers are experiencing severe financial stress this spring. Without improved economic conditions by yearend, District bankers estimate that 2 to 5 percent of their farm customers may go out of business.

Banking. Tenth District banks report that loan demand is unchanged from last month. Commercial and industrial lending is down slightly while real estate lending is up slightly. Although loan quality is generally stable throughout the Tenth District, a few banks have tightened nonprice terms of lending due to concern about quality. The prime lending rate ranges from 10.5 to 12.5 percent with 11 percent the most common rate. This represents a decline from last month's rates of 11 to 13 percent with 11.5 percent most common. District banks report strong growth in deposits and substantial shifts in the composition of deposits. Demand deposits and large CD's are down sharply from the previous month while conventional NOW accounts, money market certificates, and small saver certificates are down slightly. Super-NOW accounts are still being opened, but not in large numbers. In contrast, all of the banks surveyed report significant growth in money market deposit accounts (MMDA's). While most of the growth is from depositors shifting out of other types of accounts, net deposit inflows are a significant source of MMDA growth.

ELEVENTH DISTRICT—DALLAS

The Eleventh District economy continues to show some signs of recovery primarily from gains in residential construction and related sectors. Weakness in the energy sector, however, is keeping unemployment high and industrial production low. Lending at commercial banks and savings and loans increased because of growth in construction loans. Auto sales are well above last year's level but below the robust monthly gains reported in January. Other retail sales are mixed; some areas are showing gains in real terms, mainly in spring apparel and big ticket items, but sales along the energy-dependent Gulf Coast and along the Mexican border are weak.

The Texas unemployment rate climbed to 8.8 percent in February from 8.2 percent in January. Layoffs in oil field equipment and related industries overshadowed gains in services and construction-related industries.

Drilling activity continued to decline sharply in February, although the rate of decline in early March slowed. Falling crude prices on the spot market, uncertainty about an OPEC price agreement, the natural gas glut, and seasonal factors contributed to the decline. In addition, rather than drilling for new reserves, larger oil companies are buying reserves from bankrupt firms. The recent OPEC agreement has reduced uncertainty about oil prices, but drilling activity should continue to fall as adjustments are made to lower oil prices and the excess supply of natural gas.

Manufacturing production is mixed. Oil field equipment production is still declining. Inventories have been greatly reduced, but at current drilling rates, still exceed a year's supply. Steel orders from commercial construction continued down, but orders of flatroll steel for auto production increased. Refinery production is stable, as is chemical production. Strength in residential construction is pushing up lumber and wood production as well as stone, clay, and glass output. Electronics orders were up, although manufacturers are concerned that this may be temporary. Orders for aluminum products increased sharply, but idled capacity has not been brought on line. Producers are concerned that buyers may be stockpiling before scheduled price increases take effect and labor contracts expire.

Deposit growth at commercial banks picked up. Declines in demand and time deposits were more than offset by gains in MMDAs. Rates on MMDAs were reduced and are now at or below large CD rates. Weekly inflows are now averaging just under $1 billion. Declines in the energy sector kept business loans weak. Business loan demand is expected to remain sluggish in the near-term. Real estate lending picked up, mainly from drawdowns on previous commitments. Seasonally-adjusted consumer loans increased modestly. A major bank lowered its credit card rate to 19.5 percent, and other banks may follow.

At S&Ls, net deposit inflows from MMDAs continued. Loan demand for residential mortgages has slacked off recently. Respondents suggest that a slight uptick in mortgage rates may have induced borrowers to wait for lending rates to turn down again. But demand for residential mortgages is expected to be strong in the second quarter. Demand for interim construction loans is high. Builders are increasing inventories to prepare for the prime selling season. Foreclosures have increased, especially in Houston, but not by enough to cause concern.

New car sales in February were substantially higher than last year's but a little below the January pace. Dealers expect a surge in sales towards the end of March when discount financing plans are scheduled to end. Inventories generally are consistent with dealer plans, except in Houston and San Antonio, where some dealers have an unusually large number of 82's. Used car sales picked up in late February and early March from generally soft levels.

Texas cotton farmers are expected to plant 22 percent fewer acres in 1983 than in 1982 because of heavy participation in acreage reduction programs. As a result, cotton prices should firm later this year. February cattle marketings were the second highest in three years. If this level continues, herds should be reduced enough by late spring to push up cattle prices and increase profit margins.

Residential construction is the dominant force in the Texas recovery. Single-family housing starts and sales are booming. Inventories of new single-family homes should increase during the next two months as January starts are completed. Builders are no longer waiting for a sale before beginning construction. Multi-family housing construction has slowed, but still is unseasonally high.

