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CURRENT ECONOMIC COMMENT BY DISTRICT

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by the Staff

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SUMMARY*

Economic activity around the Nation is maintaining its forward momentum according to reports from the twelve Districts. And, the outlook for 1973 ranges from optimistic in several Districts to "almost universally ebullient" in the Seventh District. Orders, inventories, and shipments of manufacturers were reported on the rise, and manufacturing employment is expanding. Retail sales are strong, and the 1972 Christmas season is expected to result in sales well above the 1971 level. Construction activity has generally remained at high levels or expanded further, but signs of weakness in construction were noted by several Districts. With the economy continuing to expand, shortages of labor and materials were noted as emerging problems. Wet weather has curtailed the harvest of several crops and inflicted some losses, but the overall farm income situation remains favorable. Loan demand continues strong at banks, but trends in deposits have varied significantly between Districts.

Manufacturing activity was reported on a noticeable upswing according to survey results reported by the Cleveland, Richmond, and Minneapolis banks. Steel shipments were cited as especially strong in the Cleveland report, and steel economists predicted a record year for steel shipments in 1973. Chicago noted that auto and truck production was at high levels and further gains were expected in 1973. However, in the Philadelphia District, manufacturers reported a lull in their December orders while maintaining an optimistic view about the next six-month period.

*Prepared at the Federal Reserve Bank of Dallas.

The increase in business activity continues to generate expectations of higher levels of capital spending. Several directors of the Boston bank anticipated large increases in capital spending in 1973 because of the approach of production to capacity levels. Atlanta reported that the construction of numerous small plants had been announced recently in the Southeast, and Chicago indicated that auto makers were accelerating their capital spending plans. However, St. Louis reported complaints from businessmen in their District that profit margins were not sufficient in some industries to stimulate plant and equipment spending even though utilization rates were near capacity.

Although construction activity is still characterized as strong in most Districts, there is growing concern about possible overbuilding of multi-family residential units. Cleveland, Boston, New York, San Francisco, and Minneapolis all indicated that apartment and/or condominium construction may be excessive in parts of their Districts. Although several Districts suggested the possibility of a decline in housing activity in 1973, the extent of the possible decline was not large. Builders in the St. Louis District were reported to be optimistic about further gains in construction in 1973, including an increase in single-family housing for the St. Louis metropolitan area. Atlanta reported numerous large-scale construction projects--both residential and nonresidential--in the Southeast, especially in Atlanta and in central Florida.

Retail sales are rising and the outlook for the months ahead is favorable. All of the Districts commenting on retail trade indicate that 1972 Christmas sales should be well ahead of last year. San Francisco and Chicago noted that luxury and "big ticket" items were selling well. And Kansas City reported that the strong auto sales included many of the

more expensive models or models with large amounts of optional equipment. Although reporting retail sales as generally good, Minneapolis indicated that sales of winter recreational vehicles had not been up to the earlier expectations of one manufacturer.

Employment is expanding in most areas and declines in unemployment were mentioned by several Districts. Dallas reported a record level of employment in the Eleventh District states in October as a result of widespread gains. In the Third District, Philadelphia noted that the unemployment rate had fallen from 5.7 to 4.5 percent in the last three months. Atlanta indicated that unemployment rates in several southeastern states were at their lowest levels in years. With the gains in employment, some signs of labor shortages were reported by the Atlanta, St. Louis, Richmond, and Chicago Districts. And Chicago noted that turnover rates and absenteeism were rising at firms in the Seventh District.

The generally favorable agricultural situation has been set back somewhat by wet weather in the Midwest, Southeast, and Southwest that delayed the soybean, sorghum, and cotton harvests. Kansas City indicates that the production of soybeans and sorghum will fall below the November crop report estimate, and Atlanta cited a loss of 30 million bushels of soybeans in Tennessee. The extent of the losses in the Chicago District was uncertain, but it was noted that the overall farm outlook was still the most favorable in many years. Dallas reports that the cotton yield continues to look good, but the delay in harvesting may hurt the quality of the crop. While the wet weather hurt production in most areas, Florida citrus and vegetable growers were aided by the moisture.

Loan demand was reported to be generally strong by Dallas, Kansas City, and Richmond. Consumer instalment loans and mortgage loans were mentioned as areas of strength by bankers in the Cleveland and Philadelphia Districts. The trend of bank deposits varied considerably among the Districts. Cleveland reported a strong rise in deposits while Kansas City and Philadelphia indicated that deposits were largely unchanged. Bankers in the Kansas City District are trying to attract additional deposits by offering higher rates on CD's than currently prevail in the New York market. Banks are apparently not experiencing a shortage of funds, and Cleveland reports that most banks in the Fourth District are highly liquid.

