

For use at Noon, E.S.T.
Wednesday
January 18, 1995

Summary of Commentary on _____

Current Economic Conditions

by Federal Reserve District

January 1995

SUMMARY OF COMMENTARY ON CURRENT ECONOMIC CONDITIONS

JANUARY 1995

TABLE OF CONTENTS

SUMMARY	i
First District--Boston	I-1
Second District--New York	II-1
Third District--Philadelphia	III-1
Fourth District--Cleveland	IV-1
Fifth District--Richmond	V-1
Sixth District--Atlanta	VI-1
Seventh District--Chicago	VII-1
Eight District--St. Louis	VIII-1
Ninth District--Minneapolis	IX-1
Tenth District--Kansas City	X-1
Eleventh District--Dallas	XI-1
Twelfth District--San Francisco	XII-1

SUMMARY¹

Summary. Economic expansion remained vibrant around much of the nation in recent months, and conditions seem to have grown more uniform among the Districts. The underlying momentum in consumer spending growth remained quite strong. Manufacturers continued to offer some of the brightest reports within the Districts, although the overall pace of expansion in industrial output may have eased somewhat. Assessments of auto industry conditions remained upbeat. Higher mortgage interest rates appear to have slowed single-family housing activity, but multifamily residential and commercial construction remained relatively strong. Expansion in bank loans slowed, led by weaker demand for home mortgage, home equity, and residential construction loans. Production responses to livestock price declines are anticipated to bolster farm income in the current year. Labor markets continued to strengthen, with most reports indicating unchanged to somewhat higher wage increases. Price increases seemed somewhat more widespread than were reported in early December, while higher inflationary expectations were apparent in business surveys.

Retail Sales. Retail sales increased at a moderate pace in the holiday season. Sales gains may have fallen modestly below expectations formed just after the Thanksgiving weekend, but weather effects and other factors point to stronger underlying momentum in spending growth. Nearly every District reported continued strength in sales gains for hard goods and/or big-ticket items, including personal computers, other consumer electronics items, home furnishings and appliances. Assessments of auto sales remained quite positive in much of the nation. Apparel sales were weaker in normally cold Districts that experienced relatively warm winter weather, and many apparel retailers reported heavier-than-anticipated discounting. However, there were signs of underlying strength even in the apparel category. Several Districts in the northern part of the country noted that apparel sales weakness was concentrated in outerwear, while retailers in the Atlanta District noted that warmer-than-usual weather held back overall holiday sales gains, *except for apparel*, which showed relatively strong gains.

¹Prepared at the Federal Reserve Bank of Chicago based on information collected before January 10, 1995. This document summarizes comments received from businesses and other contacts outside the Federal Reserve and is not a commentary on the views of Federal Reserve officials.

Manufacturing. Manufacturers continued to provide some of the strongest reports within the Districts, although the overall growth rate may have slowed modestly. Philadelphia's survey of manufacturers showed output continuing to grow in the fourth quarter, although somewhat more slowly than a strong year-earlier period; looking ahead, about twice as many respondents expected order increases than decreases during the first half of 1995. Richmond's mail survey also suggested that most manufacturers expect further gains in output, with little change in the pace of current growth reported since the last survey. Purchasing managers' surveys in the Chicago region pointed to vigorous gains in industrial output as 1994 came to a close, although expansion was not quite so strong as earlier in the year.

Production and orders trends in durable goods industries continued to lead growth within the overall manufacturing sector. Cleveland's industrial contacts indicated that orders growth remains solid, with particular strength in capital goods industries. Automotive contacts reported some of the strongest sales gains within Boston's manufacturing sector. Cleveland and Chicago reported strength in demand for steel, with Chicago noting that steel output plans for the first quarter were recently increased in response to stronger automotive orders. Auto parts suppliers continued to announce construction of new production facilities in the Atlanta region. Increased exports to Europe boosted recent results among Cleveland's manufacturing contacts. Uncertainty over Mexican developments clouded expectations in several regions, however.

Construction and Real Estate. Higher mortgage interest rates appear to have slowed homebuilding and residential real estate activity around much of the nation. Seasonal patterns account for some of the recent weakness, but home sales weakened in normally cold regions that enjoyed relatively warm and favorable weather. Multifamily and commercial construction were stronger than single-family homebuilding in nearly every District. For example, Dallas reported that overall demand for construction-related products edged up; lumber producers reported lower sales for residential building but increased orders for commercial construction, and glass producers reported record sales partly for the same reason. Declining commercial vacancy rates were widely reported, and continued growth in commercial and multifamily development was generally anticipated in 1995. However, a wider group of

contacts expressed concern about the future impact of higher interest rates on real estate and commercial construction activity.

Banking. Expansion in bank loans slowed, led by weaker demand for home mortgage, home equity, and residential construction loans. Most Districts indicated that commercial and industrial loan demand remains relatively strong. "Outside of housing," San Francisco noted, "bank lending activity is reported to be brisk." A number of Districts reported slower growth or declines in business loan demand, however. After a relatively strong group of reports in December, assessments of trends in consumer loan demand were mixed, with some new slowing apparent even in Districts with relatively strong retail sales gains. Wherever noted, delinquency rates continued to decline. Philadelphia characterized loan officers' outlooks as "positive but cautious," with overall loan growth expected to ease as the year progresses. Reports of tighter lending margins were noted in several Districts, and Philadelphia stated that officers may review future lending plans as a result. Agricultural banks in the Kansas City District reported that crop loans were in better condition than a year ago, while a slump in hog and cattle prices weighed on livestock loan quality.

Agriculture. Production responses to livestock price declines are anticipated to help bring some recovery in farm income in the current year. Kansas City reported that bankers generally expect farm income to improve slightly in its region during 1995, assuming normal crop yields, as livestock prices are anticipated to return to break-even levels. Chicago noted that hog production was up only marginally from last year and well short of expectations. Producers in the Chicago region account for a substantial share of national output, and they have made sizable cuts in planned production. Minneapolis noted that modest recent improvement in livestock prices have improved producer outlooks for 1995, and there are signs of increased farmer willingness to invest in new machinery.

Labor Markets. Continued strengthening and/or increasingly tight labor markets were widely noted, although a minority of Districts suggested that wage pressures may have eased in some occupations. Minneapolis stated that "evidence of tight labor markets abounds." Retailers in the St. Louis and Chicago Districts reported difficulty meeting holiday seasonal labor needs, and St. Louis found that retailers were actively recruiting personnel from other stores. Strong demand for temporary workers was reported in the Boston, Atlanta, and Dallas Districts, with Dallas also noting increasing wage

pressures for temporary labor. Chicago reported that shortages of machine tool operators caused some production bottlenecks, and prompted some capital spending delays because workers were not available to operate new machinery. Reports on permanent manufacturing employment trends were mixed; growth was noted by contacts in Cleveland, Chicago and Richmond, while employment seemed to remain relatively flat among manufacturers contacted by Boston and Philadelphia. At the same time, Boston reported a tighter market for clerical workers, with increased opportunities for permanent employment. New York reported significant job cut announcements in the financial services sector.

Increasing wage pressures were reported more frequently in the Atlanta, St. Louis, Minneapolis, Dallas, and San Francisco Districts, while Kansas City stated that tightness in markets for skilled manufacturing and construction labor had eased. Surveys by compensation consulting companies in the Chicago region suggest that salary increases for exempt salaried employees of large firms will remain in line with 1994, while pay varying with sales growth, profitability, customer service, or other organizational goals will continue to take an increased share of total compensation.