Commercial construction activity is relatively stable. Contacts indicate that the pace of retail and office building construction last month was even with January's. Retail construction is strong, but new announcements on office building projects are slow.

TWELFTH DISTRICT -- SAN FRANCISCO

The Twelfth District economy appears to have moved out of the depths of recession and into the early stage of recovery. Consumer spending and residential construction are leading the upturn. Retail sales at department stores and auto dealerships are improving, while the decline in mortgage interest rates continues to spur a steady recovery in Western homebuilding and sales activity. Manufacturing and mining activity is picking up in a few important industries such as forest products and nonferrous metals, but most of the region's industries continue to experience extremely weak demand. District banks are beginning to more actively seek consumer loan business as an attractive investment for their large new inflow of funds into the Money Market Deposit Account.

Consumer Spending

Retail sales appear to have strengthened in January and to have remained stable in February despite abnormally inclement weather in some areas. Major department store chains in Southern California reported "excellent" sales results for both months, with sales for January up nearly 10 percent from a year earlier and sales in February recording a 9 percent year-to-year gain. Even in the Pacific Northwest, where sales had been extremely depressed, department stores are reporting strong year-to-year increases. Sales of both nondurable and durable goods are reported to be improving. The upturn in home sales is helping to spur sales of furniture and other big ticket household items. Interest rate concessions by automobile manufacturers, and declining gasoline prices, have stimulated sales of automobiles and recreational vehicles. Inventories at retail outlets (non-auto) are very low and it is evident that some re-stocking will have to take place soon if sales continue to pick up.

Manufacturing and Mining

While manufacturing and mining activity is still extremely depressed, some important Twelfth District industries are finally beginning to show some life. In the Pacific Northwest lumber industry, orders and prices have been rising in response to the recovery in national homebuilding activity, enabling numerous mills to reopen. The aluminum industry also has reactivated some idle capacity. In the Intermountain states--Arizona, Nevada, Utah--some mining facilities also have been re-opening as a result of some improvement in the demand for copper and other nonferrous metals. Layoffs continue in a number of other important industries however. In both California and Washington, the aerospace equipment manufacturing industry has continued to cut back overall employment as growth in defense-related payrolls has been insufficient to offset continued layoffs in commercial aircraft and electronic equipment programs. The move by Atari, Incorporated to move its manufacturing operations from Northern California to Hong Kong and Taiwan to reduce costs is indicative of the intense competitive pressures existent in the electronics industry. The decline in oil prices is depressing oil drilling activity and revenues in Alaska and California and causing layoffs at Intermountain coal and uranium mining sites.

Construction and Real Estate

The drop in mortgage interest rates continues to spur a further recovery in homebuilding and sales activity. Housing starts in the West are now running at more than double the post-World War II low reached a year ago, and permit activity points to still further gains in the months ahead. Sales of new homes also are increasing, but the inventory of unsold homes still remains high in some areas, particularly Southern California. Home prices are reported to be rising again. In contrast, commercial development and construction activity is clearly slowing, and the completion of office buildings started earlier has led to a rise in unused office space.

Agriculture

Rain storms and flooding have seriously damaged the California farm sector this winter, causing crop losses estimated at around $300 million. About 20 percent of the state's normal winter wheat harvest has been lost. Other important fruit and vegetable crops such as lettuce, artichokes, asparagus and strawberries have suffered serious damage, causing some increase in prices. But the strongest pressure on prices could come around May and June, because of delays in plantings of processing tomatoes and an array of other vegetables. Also, the storm is threatening the tree fruit and nut crop by preventing pollination of blooming orchards. Despite recent price increases, District farmers and ranchers expect 1983 to be another difficult year, with net income showing little, if any, improvement over 1982's depressed level. The acreage cutback under the Federal payment-in-kind program will help stabilize income for producers of grains and cotton, but only permit them to "survive" for another year.

Financial Institutions

Loan growth at Twelfth District commercial banks remains weak. Instead of turning to banks, businesses are taking advantage of improved bond and equity markets. Mortgage lending remains weak, as the upturn in housing takes time to translate into mortgage borrowing. Consumer lending is showing some signs of a pickup however. Captive finance companies providing discount financing on auto loans, for example, are experiencing a strong demand for credit, which in turn is helping to boost auto sales. One large California bank has already started offering auto loan rates that are competitive with finance company rates. Other banks appear ready to more actively promote consumer loans, given their relatively high yield and the need to invest the sizeable volume of new funds generated by the MMDA's. With the continued strong inflow of funds into MMDA's, these accounts now represent nearly 20 percent of total domestic deposits of District banks.