FIRST DISTRICT - BOSTON

Our business directors reported business conditions as very strong. Improvements in machinery and aerospace orders were noted, while orders in the consumer durables area were variously termed as "steadily improving" to "fantastic." Some directors felt that the Price Commission's profit margin rules would begin to pinch profits in the second half of 1973, while others noted current problems.

A raw material supplier to the tire industry noted that business was excellent, with record sales and orders in November. There is some apprehension, however, that retailers are overstocking tires so that the high level of manufacturers' sales now may be borrowing from future sales. A high orders backlog was noted by a manufacturer of superalloys who also reported that commercial aircraft engine orders were finally getting back to respectable levels. These are replacement engines for the 727 and 747 planes. A manufacturer of general aviation aircraft also noted strong orders. Machine tool orders were also reported as finally really turning up.

Several directors expected large increases in capital spending in 1973. Two directors noted that in a number of lines, production had already reached capacity levels, although one director of a large conglomerate stated that most of his lines still had slack.

A bank director whose bank does the payroll for a number of firms in the Boston SMSA reported no increase in employment in November from August levels, although payrolls rose 18 percent from the previous month's level. Obviously, firms are still relying heavily on overtime rather than new hiring.

A New Hampshire banker reports a slowing in both savings and demand deposit growth. Apartment building remains strong, and the demand for mortgages almost exceeds the bank's ability to make the loans. Mortgage rates are up one-fourth percent, but other rates have been steady.

All our directors were asked to comment on the effects of the Price Commission's profit margin guidelines. One director said that the recent change in the way of calculating costs (allowing the inclusion of interest on long-term debt and adjustments for divested companies) meant that the guidelines would not affect his firm in 1973. Another director noted that the guidelines had caused some inequities. For example, a large consumer paper goods producer whose costs had risen substantially could not raise its prices because another large, diversified consumer goods producer, which also is a major supplier of consumer paper products, could not raise its prices because the latter company had hit its profit margin ceiling. Thus, the first company's profits were being squeezed. This director noted he is aware that this kind of problem is occurring in a number of firms. Two directors stated that they had recently raised prices in a number of lines and, therefore, did not expect any profit squeeze in the first half of 1973.

Two of our academic correspondents this month, Professors Samuelson and Wallich, stressed that a "well-behaved, speedy" expansion has occurred with inventory accumulation still "held in reserve" and showing signs of coming to life. Professor Wallich felt the wholesale price figures confirm an increasing rate of inflation; the behavior of the deflator, he argued, was in part a statistical quirk due to devaluation. Preferring a more lengthy expansion to speed at this stage,

Samuelson favored moving toward restraint. Specifically, he would like to see a gentle rise in the Federal funds rate--130 basis points over the next year--and would not be upset by a 4-percent rate of monetary growth even if it brought a substantially faster rise over the next month or two.

Professor Eckstein disagreed with this viewpoint, arguing that an increase in banks reserves at an annual rate of at least 6 percent is of critical importance. Unless the Federal Reserve accommodates the expansion that much, "all bets are off" on the prevailing handsome forecasts, as well as the hope of holding the bill rate under 5.55 percent and the Aaa utility rate under 8.0 percent during 1973. The only serious danger of excess in the current outlook is in housing, where rationality may be destroyed by the tax shelter feature in apartment building. The bottlenecks which have been experienced are mainly a by-product of the housing boom and are not surprising for this stage in an expansion. There is still no prospect of a general excess demand for labor. Eckstein was dubious about the projected amount of overwithholding refunds as well as the stimulative impact of the refunds on consumer spending.

All three criticized attempts to hold interest rates down administratively. Eckstein felt it would lead to demands for more rigid interest rate controls and for capital allocation. Wallich argued it would result in serious distortions, in particular by forcing borrowing outside the banking system. This would be institutionally damaging and could weaken the Fed's ability to control the situation. He felt the political trade-off could be better achieved by an increase in the corporate income tax rate. To Samuelson, the key is to gain the cooperation

of labor leaders who, he suspected, are more concerned with profits than with the prime rate. He did not feel there would be serious distortions in the short run but suggested the problem will not disappear after the spring round of labor negotiations since any restraint on the part of labor would probably be contingent on the continuation of profit-price controls.