Prices. The pace of price increases seemed steady to somewhat higher since reports in early December, while higher inflationary expectations were apparent in business surveys conducted in San Francisco and Chicago. District reports continued to emphasize shortages and increasing input prices in manufacturing and construction, coupled with stability in most retail prices. Price discounting during the holiday season ran heavier than many retailers had anticipated, particularly in apparel.

Manufacturers continued to report strong (but perhaps diminishing) pressure against output price increases. Boston stated that long-term agreements with suppliers, low labor cost increases, pressure from customers and greater operating efficiency continue to limit many manufacturers' needs for output price increases. Reports from a minority of Districts included a growing set of exceptions to this rule, however.

Retailers in Dallas and San Francisco noted higher price pressures from rising packaging costs. Labor shortages and strong demand increased price pressures among service firms in the Dallas region. Agricultural businesses in the San Francisco region expressed concern about rising labor, transportation, packaging, and raw materials costs.

FIRST DISTRICT - BOSTON

Reports from First District businesses in early January were similar to those in October and November. Manufacturers' gains are widespread, while retailers' results vary considerably. Prices of selected inputs are reportedly rising.

Retail

First District retail sales results were highly varied during the holiday season. Two "category" chains reported sales increases of 15 to 30 percent compared to year-earlier levels. Department stores and food chains cited more modest growth of less than 5 percent. And contacts at off-price discount and specialty apparel chains experienced declines in December sales of 3 to 6 percent, which they attributed, in part, to department stores' huge promotions prior to Christmas. Products that fared best were hard goods such as electronics, appliances, audio equipment, sporting goods, and furniture. State tourist agencies report exceptional fall and winter tourism in New England because of increased business and international travel.

Retail contacts' expectations for the first half of 1995 also vary widely, ranging from 0 to 20 percent sales growth from a year earlier. Vendor and retail prices remain fairly level, although the number of exceptions is growing, including plastics, resin-based products, paper, and cotton. Most contacts report higher profits in fiscal 1994, and only one mentioned lower gross margins because of holiday promotions. Major capital and employment expansions in 1995 are limited to the top-performing large category chain-stores.

Temporary Employment Firms

Contacts in the temporary services industry report steady growth in business in the fourth quarter of 1994. The market for clerical

workers has tightened, a development which personnel firms attribute to increased opportunities for permanent employment; client companies are encouraging more temporary workers to "go permanent" and hiring new staff directly. Temporary employment firms sense an overall upswing in optimism among their business clients and expect demand for their services to remain strong. Winter activity is somewhat weather-dependent, as weekday storms can force workers to cancel assignments.

Manufacturing

First District contacts report that demand for manufactured goods continues to increase, with variations across products similar to the recent past. Automotive and computer-related sales show double-digit increases from a year ago, while electrical and paper products generally show solid single-digit growth. Appliance sales reportedly continue to increase, although more slowly than in early 1994. Demand for textiles and medical and pharmaceutical equipment remains sluggish.

Manufacturers report significant cost increases for paper and packaging, plastics, steel, polyester fibers, and postage; moderate cost increases for chemicals; unchanged costs for cotton fibers; and declining costs for electronics components. Selling prices mostly are flat or slightly higher than a year ago. Some contacts report that their industrial customers are imposing limits on price increases. In other cases, negotiated agreements with suppliers, a lack of labor cost pressures, or greater operating efficiencies are limiting the need for price hikes.

At most respondent companies, U.S. employment has remained flat or has decreased at a single-digit rate over the past year. Only a couple of smaller firms have expanded their work force to any significant degree.

Most manufacturers expect good results in 1995, although the majority anticipate a slowdown in U.S. GDP growth by the second half of the year. Exports are projected to be a bright spot. Several contacts say that they will try to raise prices before the anticipated slowdown.

Residential Real Estate

Contacts report that recent increases in mortgage rates are starting to depress the residential real estate market, particularly for existing homes, but normal winter slow-downs make current trends hard to identify. Respondents in the three southern New England states and Maine note that fourth quarter sales of existing homes were at or below year-ago levels. By contrast, newly constructed homes in the middle and upper price ranges are selling well, although more slowly than last fall. Housing prices are stable in most places. Several contacts express concern that higher interest rates will further dampen the spring market.

Nonbank Financial Services

Respondents at insurance companies report increases in sales between 2 and 20 percent in the fourth quarter of 1994 compared to a year earlier. Annuities and variable life insurance continue to be strong sellers, while whole life products are lagging. A number of respondents have added distribution channels for their products or are exploring doing so, particularly distribution through banks.

Employment was flat in the fourth quarter at all but two insurance contacts (who expanded slightly). Half the respondents plan to cut employment in 1995, some significantly; the rest plan either small increases or no change.

SECOND DISTRICT--NEW YORK

Reports on District developments in recent weeks by and large indicated some improvement. Most retail contacts reported that holiday sales were on or slightly above their expectations and office leasing activity was sufficient to reduce the vacancy rates in several parts of the District. District unemployment rates fell sharply in December. Homebuilding activity, though, has been seasonally slow. Almost 90 percent of the senior loan officers surveyed at small and mid-sized banks reported steady or lower aggregate loan demand compared with two months earlier.

Consumer Spending

Most District retail contacts reported that holiday sales results were on or slightly above plan though their own targets were apparently lower than many analysts saw for the industry as a whole. The weak sales plans were at least in part based on lackluster sales of apparel and outerwear during much of October and November. As a result, some respondents had reduced their orders for soft goods prior to Thanksgiving, and all prepared for what several described as the most promotional holiday selling season they could remember. As a result, profit margins are expected to have suffered.

The annual survey of the Retail Council of New York State found that sales gains throughout the state averaged 3 to 5 percent above the 1993 level for the day-after-Thanksgiving through day-after-Christmas period. Household durable goods, computers, VCRs, jewelry, accessories and in-line skates were some of the best-selling items. Individual retail contacts in the District reported over-the-year changes ranging from virtually flat to +8 percent during December. Inventories were generally in satisfactory shape by year-end with most contacts expecting to eliminate any excess amounts during January clearance sales.

Residential Construction and Real Estate

Homebuilding activity has been seasonally slow in most of the District recently. Looking ahead, some contacts expressed concern that higher interest rates may become more of a deterrent in the spring (when buyer traffic typically picks up substantially) than they have been up to now. Others are apparently more optimistic as witnessed by the fact that several large, long-stalled projects have recently been revived in the District. These include waterfront developments in Jersey City and the Bronx as well as a townhouse project on Staten Island.

While office leasing activity has reportedly slowed somewhat from earlier months, it was sufficient to reduce the vacancy rates in several parts of the District recently. In downtown Manhattan the office vacancy rate has moved down in each of the last three months after a jump in September, while in midtown Manhattan, the rate in December was a full percentage point lower than three months earlier. Among other areas reducing office vacancy rates between the third and fourth quarters were Fairfield County, Connecticut and, in New York State, Westchester County, where the rate fell more than two percentage points, and Nassau County. Office vacancy rates rose in the fourth quarter in Northern New Jersey and Suffolk County.

Other Business Activity

District unemployment rates fell sharply in December as New York's rate dropped to 5.4 percent from 6.3 percent in November and New Jersey's declined to 6.1 percent from 6.6 percent. State unemployment rates are very volatile, however, and could bounce higher in the near future. There have been several recent announcements and reports which point to future job cuts. Chemical Banking plans to eliminate 3700 positions, 9 percent of its staff, and further layoffs are slated in the brokerage industry as well. Cutbacks and reduced profits in the financial industry have been cited as one major factor in the recent widening of New York City's budget gap.

The City, New York State, and New Jersey all face budget gaps in the billions of dollars which at best will mean further declines in services and could involve additional employment cutbacks. Finally, as an outcome of the Macy-Federated merger, A&S will close its executive offices in Brooklyn, laying off some 650 employees there.