SECOND DISTRICT - NEW YORK

Reports from our directors and other business leaders recently contacted indicate that economic activity remains very strong. Respondents cited the high and improving degree of business confidence and described the outlook for 1973 in generally favorable terms.

Most respondents characterized retail sales as very good now that the holiday season is underway. The chairman of the board of a Rochester department store, who earlier had been somewhat skeptical about consumer spending, said that Christmas sales were likely to outpace last year's showing by a wide margin, and this view seemed to be generally shared. A director of the Buffalo branch attributed the buoyancy of consumer spending to the expectation of a Vietnam settlement, increased personal income, the removal of election uncertainties, and the stability accompanying wage-price controls.

The economic outlook for 1973 was described as favorable by all respondents although the degree of optimism varied. In the view of most directors, production, sales, and employment are expected to show further advances. One director felt that the growth in output and employment would be almost as rapid as the gains experienced this year. Several respondents said that production is likely to outpace sales because of the need to rebuild inventories. On the other hand, a director associated with the metals industry commented that inventory accumulation by the metals-using industries was being held down by the continued presence of considerable excess capacity and a weak price outlook. A director of the Buffalo branch, who is a senior official of a large upstate manufacturer, suggested that unemployment will average about 5 percent for 1973 as a whole.

He added that wage increases might moderate a bit but that advances in prices will probably be about the same as in 1972.

In this connection, almost all of the respondents were agreed that wage-price controls would remain necessary next year. A bank chairman said the program should be maintained for at least a while longer, although he felt that it should not become a permanent feature of the economy. Another director said that the program, at least in some form, should be continued for another 9 to 12 months. Only one director, associated with the metals industry, expressed reservations about the program. He said that the metals industry favors eliminating the controls and noted that fluctuations in uncontrolled raw materials prices combined with controls on the prices of final products had resulted in distortions and inefficiencies in overall pricing.

All of the directors detected a high and improving degree of business confidence in the economic situation, but the current state of confidence was described in terms that fell short of exuberance. Changes in inventory spending were variously described as minimal to robust. One director said that inventory controls were still very tight, while another in the automobile parts business said that inventory spending is increasing sharply as a result of a tightening supply situation and slower deliveries. Several respondents noted that there was some progress in implementing capital spending programs which earlier had been slowed down or held in abeyance pending clarification of the overall economic outlook.

The chairman of a large New York bank said there are signs of serious overbuilding of apartments in some parts of the country and was concerned about the proliferation and credit status of real estate investment trusts and land development companies. He suggested that these

enterprises may represent the one significant weakness in our overall credit structure. Another director thought that overbuilding would become a national problem if housing starts remained at their high 1972 level. However, he expected a reduction in housing starts of about 10 percent during 1973 because of shortages of building materials and reduced availability of mortgage money and felt that this would prevent overbuilding from becoming a general problem.

THIRD DISTRICT - PHILADELPHIA

The outlook is still optimistic in the Third District; approximately 65 percent of the respondents to this Bank's monthly business outlook survey report expectations of increased business activity during the next six months. However, some area businessmen do expect a temporary lull in production between now and Christmas. Current employment opportunities are unchanged, but the longer-run outlook is better. Over 40 percent of the responding firms are planning to increase their investments in inventory and plant and equipment during the next six months. Home construction continues at a high level. Most banks' deposits are flat while their consumer, small business, and mortgage loans continue to expand. On the darker side, inflationary expectations are on the rise.

Some lull in production for December is showing up in the responses from businessmen polled in the Third District. Three times as many firms report increases as decreases in their new orders and shipments for November. But, for December, the decreases in planned production slightly exceed the increases. The longer-run outlook still remains bright, however, as over half the area businessmen report plans for increased production during the six months ahead.

Over 85 percent of the respondents to the Third District's business outlook survey report no change in the number of persons they employed or the length of their average employee's workweek during November.

During the next six months, over half the firms still report no change in their employment plans, but, one-third of them do report plans to increase the number of persons in their work force. The

unemployment rate in the Third District has just fallen to 4.5 percent from 5.7 percent three months ago.

Only a few more firms report increased inventories for November than report decreases, with the majority having no change. Looking six months into the future, however, 40 percent of the firms report plans to increase their inventory investment. Similarly, over 40 percent report plans to increase investment in plants and equipment during the next six months.

Home construction activity in the Third District is continuing strong at the high levels of past months with very large increases occurring in the Atlantic City area. Nonresidential construction is flat. Public works construction in the Third District is off substantially. However, total construction is still rising.

Area bankers report that demand deposits are flat. Time deposits are increasing slowly at some banks. Small business, consumer, and mortgage loans continue to be in strong demand, but few large national corporations are increasing their borrowings at this time.

Not one respondent to this month's outlook survey reports experiencing any decrease in the prices he pays or the prices he receives. On the six-month horizon, over half the firms expect to pay higher prices and over one-third expect to receive higher prices.

FOURTH DISTRICT - CLEVELAND

The pace of business activity in the District has become noticeably stronger in recent months, and some signs of tightening in resource utilization are apparent. Improvement in the manufacturing sector continues to be robust. Gains in retail sales have been sizable, and banks are experiencing heavy demand for consumer loans, especially for auto financing. Most of the large banks are highly liquid, reflecting large deposit flows, and consumer and mortgage loan demand remains strong. Business loan demand seems to be following a normal seasonal pattern but is short of expectations.

The recent behavior of the insured unemployment rate provides some indication of the increasing tightness in labor markets in the District. The insured unemployment rate has declined to about 2 percent in recent months from a high of more than 4 percent that was reached in late 1971. (The prerecession low was 1 percent.) Gains in nonfarm payroll employment have been sizable since midsummer, and the improvement in manufacturing employment has been more pronounced in the District than in the Nation.

Preliminary results of our latest survey of District manufacturers indicate that the pace of industrial activity in this area is becoming particularly strong. For the month of November, our composite diffusion index of eight key items rose to the highest level since early 1966. (The composite diffusion index conforms closely to the national index of leading indicators before trend adjustment.) Responding firms reported substantial gains in new orders, shipments, and backlogs during November but only limited strength in inventory accumulation. Extensions in

delivery times were reported by an increasing percentage of firms in the survey. Employment and the workweek rose sharply last month. The diffusion index for prices paid, which had remained in the 60 percent area between February and October, jumped to 67 percent last month. Firms responding expect a continuation of the strong upward pace in December in all survey items except inventories.

Economists from major steel companies in the District report that shipments will be somewhat stronger than usual in December. Some customers are placing orders now to beat the price increases, effective after the first of January, on selected products. (Bethlehem Steel announced they will not change steel sheet and strip prices until April 1.) Current orders for steel plates and structural steel are showing a seasonal increase, reflecting a pickup in machinery production. Steel orders from consumer goods producers are still very strong. One major area of weakness in the steel industry stems from the railroad industry. Despite the shortage of freight cars, the railroads have been unwilling to make commitments for new freight cars because of the possibility for Government subsidies. (Congress had considered such legislation.) The steel industry economists are projecting 1973 shipments of 96 million tons or better, a gain of 5 percent from this year. (The steel industry's previous record year was 95 million tons in 1969.)

On the financial side, bankers throughout the District emphasized the continuing strength in mortgage loans, with little sign of slackening thus far. A few reports, however, suggest that bankers expect some slackening in residential construction in 1973. One banker said the condominium market in Cleveland seems to be saturated; another noted that apartment

overbuilding is a problem in Columbus; and a third banker mentioned overbuilding of HUD units in Pittsburgh. (In addition, he spoke of natural gas shortages limiting homebuilding in that area late next year.)

The observed strength of retail sales is also reflected in heavy demand for consumer credit, according to banks contacted. As yet, none of the banks are experiencing any abnormal delinquency problems, however. According to respondents of some of the largest banks in the District, business loans have been growing about in line with normal seasonal patterns, but somewhat below expectations. Loans for capital spending and inventory accumulation have fallen short of expected paths, in part reflecting the huge cash flow of many businesses. Major banks in Pittsburgh, Cleveland, and Cincinnati reported they are in highly liquid or comfortably liquid positions and that they plan to participate heavily in the forthcoming Treasury financings.

Demand, time, and savings deposit flows have been very strong in major centers. One exception, however, is western Ohio, where deposit flows were described as moderate. Farmers in that area have sustained extensive financial losses because extremely bad weather ruined a significant share of corn and soybean crops.

FIFTH DISTRICT - RICHMOND

Fifth District business conditions continue to improve, according to the results of our most recent survey of businessmen and bankers. Manufacturing shipments, backlogs, and new orders continue to reflect the strength evident in recent months. The retail sales picture is bright with better than seasonal increases being reported. Further increases in employment and hours worked per week were reported, with labor shortages restricting the output of some firms. Widespread increases in wages and prices received were reported. Businessmen and bankers in the District remain optimistic about the prospects for business during the next several months.