On a more positive note, New York City was one of six cities chosen nationwide as urban empowerment zones, each of which will receive \$100 million in social service grants and tax breaks for businesses located in the zones. In addition, KMart recently signed a lease to open its first Manhattan store--the latest of the chain stores making their first forays into the borough in response to lower rents and the enticement of population density.

Financial Developments

Almost 90 percent of the senior loan officers surveyed at small and midsized banks in the District reported that aggregate loan demand was either steady or lower when compared with two months earlier. The residential mortgage and refinancing segments saw the largest declines in activity. About half of the banks experienced less residential mortgage demand while over three-fourths experienced lower or no refinancing activity. The commercial and industrial loan segment was the strongest, with over half of the survey participants reporting steady demand and about one-fourth reporting higher demand.

Loan rates are mainly higher or the same across all categories of lending. Almost all of the respondents noted that recent increases in deposit rates resulted in no change or a narrowing of the spread between the average lending and deposit rates. Of the senior loan officers surveyed, about 80 percent maintained and about 20 percent increased their willingness to originate various types of loans. Very few banks changed their credit standards, and almost all had stable or lower delinquency rates.

THIRD DISTRICT - PHILADELPHIA

Reports from Third District business contacts in early January suggested that economic activity was continuing on an upward path, but the rate of growth had eased somewhat from the pace set in the fourth quarter of last year. On balance, manufacturers reported increases in orders and shipments, but the gains were not as widespread in January as they had been in December. Retailers gave mixed reports for the Christmas shopping period. Sales of consumer electronic goods were up strongly from the prior year, but apparel sales were below expectations, leading to widespread discounting to clear out inventories in the weeks after Christmas. Auto dealers said sales slowed seasonally in December, but the overall trend continued to be up, with strong demand for certain models leading to price increases and waiting periods for buyers. Bankers generally indicated that lending continued to move up moderately as the new year began, with business and credit card lending being the strongest categories of credit.

Forecasts for the new year in the Third District are generally positive, although guarded. Manufacturers expect activity to continue to rise, but they anticipate just steady employment over the next six months. Auto dealers expect unit sales in 1995 to exceed those in 1994, but other retailers say it is difficult to make a forecast for the year at this time. Bankers expect some continued growth in lending in the months ahead, but some believe loan growth may taper off in the second half.

MANUFACTURING

Reports from Third District manufacturers in early January indicated that industrial activity continued on an upward trend, although the rate of growth had

slackened from the final quarter of last year. Slightly more than one-fourth of the firms polled reported that they were receiving more orders and making more shipments in January compared with December, while about half indicated that orders and shipments were steady. Gains were more common among producers of metal products and equipment, while steady conditions or declining activity were more frequently noted by makers of nondurable goods.

Employment conditions were virtually steady at manufacturing plants in the District. While there were a few reports of stepped-up hiring, three-fourths of the industrial establishments contacted were holding employment steady. On balance, area firms were reducing working hours slightly in early January.

Industrial prices in the region continued to move up as the new year began. More than half of the firms commenting on prices said they paid more for inputs in January than they had in December, and there were very few reports of price declines. About one-fourth of the manufacturers contacted said they were raising prices for their own products; most said they were holding prices steady.

Looking ahead, Third District manufacturers expect business to continue moving up through the first half of the year. About four in ten of the firms contacted for this report forecast increases in orders and shipments, and two in ten anticipate declining demand for their products. Overall, Third District manufacturers plan to hold employment and working hours steady, and to reduce inventories. While most will also keep capital spending on an even pace, more than one-fourth have scheduled increased investment expenditures for the first half of the year.

RETAIL

Retailers in the Third District gave mixed reports on sales for the Christmas shopping period. Stores selling consumer electronic items--personal

computers, large-screen televisions, and camcorders--said sales were well above the year-ago period. Home furnishings were also listed among the categories of merchandise that sold well. Apparel retailers had disappointing results; with sales falling below expectations, they were prompted to offer deep discounts both before and after Christmas. The pace of retail sales in early January appeared to be somewhat subdued, with price reductions being continued in efforts to reduce inventories, especially for apparel.

Third District auto dealers said sales slowed seasonally in December but rose above the level of December 1993. In general, dealers reported sales gains for 1994 over 1993, and they expect continued increases in unit sales in 1995. Sport-utility vehicles continued to be in demand, and price increases and waiting lists were becoming common for these and some other popular models.

FINANCE

Third District commercial bank lending officers contacted in early January said loan volume was growing moderately. Several mentioned modest growth in commercial and industrial lending, with middle-market companies prominent among new borrowers. Bankers continued to describe the market for new business lending as competitive. In general, bankers also said consumer credit was growing, with credit card borrowing being the strongest category of personal lending. Some bankers noted that while there were signs of increased interest by institutional investors in commercial real estate, banks in the District did not plan to increase their exposure in office or industrial properties.

The outlook among the commercial bank officers interviewed for this report is generally positive but cautious. While most expect the region's economic performance to be good, at least through the first half of the year, they foresee a slowdown in the growth of consumer spending that will limit growth in total

business activity for the year as a whole. In line with this forecast, they expect overall loan growth to ease as the year progresses. Several bankers also noted that loan profitability, for both business and consumer lending, has been coming under pressure and that they may review their own lending plans for the year as a result.

FOURTH DISTRICT - CLEVELAND***Summary***

Business activity in the District is holding steady at a high level, with industrial producers reporting continued growth in production and orders. Employment levels have picked up recently, although not in all regions or sectors. Further, there are few indications of any broad-based wage pressures, and price pressures remain largely centered in industrial commodities. District retailers indicate sales were good over the holiday period, and undesired inventory accumulations were limited. In fact, area auto dealers continue to complain about inventory shortfalls of 1995 models.

Lending is active in most institutions, and credit margins are still narrowing. Only in the mortgage area has there been a significant drop-off in loan growth since the last District report.

Manufacturing

District manufacturers continue to report solid orders growth, and the orders backlog in capital goods industries remains unusually long. Export orders are also reported to be holding up well. Chemicals, plastics, steel, heavy truck, and some machine tool industries are reporting production levels near historic highs. Surprisingly, capacity constraints in these industries are not generally seen to be holding down production, and many District producers anticipate expanding productivity further to meet current demand. Nevertheless, resistance to adding new workers seems to have diminished somewhat, and a few firms here indicate more willingness to add to their permanent staffs.

Capital goods producers continue to report a further growth in orders, with the domestic auto industry a heavy source of demand. Orders for metal-cutting and metal-forming machine tools are strong, following the upward trend in steel demand: The orders backlog here extends well into 1995. Export orders for capital goods are improving

IV-2

gradually for European customers, and District manufacturers expect sales to Europe to improve further in 1995. Small growth in the Japanese market is also hoped for this year. However, there still is reported to be little room for substantial price increases for finished capital goods, despite reports of production constraints by many capital goods producers.

Industrial materials producers also note strong business conditions, especially steel and chemicals suppliers. Both industries are also reporting improved sales volume in Europe. Industrial materials production is reported to be near capacity, and raw materials prices are still increasing, particularly for steel and certain industrial chemicals. However, plans to increase employment in these areas remain modest.

Retailing

Retail sales were strong overall during the holiday period, but activity is reported to have diminished in late December. Some retailers indicated a small inventory overstock at period's end, prompting increased discount activity in early January. Indeed, competitive pressures in the retail sector continue to exert downward pressure on prices, and at least one major retailer noted an easing of prices from suppliers. In general, though, inventory positions appear to be in line with sales, with a notable exception for apparel items, where sales performance has deteriorated further in the wake of unseasonably warm temperatures during the period. Seasonal employment patterns in retailing were about average, and no shortages of temporary workers were reported.

District auto sales in December were also average for this time of year, but some vehicle types are still reported in short supply. Most dealers indicated availability problems with the 1995 models, particularly light trucks and utility vehicles. There is a presumption that low inventory positions dampened dealers' sales performance in December.

Banking and Credit

Virtually every respondent reported strong and growing loan demand. District bankers indicate a particularly high level of commercial lending activity--presumably a response to inventory floor plans, although most categories of commercial lending activity were reported to be somewhat stronger (notably new construction and expansion). However, credit margins are narrowing, particularly for commercial loans, where one District banker had concerns about the erosion of credit quality.

Consumer borrowing remained high during the holiday period, and revolving credit balances are reported to be substantially above this time last year. Mortgage credit activity has fallen off, and although some of this is typical for the season, higher mortgage rates are presumed to have flattened mortgage refinancing.

FIFTH DISTRICT - RICHMOND

Overview: Economic activity in the Fifth District grew moderately in late November and December. Areas experiencing growth included the service-producing sector, state revenues, and agriculture. Strong holiday sales boosted consumer spending. Port trends were mixed, and manufacturing and commercial real estate activity were flat. Loan demand, home sales, and tourist activity declined.

Consumer Spending: Retail associations and retail analysts contacted by telephone reported that Christmas sales increased between 8 percent and 12 percent from last year's level and that after-Christmas sales were good. They also said that retailers offered fewer after-Christmas discounts than they did last year. Analysts' outlooks for early 1995 sales were mixed. Those expecting weaker sales compared to 1994 pointed to higher consumer debt levels, while those expecting stronger sales pointed to last year's unusually harsh weather that kept shoppers at home.

Service-Producing Firms: Preliminary results from a mail survey indicated that activity in the service-producing sector increased in December. Revenues rose, except in health services, where they decreased. Wages also rose, and employment changed little. Service producers indicated that prices rose 0.5 percent in December. They expected increased demand for their services and an increase of 1.3 percent in their prices during the next six months.

Manufacturing: Indicators of factory activity changed little in December from their November levels, according to preliminary results of a mail survey of District manufacturers. Raw materials inventories were up compared to six months ago, and respondents expected a further increase during the next six months. Manufacturers expected shipments and employment to increase during the next six months, but they anticipated little change in the

workweek. Finished goods prices increased faster in December than in November, but at a rate less than the general inflation rate. Raw materials prices increased more in December than in November, and at a rate higher than the general inflation rate. In December, respondents expected prices to rise more during the next six months than they had in November.

Tourism: A telephone survey of hotels, motels, and resorts throughout the District indicated that tourist activity generally decreased in December from November. December activity at ski resorts was below its year-ago level because of warmer weather, but bookings were up for the rest of the winter. Contacts expected better-than-normal business and slight price increases during the next six months.

Ports: Telephone interviews with representatives at the District ports of Baltimore and Hampton Roads (Norfolk) indicated that import and export levels in November were higher than those of a year ago but were mixed compared to their levels in October. Charleston's representative, however, reported that the Charleston port experienced one of its busiest months ever. Representatives at Charleston and Baltimore expected imports and exports to increase during the next six months, but the representative at Hampton Roads expected both to decrease.

Finance: District financial institutions contacted by telephone reported that loan demand continued to slow during late November and December. Consumer and commercial loan demand fell moderately, while mortgage loan demand declined slightly. Interest rates were higher on consumer, commercial, and mortgage loans. Many District lenders expressed concern that future interest rate increases might dampen loan demand. Most consumer and commercial lenders in North Carolina, however, were confident that loan demand would remain strong in that state.

Residential Real Estate: According to a telephone survey of District realtors and builders, residential real estate activity declined in December. District home sales decreased despite increased sales of lower-priced houses. Building permits, buyer traffic, and housing starts, however, were unchanged. Most real estate agents attributed the decline in home sales to increased mortgage interest rates. Home prices remained stable, although prices of nonlumber building materials rose slightly.

Commercial Real Estate: District contacts reported that commercial real estate activity in December grew at the same pace as in November. Real estate contacts reported little change in construction, except in West Virginia, where retail outlet building activity increased. Posted commercial rental rates increased throughout the District. Commercial vacancy rates remained steady except in North Carolina and Virginia, where they declined. Leasing agents reported that the availability of prime office space tightened, especially around Washington, D.C.

State Revenues: State government forecasters said that tax collections grew moderately in November and December. Real revenue growth was strong in Maryland, North Carolina, Virginia, and West Virginia, somewhat weak in South Carolina, and flat in the District of Columbia.

Agriculture: Agricultural conditions were better than a year ago, according to District farm analysts. Small grains were in good-to-excellent condition because temperatures were above normal in December and early January. Tobacco prices remained strong, and farmers' 1995 production quotas rose because tobacco companies purchased farmers' excess stocks of tobacco. Hog and poultry output rose despite sharply lower hog prices and slightly lower poultry prices. One contact said long-term contracts insulated North Carolina hog producers against plunging prices on national markets.

SIXTH DISTRICT - ATLANTA

Overview: According to contacts around the District, business activity in the Southeast continued to expand through the end of 1994, although more slowly than earlier in the year. Most retailers reported that the holiday shopping season went well. Sales generally met expectations, but many contacts had to use more discounting than they would have liked in order to generate business. Auto sales were reported as steady. Tourism and business travel contacts say activity remains above year-ago levels in most of the District; however, parts of the Florida tourism industry have not yet fully recovered from their year-long slowdown. Single-family home building and sales have continued to slow, and most contacts expect a moderately slower 1995. On the other hand, commercial real estate market reports continue to improve. District wages and prices were generally steady; however, there were an increasing number of reports of tight labor markets and higher materials prices.

Consumer Spending: District retailers reported that sales in December met or exceeded their expectations; however, retailers attributed much of their success to aggressive promotions. Several merchants stated that unseasonably warm weather held sales down a bit. Once again, men's apparel and home products were strong sellers and several retailers noted substantial improvements in women's apparel over last year. Retailers said after-holiday inventories were, for the most part, at anticipated levels. Most contacts expect year-over-year sales gains to continue, although some are concerned that the credit card debt incurred during December will curtail consumer's purchases more than usual during the first quarter of 1995.

Manufacturing: District manufacturers reported ongoing spotty growth in December and early January. Strength in orders for paper, pulp, metals, and industrial chemicals is keeping plants in these industries operating near capacity. Auto parts suppliers continue to announce construction of new production facilities in the region. Some producers of electronics for cable television and data communications report order backlogs increasing at double-digit rates. Producers of home textiles such as sheets and towels are optimistic that business will remain strong. However, respondents note that the

market has softened for other products linked to housing such as building products and heating and air-conditioning equipment.

Contacts in the apparel industry continue to report a shrinking factory workweek and payrolls. Temporary help firms supplying personnel for manufacturers report that the pace of placements remains brisk. Foreign orders for military aircraft have brightened the outlook for Lockheed's Marietta, Georgia, facility. However, recent cancellations or scalebacks of U.S. Department of Defense contracts continue to adversely affect many defense-related firms in the District.

The recent peso devaluation has some regional manufacturers concerned that exports of their products will slow as U.S.-made products become more expensive in Mexico. A broad range of regional industries has posted significant gains in exports to Mexico since NAFTA was enacted last January. Most industrial contacts remain optimistic about the near-term outlook.