District manufacturers report that shipments, new orders, and backlogs continued the strong upward momentum recorded last month. Increases in these indicators of business activity were reported by approximately 40 percent of all manufacturing respondents. While the increases appeared to be fairly general, strength was especially evident among textile and apparel producers. Boxcar shortages continue to plague some District manufacturers, and furniture production is reportedly being restricted by a shortage of both skilled and unskilled labor. More than one-half of the manufacturing respondents indicated a decline in inventory levels, but inventories relative to desired levels were reported to be about right by most respondents. Over the last several months, a growing number of manufacturing firms have reported that current plant and equipment capacity is at lower than desired levels.

Employment expansion continues and more firms report a shortage of both skilled and unskilled labor. Both manufacturers and trade and

service respondents show increases in employment and hours worked per week. On balance, bankers report increases in employment in their areas. Both manufacturers and retailers report that wages and prices received have increased during the last month.

The retail sales picture in the District remains bright. More than 50 percent of the bankers surveyed indicated that general retail and automobile sales have increased since the last reporting period. Contacts with regular survey respondents, directors and other businessmen, in the District suggest that department store sales are strong.

In general, loan demand increased at responding banks in the past month. Increases were reported for business, mortgage, and consumer loans, with more than 50 percent of the banking respondents showing an increase in consumer loans. Banks also report continued strength in the construction sector, with nonresidential activity being at a somewhat higher level than residential activity.

District farmers' total cash receipts from farm marketings during the first nine months of 1972 were 10 percent above those in the same period last year, with gains of 14 percent in crop receipts and 7 percent in receipts from livestock. Record high prices averaging 10 percent above a year earlier highlighted the 1972 flue-cured tobacco marketing season. Volume of marketings was 5 percent smaller, however, so value of sales increased only 5 percent.

Optimism concerning the economic outlook remains high among District businessmen and bankers. More than two-thirds of the banking respondents expect an improvement in business activity in their areas in the immediate future.

SIXTH DISTRICT - ATLANTA

Economic activity continues to surge, according to reports of businessmen and bankers. The outlook is optimistic, but the exuberance of the expansion is causing some bottlenecks and is exerting inflationary pressures. A number of large residential and commercial construction projects have been announced. The pace of new plant announcements has accelerated. Labor shortages are reported in some areas.

Residential construction continues strong. A \$100 million planned development has been announced for an area south of Atlanta. This development will include industrial sites, apartments, single-family homes, and retail areas. A 216-unit condominium development also will be built south of Atlanta. A \$70 million planned community is to be built on the Gulf in north Florida. Home building continues at a hectic pace in central Florida. A 4,000-unit development has been announced for an area near Orlando. This is the sixth major planned unit development under way in central Florida. A shortage of apartments is reported in the Orlando area. In the Birmingham area, however, there is evidence that home building will soon begin to taper off, but 1973 is still expected to be a good year for housing there.

The outlook for commercial construction is also strong. A \$100 million, 2,034 room hotel has been announced for the downtown Atlanta area. This is the fifth major hotel announced for downtown Atlanta in the past year. A \$47 million complex has been announced for an area in north Atlanta. It will include a 29-story office tower, a motel, and apartments. In the Tampa area, a major retail firm is planning a distribution center and an insurance company will build an office complex. A 21-story hotel has been announced for the Orlando area. A new 18-store

shopping center is to be built in the Huntsville area.

A group of ten oil companies plans to build a \$500 million superport near New Orleans. Western electric will build a material management center near Montgomery, Alabama. There has been a rash of announcements of relatively small plants in the last month. Most of these plants are in the textile and apparel industry, but they also include plants for processing wood, fabricating metals, and producing auto emission control equipment.

Retail sales are reported strong throughout the Southeast, and merchants are unanimously optimistic about the Christmas season.

A shortage of labor is reported in much of Florida. In parts of that state, the unemployment rate is less than 2 percent. A bank in the Jacksonville area reports difficulty in finding qualified help. An apparel plant to employ 500 will be built near Pensacola, provided a labor survey indicates that adequate labor can be found. The citrus industry is worried about finding sufficient harvesting labor if the projected huge crop materializes. In areas of Tennessee, Louisiana, and Mississippi, unemployment rates are at the lowest levels in many years. Delta Airlines is adding about 400 employees in the Miami area to handle increased traffic. However, 600 employees will be out of work in south Georgia because a poultry processing plant has gone into bankruptcy. Two hundred and ninety employees are being laid off at an unprofitable apparel plant south of Atlanta. A laboratory in Oak Ridge, Tennessee, is laying off 200 employees.