Tourism and Business Travel: Winter bookings and occupancies are up for some Florida destinations; however, state officials are concerned that rival destinations are capturing a significant portion of the state's market. Weak early winter cruise bookings are expected to pick up in February following an unusually soft fall season, partly attributed to unseasonable weather. Although overall casino traffic in Mississippi continues to grow and larger firms continue to expand, contacts report that weaker firms are laying off employees or filing for bankruptcy. Interest in the 1996 Olympic Games is sharply increasing foreign visits to Atlanta.

Construction: A majority of real estate contacts reported that single-family home sales and construction slowed slightly in December. However, contacts in the Miami and Nashville markets stated that December sales exceeded year-ago levels. Most real estate agents and builders continue to anticipate a modest decline in home sales and construction in 1995.

Commercial and multifamily real estate contacts continue to report improving market conditions. The apartment market is characterized by steadily rising rental rates and high occupancy levels. Contacts say that, as a result, multifamily construction is on the rise in many areas of the District.

Commercial realtors also report declining vacancy rates and steadily increasing rental rates. While commercial construction is reportedly accelerating, the majority of current construction is build-to-suit with most of the space leased prior to building, leaving very little speculative space available. However, builders say that shortages of skilled labor continue to push building costs up. Realtors anticipate both commercial and multifamily markets will exhibit continued strong growth in 1995.

Financial Services: According to District bankers, overall loan demand has been rising modestly. Most contacts reported that business loan demand was up, while consumer loan demand was slightly off. Commercial real estate lending was reported to be fairly active by several contacts. Weakness in consumer loan demand was accounted for mainly by auto lending. Residential mortgage lending has declined. Commercial and consumer default rates remain low.

Wages and Prices: Reports of upward pressures on wages are becoming more frequent among contacts surveyed. Demand in the areas of skilled construction and food services personnel is especially strong in parts of the District. Manufacturers report that prices of raw materials continue to escalate, and more producers expect to be able to increase final product prices. Paper, chemicals, metals, and textile contacts continue to report rising raw materials prices. Apparel and fabric producers are coming under increasing pressure from raw materials price increases but are reportedly not able to raise finished product prices because of consumer bargain hunting pressures at the retail level. A few companies report that higher than usual inventories at the end of 1994 are designed to help offset anticipated additional price increases in 1995. Residential home builders throughout the District report that both materials and labor costs have stabilized, generally steadying home prices.

SEVENTH DISTRICT--CHICAGO

Summary. The District economy expanded at a moderate to vigorous pace in recent months. The underlying momentum in retail sales growth remained strong during the holiday season, and probably exceeded its third quarter pace on a seasonally adjusted basis. Manufacturing activity remained robust for the time of year. Labor markets continued to strengthen, with little sign of softening in employers' hiring intentions heading into the new year. Transaction price increases seem to remain centered in basic materials and intermediate goods, as retailers continued to stress intense competitive constraints on pricing.

Retailing. The underlying trend in retail sales growth remained quite strong during the holiday season. Sales gains reported by large retail chains were generally in line with or somewhat better than pre-season expectations, except for apparel sales, where relatively warm weather held back sales prior to the last week of December. Apparel retailers blamed shifts in consumption toward hard goods, and not weakness in total consumption, for their relative sales weakness. Apparel sales have strengthened in early January, but as one retailer noted, "a good December is a heck of a lot better than a good January."

Most large retailers indicated that year-over-year sales gains improved as the season matured, except in apparel sales. For example, one large durable goods retailer characterized sales in the last week of the season as "booming," with sales gains running well ahead of previous weeks. A number of retail chains indicated that toy sales gains were in line with or stronger than companywide averages, and home entertainment software and computers were among the strongest gift-giving categories.

Excluding apparel sales, most large retailers reported better overall sales gains in the District than their national average. A late December survey by an accounting firm suggested that Midwest consumers had higher planned and actual spending levels than consumers in any other major Census region. Large prospective and actual bonuses in the auto industry boosted retail sales in Detroit and other areas of the District.

The District has experienced large-scale expansion in retailing capacity in recent years. As a result, survey data, reported same-store sales gains, and anecdotal evidence on individual store chain results may well understate the strength of aggregate sales growth. Increased retailing

capacity also helps explain why discounting ran more aggressively than many retailers anticipated at the onset of the 1994 season, in spite of strong demand and customer traffic. The strongest holiday sales gains seem to have arisen in products where prices have been declining (such as computers and electronics) and in outlets where prices are relatively low. Several retailing analysts suggested that discount stores took a larger share of holiday sales growth in the region during 1994, as consumers turned more aggressive in their search efforts after a less-cautious shopping season in 1993. One large outlet mall characterized its holiday sales season as "awesome." Customer traffic was up nearly 30 percent based on vehicle counts, and the number of motor coach trips to the mall were up 36 percent. Separately, this contact noted that charitable gift giving rose markedly from 1993.

Manufacturing. District manufacturing activity remained robust as the year came to a close. The composite production index for purchasing managers' surveys in Milwaukee, Detroit and Chicago has eased back from especially high levels in the second quarter of 1994, but in December still remained at a level consistent with vigorous growth in District industrial output. A similar trend was evident in surveys conducted in Western Michigan. Reflecting continued gains in durable and capital goods output, District steel production posted relatively sharp increases in October, November and December, in contrast to a normal seasonal slowing.

A large automaker stated that dealer orders and showroom traffic remained stable or even picked up a little around the industry in recent months, on a seasonally adjusted basis. A large steelmaker stated that first quarter production plans were recently raised in response to modestly higher auto industry demand than originally anticipated. An association of machining shops reported that production continued to trend higher in recent months, with machine tool purchases among its membership surging since the industry trade show in September. One machine tool manufacturer stated that customers' capacity expansion projects accounted for a greater share of orders growth in recent months, joining continued gains in orders for tools designed more closely for productivity improvement.

Labor Markets. District labor markets continued to tighten up, and there was little sign of softening in employer hiring intentions entering the new year. A substantial number of retailers expressed difficulty meeting seasonal labor needs during the holiday season, although this experience was not universal. An association of machining companies stated that skilled

worker shortages continue to raise production bottlenecks, although they haven't intensified greatly since mid-1994. In some cases these shortages have even prompted capital spending delays, as firms postpone the delivery of needed equipment because workers aren't available to operate the machinery. Staffing services firms have suggested that labor shortages and associated wage pressures are more closely concentrated in blue-collar than white collar labor. Separate surveys by two compensation consulting companies suggested that salary increases in large firms during 1995 will remain in line with 1994, on average, but variable pay (contingent on sales growth, profitability, customer service or other goals) will continue to take an increased share of total compensation.

Agriculture. Hog production during the fall months was up only marginally from the year before and well short of expectations. Moreover, producers have made sizable cuts in both the inventory of foundation stock and in the intended number of litters to be farrowed this winter. As a result, analysts now believe the gains in pork supplies will end early in the second half. Production cuts have been especially apparent in this District, which normally accounts for about half of all hogs raised nationwide.

Prices. Price increases seem to remain centered in basic materials and intermediate goods, as retailers continued to stress intense competitive constraints on pricing. A number of large retailers indicated that holiday season discounting and promotional activity were more aggressive than expected a few months ago. Inflationary expectations continued to rise in the industrial sector, however. The price components of District purchasing managers' surveys climbed further in recent months, pointing to faster industrial price inflation even as output growth slowed a little from its extremely rapid pace earlier in 1994. The price component of the Chicago survey has climbed steadily this year, but remains below levels during the late 1980s. The price component of the Detroit survey has depicted higher price increases for most of the last year, and in December climbed to its highest level since late 1987. A large share of respondents to surveys in Western Michigan continued to express frustration with shortages and lengthy lead times. Looking ahead, another regular survey of District businesses showed a significant increase in the share of respondents expecting higher inflation. When asked to name the most serious threat to 1995 business conditions, rising interest rates and rising inflation were the most frequently mentioned factors in this survey.

EIGHTH DISTRICT - ST. LOUIS

Summary

District economic activity, buoyed by relatively strong holiday sales, continues to increase at a moderate pace. Unseasonably warm weather hindered apparel sales, but big-ticket items like jewelry were large sellers. While a recent survey of small businesses reveals that the majority expect little change in business conditions over the first half of 1995, one-fifth anticipate improving conditions. Tight labor markets remain a major concern among contacts. Firms in various industries report sales and employment growth. Residential construction continues to slow because of higher interest rates, and average single-family home prices are up slightly. Total loans outstanding at large District banks continue to increase, though by less than they had previously.

Consumer Spending

Most retailers in the District report that holiday sales were up an average 6 percent to 7 percent over last year's season. Electronics, jewelry and other big-ticket items were the strongest sellers. Apparel sales were well below expectations because of unseasonably warm weather; however, some retailers in Memphis credit it for their strong holiday sales. Many retailers discounted apparel before Christmas to try to move the merchandise. After-Christmas sales generally met expectations, with most retailers employing their normal price reductions to reduce remaining inventories.

Car dealers generally report increased sales in December, in some cases of up to 20 percent over last year, although some dealers lost sales because of continued shortages of popular models. Many cite creative leasing programs and improved local economic conditions as boosting sales, despite slightly higher prices on 1995 models.

Outlook

A December 1994 survey of 87 District small businesses shows that slightly more than one-fifth expect a more favorable outlook in general business conditions over the next six months; this proportion is up about 5 percentage points from a similar survey conducted in November. More than half, however, expect little change in business conditions over the next six months. Slightly more than one-quarter of respondents plan to increase prices over the next three months, compared with just under one-quarter in November. Nearly half plan no change in prices in the next three months, down from about three-fifths in November who indicated a similar sentiment.

Manufacturing and Other Business Activity

Contacts throughout the District continue to report that labor markets are the tightest they have seen in years. Higher starting wages and increased benefits have not helped many firms find and keep qualified employees. For example, a nonprofit organization that regularly hires seasonal workers to aid with its holiday fund raising was unable to find people, which translated into reduced collections. One contact reports that retail stores were actively recruiting employees from other stores.

Growth in sales and employment continues around the District. Farm equipment dealers report that although sales were down slightly in the most recent period, 1994 was a record year, with sales up about 12 percent over the year before. Various manufacturers in western Tennessee and eastern Arkansas report sales and revenue increases of between 15 percent and 40 percent in late November and early December over the prior month. These contacts report, though, that profit margins are much tighter because of competition and rising costs.

Reports suggesting that many firms are facing capacity constraints are increasing. For example, a food processor reports significant overtime, a printing establishment has all plants running at capacity, and a maker of packaging products now operates three shifts to meet increased demand. In addition, announcements of new plants come from the Little Rock area, northern Kentucky, central Arkansas and northwest Mississippi. Each will bring at least 200 jobs into their areas, most by June.

Construction and Real Estate

Contacts in most parts of the District continue to report slowdowns in residential construction activity, which they attribute to higher interest rates. Northwest Arkansas, however, is enjoying an extended construction boom; the value of its residential construction contracts is up more than 60 percent from a year ago. Most contacts also report that homebuilding in the high end of the market is still relatively strong; east-central Mississippi, though, sees softening in this market. Single-family home sales are down in Louisville and western Kentucky, western Tennessee and St. Louis. Average home prices are up slightly in most parts of the District; contacts in Memphis also report sharp increases in apartment rents.

Banking and Finance

Total loans outstanding at 11 large District banks rose 1.8 percent from mid-October to mid-December after increasing 2.2 percent from mid-August to mid-October. All major loan categories—commercial, real estate and consumer—increased in both periods. Although commercial loans increased more in the latter period than they had in the former, smaller increases in consumer and real estate loans from mid-October to mid-December dragged down the increase in total loans.

NINTH DISTRICT--MINNEAPOLIS

As 1995 opens, the economy of the Ninth District shows robust growth in most sectors. Manufacturing is very strong. Construction is active for the winter season, with commercial projects replacing residential building as the focus of strength. Iron mining expects its best year in over a decade and other metal mining faces favorable conditions. Forest product output remains high, with paper production continuing to gain strength. Modest recovery in depressed farm prices reportedly is fueling some increases in farm capital spending. Consumers are actively buying vehicles, and sales of general merchandise are generally good.

But not all is favorable. Winter tourist businesses are having a slow year so far, largely due to unfavorable weather rather than lack of demand. Residential building remains below year-earlier levels, and sales of existing housing have slackened.

Moreover, some problems associated with strong economic growth persist. Urban labor markets are very tight and many businesses have difficulty in securing employees. Businesses continue to report higher wage increases than were common in recent years. Reports of price increases in raw materials and intermediate goods are common and some such goods are increasingly difficult to secure.

Manufacturing

"Virtually all of our manufacturing customers are doing very well," reports a small business lending supervisor from a major Minneapolis bank. "It is really a boom," he adds. Commercial printers and firms manufacturing circuit boards, other electronic components, die castings, building components and hardware are described as doing particularly well across the district. A Japanese firm opened a small engine plant in Wisconsin citing the current dollar-yen exchange rate as a key factor. A major window manufacturer announced plans for a new plant in Fargo, N. D. Two mainframe computer manufacturers did announce layoffs, but these seem to result from long-term changes in that industry and ongoing restructuring in the particular companies involved rather than any overall weakness in the economy.

Natural resource industries

"The taconite industry is on a roll," is how one newspaper described iron mining in northeastern Minnesota. Production was about 42 million tons in 1994 and is expected to vault to 47.5 million tons in 1995, the highest level in over 15 years. As an exception to overall brightness in this sector, a Michigan mine announced a layoff as part of a consolidation into one site. Copper and other non-ferrous producers

have not expanded output to the extent that iron mines have, since they had less slack capacity, but extremely favorable prices are allowing these operations to replace old or worn-out equipment.

Production of corrugated cardboard and other packaging as well as printing paper continues to increase. Output of other forest products, including lumber and building board, continues strong, and Montana timber employment and output have regained much of the ground lost when a major mill closed in 1993.

Construction and real estate

“Office glut lessens as businesses take up lots of space,” is one recent Minneapolis headline. “People have to build, there just isn’t any decent commercial space left,” comments a suburban St. Paul lender. Commercial projects clearly have passed up housing as the locomotive for the construction sector. New warehouses, distribution centers and other retail facilities are in particular demand. “Retail is to the 1990s what office buildings were to the 1980s,” comments one major national developer and builder based in Minneapolis. Long lead times on new commercial buildings are reported in some areas.

However, residential construction clearly has retreated from earlier highs in many areas of the Ninth District. Single-family home permits issued in the Minneapolis-St. Paul area were somewhat below year-earlier figures in October and November, and industry spokespersons indicate that the same will be true when the December numbers are available. A major home builder noted that actual slowing was less than originally anticipated and stated that business was still good. He cited increasing numbers of new home buyers opting for adjustable rate mortgages as the primary reason why residential housing activity has not slowed more than it has. This pattern, of some slowing from year-earlier levels, but of still maintaining good levels of activity reportedly is true in other urban areas of the district.

Markets for existing homes are cool, however. A Minnesota residential realtor describes sales of existing homes as depressed from levels that prevailed in the two previous winters. Existing home sales reportedly remain strong in rapidly growing urban areas such as Sioux Falls, S.D., and Billings, Mont., but have slowed slightly in other areas.