Land speculation in central Florida is reported to be at its highest level since 1929. In the Ocala area, borrowers with little or

no equity are applying for loans to speculate in real estate. The hectic pace of construction in central Florida is producing delays, shortages, and cost increases. For example, sewer pipe is reported in tight supply. Nevertheless, a pipe producer in central Florida has been unable to go ahead with a plant expansion because of the inability to obtain sufficient natural gas commitments. Attempts to line up alternative sources of energy have proved unsuccessful. Prices of homes in the Orlando area are reportedly inflating rapidly. A director from that area says that homes that a few years ago sold for \$30,000 are now selling for between \$50,000 and \$60,000.

Wet weather has continued to hamper soybean harvesting. It is estimated that 30 million bushels have been lost in Tennessee. The wet weather has been a boom to the citrus industry and to vegetable growers and cattlemen in central Florida.

SEVENTH DISTRICT - CHICAGO

The economic outlook in the Seventh District, as indicated by views of lenders, manufacturers, retailers, and farmers, is almost universally ebullient. The last residuals of recession psychology appear to be evaporating. Expectations of further substantial gains in activity in 1973 are very widely held. Margins of unused resources of facilities and manpower are shrinking, and many industries are operating at effective capacity. Inventories are uncomfortably low in both hard and soft goods lines. Residential construction is the only major sector that appears likely to show a decline in 1973, and overall, such a decline may be small in total. The extent of crop losses because of adverse weather remains uncertain.

Fourth quarter retail sales are heading for a record by a wide margin. Purchases of luxury goods and big ticket items are especially strong, and customers are using credit freely. In some cases, low inventories are impeding sales.

Hiring is increasing at all levels including managers, professionals, and manual workers--both skilled and unskilled. Staffing second and third shifts and filling dirty or hard jobs are more difficult. Among the trained workers in short supply are accountants, experienced engineers, welders, pipefitters, and machinists. Employers report higher labor turnover rates and increased absenteeism.

With ample evidence of a substantial improvement in the job market, the problems of central cities continue to increase with high levels of joblessness (not necessarily "unemployment" as defined) and growing welfare rolls.

Producers of both cars and trucks expect gains in output in 1973 from record levels in 1972. Long waiting lists exist for various models of cars and trucks. Plans for capital expenditures are being accelerated by motor vehicle companies.

Other industries operating at virtual capacity are foundries, forge shops, bearings and other parts and components, lumber, gypsum board, color television, furniture, recreational vehicles, petroleum refining, paper, some basic chemicals, machine tools, and important types of construction machinery. Some plants have been taken out of production in recent years, and some operations have been scaled down for one or more of the following reasons: cost cutting, consolidation of operations, pollution standards, OSHA rulings, and foreign competition.

Shortages, or incipient shortages, are reducing the desire of some companies to compete actively for new business or take on new accounts. Some are shifting production to the "top of the line."

Prospects for a substantial rise in total capital expenditures in 1973, including manufacturing buildings, appear excellent. Consulting firms that specialize in product development and long-range planning report sharp increases in new business in the past month or two, after a long dry spell.

Shortages of natural gas and fuel oil are developing in the face of a very cold winter thus far. Local experts view the petroleum outlook very seriously and are predicting rapidly growing dependence on foreign sources with a large adverse impact on the balance of payments and the domestic price level. Reports of the enormous LNG deal with Russia are viewed skeptically.

Because of pressure to keep production moving, some producers complain that quality control problems have increased. At the same time, warranty coverage is being extended, and consumer-oriented legislation is highlighting the need to avoid defects.

Accountants are disturbed by the steps some business firms are taking to avoid reporting profit margins in excess of the guidelines. These practices are said to resemble those that developed when excess profits taxes were in effect.

The extent of losses of corn and soybeans caused by adverse weather is still uncertain. Muddy ground is now frozen hard, but recent snows have impeded harvests. Nevertheless, actual losses may yet be quite small overall. Even if a substantial shortfall occurs, the total effect on farm income may not be adverse because of higher prices. About three-fourths of the Russian-bound grain is not yet shipped from U.S. ports. Attempts will be made to move the grain before export subsidies expire next May. In general, the atmosphere in farm areas is the most prosperous in many years.