Agriculture

With crop production in its mid-winter dead season, Ninth District farmers are focused on livestock production and on marketing the 1994 crop. Modest improvements in both crop and livestock prices have reportedly improved producer outlooks for 1995, and a few observers see increased farmer willingness to invest in new machinery before the 1995 crop season. Unseasonably warm weather in December raised

fears that stored, unprocessed sugar beets might spoil, but cold weather in early January has alleviated that threat, at least temporarily. Lack of snow cover in dairy areas is causing concern about alfalfa survival.

Consumer spending and tourism

“The day after Christmas was phenomenal,” according to a manager of a Montana discount store. Holiday retail sales apparently were very strong in Montana and the Dakotas. The Minneapolis-St. Paul area mimicked national patterns: Appliances and consumer electronics sold briskly, but apparel sales were disappointing.

Consumers continue to go for new vehicles. North Dakota’s registrations of new passenger vehicles for December were nearly 5 percent above the already healthy sales experienced a year earlier. Reports from registration agencies and dealers’ associations in other states confirm this pattern.

Winter tourism activity was slow in parts of the Ninth District apparently due more to sparse snow cover than to weak demand. Officials in Michigan’s Upper Peninsula and northwest Wisconsin report a 50 percent decline for December 1994, compared to the prior year. Business stayed even for December at a northern Minnesota ski resort, while snowmobiling dropped from year-earlier levels. Despite unfavorable exchange rates for Canadian skiers, a northwest Montana resort reports a slight increase this season.

Employment, wages and prices

Evidence of tight labor markets abounds. Help wanted signs are posted in all sorts of establishments and classified advertising sections are bulging. Even temporary agencies are scraping the bottom of the labor barrel, the CEO of a computer manufacturer reports, noting that over of half of the workers forwarded by agencies fail a drug screening test, up from less than 8 percent a year ago. Several executives of large Minnesota firms who participated in an economic roundtable hosted by the Minneapolis Fed cited increasing difficulty in securing needed workers and noted that they were raising wages much more than in preceding years. And a small Wisconsin firm that produces ribbon candy, a holiday season specialty, was unable to do so because it could not secure the needed temporary workers.

Both manufacturers and building contractors report price increases for materials they need. Some steel uses still experience delivery delays. Precast concrete panels also reportedly are in short supply, in spite of plants running seven-day a week, 24-hour schedules. However, prices of petroleum fuels continue to drop.

TENTH DISTRICT - KANSAS CITY

Overview. The pace of economic expansion in the Tenth District remains strong. Holiday retail sales increased from a year earlier and manufacturers continue to operate at high levels of capacity. Construction of multifamily residential buildings has offset slower single-family homebuilding. Agricultural bankers report improvement in the condition of their crop loans but a deterioration in the condition of their livestock loans. Tightness in markets for skilled labor has eased, and there is little evidence of upward pressure on wages. Retail prices have remained stable, while materials prices have increased in both the manufacturing and construction sectors.

Retail Sales. District retailers report that sales improved throughout the month of December and were well ahead of year-ago sales. Despite disappointing sales of outerwear due to unseasonably warm weather, sales of basic lines were strong during the holiday season. Retailers indicate they are satisfied with current inventory levels. Most auto dealers report slightly declining sales over the past month, due primarily to seasonal factors, but expect sales to be strong over the next few months.

Manufacturing. Most firms continue to operate at high levels of capacity. Shortages of skilled labor, however, are much less widespread than at the time of our last Beigebook survey. Manufacturing lead times have increased but are expected to shorten in the second half of 1995. Most respondents plan to trim inventories in the near term.

Energy. Drilling activity in the district fell slightly in December. As a result, the

average number of drilling rigs operating in district states stood somewhat below the year-ago level. Despite lackluster performance overall in the region's energy industry, parts of the district benefited from some firming in natural gas prices near the end of the year.

Housing. Builders report a slight increase in housing starts from both last month and a year ago due to a pickup in construction of multifamily buildings. Most respondents expect building activity to remain stable in the coming months. Sales of new homes increased slightly in some parts of the district over the past month, despite higher home prices. Most builders report materials are available with few delays. Mortgage demand continues to decline with higher interest rates, although most lenders expect demand to level off or increase slightly in the months ahead.

Banking. Loan demand rose last month at most reporting banks. Most banks report higher demand for commercial and industrial loans and for consumer loans. Demand was largely unchanged for home mortgage loans and home equity loans, flat to down for residential construction loans, and up somewhat for commercial real estate loans. Demand for agricultural loans was mixed. Loan-deposit ratios were constant to up from the previous month, while security investments were unchanged.

Most respondents raised their prime rate last month, and almost all expect to raise the rate again in the near term. Consumer lending rates were increased last month, and almost all banks anticipate further increases in the near future. Lending standards were unchanged.

Bank deposits increased slightly last month. NOW accounts, money market deposit

accounts, and large time deposits were up somewhat, while demand deposits and small time deposits were little changed.

Agriculture. Agricultural banks in the district indicate their farm loan portfolios had a mixed performance in 1994. Most crop loans are in better condition than a year ago. Crop yields were up significantly from 1993, more than offsetting lower prices. Nearly all bankers surveyed report weaker livestock loan portfolios, however, due to a slump in hog and cattle prices. Nevertheless, most bankers have been surprised that livestock loans did not fare as poorly as large summer losses had suggested.

The district's winter wheat crop is in good condition, although bankers in some areas are concerned that the 1994-95 winter may be too warm and dry to support a good wheat stand in the spring. District bankers generally expect farm income to improve slightly in 1995. With normal crop yields in 1995, incomes for crop farmers may be nearly equal to those of 1994. Incomes for livestock producers should improve in 1995 as input prices fall and livestock prices return to breakeven levels.

Prices and wages. Retailers report that prices remained stable in December. Manufacturers' purchasing agents report input prices increased in the past month and are higher than a year ago. Fewer agents report tightness in markets for skilled labor than in past months, and none report upward pressure on wages. New home prices rose over the last month. Most builders report that prices of materials have increased, although tightness in the market for construction labor has eased.

ELEVENTH DISTRICT--DALLAS

The Eleventh District economy continued to grow at a solid pace in late November and December. Increasing strength was reported in the service sector, and manufacturing orders continued to rise at a steady rate. Strong commercial construction activity offset a further decline in the single-family sector. Retail sales growth slowed after the Thanksgiving holiday and Christmas sales were lower than expected. Growth in loan demand continued at a strong pace, but competition between banks for customers squeezed margins. District energy activity remained unchanged but was slightly below last year's levels. Year-end agricultural production was up.

Contacts in several manufacturing industries, including petrochemicals, paper and steel, reported price increases resulting from strong demand. Apparel and food contacts said that higher costs--especially for packaging--were raising price pressures in their industries. Service sector respondents reported continued wage and price pressures resulting from labor shortages and strong demand. Retailers said competition kept prices at or below last year's levels. Oil prices held steady, but warm winter weather depressed natural gas prices. Sharp declines in livestock prices led to a decline in a regional index of agricultural prices.