EIGHTH DISTRICT - ST. LOUIS

Businessmen in the Eighth Federal Reserve District remain optimistic, foreseeing a vigorous business expansion in the year ahead. Representative firms report sales increased in recent weeks for all lines of output. Manufacturing continues to expand. Construction activity is currently at a high level and is expected to rise still further next year. Employment continues to rise moderately, and a tighter labor situation is reported over an increasing portion of the District. Profits have increased, but some businessmen complain that profit margins are insufficient to stimulate new investment despite near capacity utilization levels. Loan demand continues up, and further increases in interest rates are anticipated. Excessive rain in late October and November has led to a deterioration of agricultural conditions.

Rising retail sales are reported throughout the District with the exception of the inner-city stores in St. Louis. Major department stores report sizable sales gains in November on a seasonally adjusted basis and expect the higher levels to be maintained through the Christmas shopping season. Communities not represented by the major firms report that retail sales are booming. Inner-city stores in St. Louis, however, report little change in sales volume, and chains with downtown stores report that their sales growth is in suburban stores.

Manufacturing activity continues to expand on a broad front. Major chemical companies expanded output and deliveries in the fourth quarter. Orders for plastics, fibers, carpets, chemicals, and appliances are up. Sales of electrical equipment for new plants are rising. An increasing number of manufacturing firms report overtime work, and

delivery dates are lagging further for products in short supply. Brick plants in northeast Mississippi are not promising delivery on current orders of brick until May.

Employment continues to rise, further tightening the labor markets in most District communities. Most manufacturing firms report an increase in production workers despite major efforts to hold employment in check. Labor shortages are reported in many of the smaller and some larger communities in the District, and the unemployment rate is generally low. St. Louis, Evansville, and Fort Smith are exceptions and have shown little improvement in recent months.

Business profits have generally increased with the sharp sales gains, but complaints are made that profits are still too low to provide incentive for major investment expansion in some industries. Specific examples include the box board industry and the lumber and wood industries.

Construction remains at a high level, and businessmen in the industry are quite optimistic about the outlook for construction in 1973. Reports from Arkansas and Tennessee show a continued high level of housing starts during the autumn months with prospects for no slowdown next year. The St. Louis Home Builders Association estimates a 10-percent increase in construction of single-family units next year. One exception to this optimistic outlook is the Louisville area where an excessive number of apartments have apparently been built, and the apartment rental market is reported to be soft. Also, commercial construction in the St. Louis area remains at a relatively low level.

Demand for credit continues to expand, and interest rates continue to creep up for most types of loans. Home mortgage rates, however,

remain relatively stable, and one of the larger savings and loan associations in St. Louis reported a slight decline in its rates in November.

Agricultural prospects in the Eighth District deteriorated sharply in November. Excessive rainfall delayed the harvesting of all crops including corn, soybeans, and cotton. In some areas half of the crops remain in the field, and the damage to soybeans and cotton is quite severe. Crop prices are relatively high, but weather damage may cause severe losses to farmers in some communities.

NINTH DISTRICT - MINNEAPOLIS

The general outlook for manufacturing and retailing in the District appears bright, but some slowdown is anticipated in construction activity. Sizable manufacturing sales gains are foreseen in the fourth quarter and the first half of 1973; District manufacturers, however, have yet to encounter capacity constraints and are generally experiencing no difficulty procuring needed workers and supplies. District retailers are enjoying a good Christmas season. Construction is not very encouraging in the Minneapolis/St. Paul metropolitan area, but both residential and nonresidential building appears to be flourishing in the remainder of the District.

Results of our fourth quarter industrial expectations survey predict continued expansion in District manufacturing activity. District manufacturers reported sales up 12.7 percent from a year earlier in the third quarter and estimated comparable gains in the fourth. They also anticipate 11.0-percent increases in both the first and second quarters of 1973.

This optimistic outlook can be attributed to the District's durable goods industries. After increasing 15.0 percent in the third quarter, sales of durable goods are expected to be up 17.9 percent from a year ago in the fourth quarter and then advance 14.0 and 11.2 percent in the first and second quarters, respectively. These sales gains will occur primarily in the electric and nonelectric machinery, primary and fabricated metals, and lumber and wood products industries.

Nondurable goods sales, meanwhile, advanced 11.3 percent in the third quarter and are anticipated to increase 7.4 percent in the next two quarters, followed by a 10.8-percent gain in the second quarter of 1973.

Although strong sales gains have been reported by District manufacturers, bank directors revealed that District manufacturers are generally not bumping up against capacity limits or having difficulty hiring workers or obtaining needed supplies. According to one Wisconsin director, for example, a large manufacturer in his community is expanding facilities but anticipates no difficulty adding 100 people to the work force. Several directors did report, however, that skilled labor is becoming harder to employ. And, one Twin Cities manufacturer stated that delivery times are lengthening on some items.