District **manufacturers** reported continued growth in orders with strong growth in the demand for paper products, electronics, apparel and chemicals. Orders increased modestly for construction-related products. Domestic and foreign sales of packaging materials, boxes and paper products continued to rise. Prices were up for all types of paper products and contacts expected further price increases in 1995. Despite additional capacity, electronics orders outpaced supply leading to lower inventories. Electronics prices were reported as no longer falling, resulting in higher profits for manufacturers. A December surge in orders for jeans led to hiring in apparel

manufacturing. Demand for construction-related products edged up. Lumber producers reported lower sales of residential lumber but increased orders from commercial builders. Demand for concrete and cement increased with improving weather. Glass sales were at a record high due to rising commercial construction and robust auto production. Orders for primary and fabricated metals accelerated, and producers reported that demand for steel had picked up recently in anticipation of near-term price increases. Food manufacturers reported steady demand and had increased hiring because of strong growth earlier in the year. Petrochemical orders remained extremely strong, and despite added capacity, inventories were low and prices continued to rise. Improved business overseas kept demand for oil and gas machinery steady at high levels, but respondents expressed concern over low domestic natural gas prices. Unseasonably warm weather lowered fuel oil costs, reducing refining margins to record lows. Several refiners said they plan to shut in capacity until margins improve.

Demand for **business services** grew at a slightly faster pace. Legal firms reported a pickup in demand associated with real estate transactions, mergers and acquisitions, and initial public offerings. Growing labor market tightness for experienced accountants increased upper level salaries in the accounting industry. Demand accelerated for temporary placement services. Both trucking and temporary service firms continued to report increasing wage pressures associated with strong demand and a shortage of qualified workers. Demand for business communications and advertising services slowed slightly from their previous fast pace.

Seasonally adjusted, **retail sales** growth slowed slightly after Thanksgiving and many retailers said Christmas sales did not meet expectations. Holiday sales were reported to be strongest for electronics, jewelry, toys and other hard goods. Sales of fragrances, cosmetics and most fashion apparel were less than expected. Heavy discounting and competition kept selling prices unchanged or below a year ago. Stores along the Mexican border said that sales dropped following the peso devaluation and are not expected to pick up for at least 3 to 4 months. Contacts in the auto industry

reported that sales growth had slowed somewhat in December after an extremely strong November. Popular car models were said to be in short supply.

Contacts in the **construction and real estate** industry reported that higher mortgage rates continued to cause a decline in single-family construction. Commercial construction--especially for retail space--remained strong, but contacts voiced uncertainty about the year ahead. Demand for suburban office and retail space remained at high levels, and the apartment market was reported to be tight despite a number of recently completed projects.

Bankers reported that loan demand continued to increase at a strong pace, but said higher interest rates and competition had squeezed margins. Consumer lending remained very competitive, and strong demand for commercial loans had offset the decline in residential mortgage lending activity.

District **energy** producers reported that activity was unchanged. Strong global demand kept oil prices between 17 and 18 dollars per barrel, but warm winter weather pushed natural gas prices below last year's level. The district rig count was slightly below that of a year ago, but drilling activity in the Gulf of Mexico was still at good levels, according to contacts.

Most district **agricultural** producers reported higher production than expected. Livestock conditions were reported to be well above average across the district. Although prices for cotton, wheat, sweet corn and lettuce were higher, lower livestock, corn and soybean prices pushed the Texas All Farm Products Index down 6.2 percent from a year ago.

TWELFTH DISTRICT -- SAN FRANCISCO

Summary

Economic growth in the District as a whole appears to be accelerating slightly, bringing higher rates of resource utilization. Strengthening of activity in Arizona, California, and the Pacific Northwest appears to have been only partly offset by a slight moderation in the fast-growing states of Idaho, Nevada, and Utah. Retail sales during the holiday season were reported to be moderately strong in most of the District. The services sector continues to expand noticeably. Except for aerospace, manufacturing activity generally remains at high levels in most of the District outside California, with a few industries reporting capacity constraints and large price increases. In response to higher interest rates, home sales and construction appear to have dropped back a bit, but business investment continues to pick up. Outside of housing, bank lending activity is reported to be brisk.

Business Sentiment

Twelfth District business leaders generally remain optimistic about the outlook for real activity in the nation and region. Survey respondents expect that over the next four quarters national growth will exceed the long-run historical average pace, the unemployment rate will fall further, and inflation will accelerate slightly. Within the region, growth in most states is expected to exceed the national pace. Among regional spending components, business investment is expected to strengthen further, but housing starts generally are expected to drop back; the main exception is California, where some respondents anticipate a slight improvement in housing construction from relatively weak levels.

Retail Trade and Services

Holiday season retail sales were reported to be moderately strong in most parts of the District and in some areas to be substantially stronger this season relative to weak levels a year earlier. Big-ticket items reportedly sold better than less expensive merchandise; for example, sales of computer peripheral equipment, software, other electronic goods, and automobiles generally were reported to be robust, but lower-end apparel sales were weak, leading to substantial price discounting in many areas. Within California, the relative strength in holiday sales was particularly noticeable in Central and Southern California, where activity last holiday season was at low levels. Retail sales in Idaho and Utah reportedly were boosted by the addition of recent domestic in-migrants to the pool of shoppers in the states, with furniture, housewares, and other items used in new homes said to be particularly strong. Respondents from the border region of Arizona noted that the late-December devaluation of the Mexican peso noticeably inhibited trans-border shopping by Mexican residents, but this devaluation reportedly had less immediate effect on holiday sales in the San Diego area.

The services sector continues to expand moderately, boosted by gains in tourism and business services and less of a drag from restructuring in the health care industry. Hospitals were reported to be more willing to make investment purchases recently. Hotel occupancy rates were reported to be high in most of California and Utah, owing in part to convention activity and a strong start to the ski season. Among business services, software development has been strong, and in tight labor markets--such as in Idaho--wages for computer programmers were reported to be increasing rapidly.

The government sector remains weak, and new concerns about budgetary pressures

have been expressed in some areas. In Oregon, wages of state government employees are scheduled to be cut in mid-1995. In eastern Washington, expectations of a significant reduction in the workforce at the Hanford site this year are dampening the business outlook in that area. In Southern California, respondents expect the Orange County bankruptcy and investment pool losses to result in a combination of local government layoffs, service cuts, infrastructure project delays and cancellations, and higher "user fees."

Manufacturing

Outside of aerospace, manufacturing activity generally remains at high levels in most of the District outside California, with a few industries reporting capacity constraints and large price increases. In the Pacific Northwest, electronics manufacturing industries were reported to be producing at high levels, but growth appears to have slowed somewhat recently. In the pulp and paper industry group, all segments were reported to be tight now, with strong demand and low inventories. Newsprint prices reportedly jumped 20 percent in 1994 and are expected to climb about 25 percent further this year. A major food retailer noted that paper and other packaging costs were increasing and indicated that the increases will have to be passed on to consumers.

Agriculture and Resource-Related Industries

District farmers report generally good conditions but express concern about rising costs of labor, transportation, and raw materials. Crop and cattle grazing conditions generally have been aided by high levels of precipitation; water levels in most parts of California are well above normal so far this winter, and an Arizona rancher reports enough rain to let cattle feed over a wider than usual range. In California, some pressure on wages was reported,

particularly for drivers of trucks containing agricultural products, and transportation costs also have been boosted by an increase in diesel fuel prices. Several agricultural sector respondents noted that chemical, water, and packaging costs are increasing rapidly.

Real Estate and Construction

Homes sales and construction appear to have dropped back a bit in many parts of the District recently. In Central and Southern California, new home construction reportedly weakened, and sales of existing homes were off. In many other areas, housing sale and construction activity typically are at seasonal lows this time of year; changes in activity were less discernible in the thin markets.

Financial Institutions

Bank lending activity is reported brisk, but margins appear to be shrinking in some areas, as pricing has become more competitive. In California, some banks expressed concern about the effects of past lending to businesses that sold products and services to Orange County and uncertainty about the effects of the Mexican peso devaluation. However, this was not expected to slow the improving economic conditions in the state or banking industry substantially, and community banks in Northern California were particularly upbeat. In Utah, banks were reported to be experiencing strong deposit growth and strong demand for consumer and commercial loans.