Also according to bank directors' reports, District retailers generally are having a very good Christmas season. One major Minneapolis/St. Paul area retailer reported that Christmas spending so far has been very good; he expects his Christmas business to be up 10 percent or more from a year ago. One director indicated that not only are his area's retailers optimistic about Christmas business but several also anticipate business to be quite good in January. A major Minnesota producer of winter recreational vehicles, however, reports that sales have not been up to earlier expectations.

Construction activity will probably slacken in the Minneapolis/St. Paul metropolitan area during the first six months of 1973 but continue quite strong in the rest of the District. According to a Minneapolis/St. Paul area banker, housing sales in the Twin Cities metropolitan area have virtually stopped, and large developers are curtailing activities until the market improves.

In addition, apartment vacancy rates are quite high in this area, and little apartment construction is anticipated there in 1973. In other parts of the District, however, several directors reported quite

favorable outlooks for residential construction. This optimism was dampened only slightly by a South Dakota director who indicated that new home prices in his area have recently risen 10 percent.

The prospects for nonresidential construction in the Minneapolis/St. Paul metropolitan area are not very bright either; the area already has a surplus of office and warehouse space. But directors outside this Twin Cities region reported a number of nonresidential construction projects. Efforts to meet pollution control standards, for example, are spurring construction activity in northeastern Minnesota. And, although some consider it too early to assess revenue sharing's impact, several directors believe those funds will stimulate public construction in their areas.

A director associated with the construction industry foresees no pickup in District highway construction during the first six months of 1973. Looking ahead in another direction, however, this director feels that the Administration's allotted funds for sewage treatment plant construction will significantly bolster this type of construction, if spent, although only 45 percent of the funds authorized are to be used in fiscal years 1973 and 1974. Local governments so far have received very little funding from the Environmental Protection Agency.

TENTH DISTRICT - KANSAS CITY

Weather conditions in the Tenth District are adversely affecting the agricultural harvest, and according to major retailers contacted in a number of large metropolitan areas in the District, slowing down Christmas shopping traffic as well. Despite this slowdown, however, sales are described as good, particularly for hard goods, and, retailers are quite optimistic for sales prospects over the Christmas season as a whole. This strength in the retail area extends into new car sales, and the more expensive models or options are reported to be in strong demand. The strength of retail activity is reflected in Tenth District banks, where several bankers noted improved consumer attitudes toward installment buying. In fact, demand in all major loan categories is still reported as strong, and, in the face of either flat or declining demand deposit figures in November among larger Tenth District banks, a more aggressive seeking for funds has emerged. Negotiable CD growth appears to have picked up, with several District banks paying from one-eighth to one-half a percentage point more than the going New York rates.

Adverse weather conditions over a wide area of mid-America have greatly slowed the harvest of soybeans and feed grains this fall. At last report, considerable acreage remains standing as heavy rains and snow have turned the fields into a quagmire of mud. Temperatures within the District have recently dropped below the freezing point, and many farmers are now able to move through the fields with less difficulty. However, field losses appear to be heavy--particularly for soybeans and grain sorghum. Consequently, final production levels likely will fall considerably short of the estimates released in the November crop report

coupled with reports about additional grain sales abroad. These developments have led to sharp price advances in the grain markets. In the period ahead, prices likely will remain sensitive to new rumors--pro and con--until the harvest is completed.

Bad weather also is blamed for slowing down Christmas shoppers, but major department stores throughout the District still expect strong finishes to a year of good business. Since Thanksgiving, snow and extreme cold have cut traffic in many stores, although a few report that their sales paces are above last year at this time. Managers report little difficulty in finding extra clerks for the holiday season, nor do they complain generally of problems with suppliers. For the year to date, sales of hard goods have been especially good, notably major appliances and furniture. Without exception, store managers expect strong sales into 1973, although one thinks the first quarter of 1972 will be hard to beat.

New car delivery times, for all of the big three, have doubled in major District cities. Sales are as good as or substantially better than last year. Buyers seem more flush. They have more to put down, and if they don't buy the top of the line, they buy a lot of options. Most dealers expect next year's sales to top this year's.

After recording moderate to sizable gains in demand deposits during September and October, the larger banks in the Tenth District reported flat or declining demand deposit figures for November. Interbank deposits were the weakest category, showing a significant decline--perhaps, as a result of the change in Regulation J--but all categories apparently were sluggish. In contrast, negotiable CD growth seems to have picked up. Several District banks are paying from one-eighth to one-half percentage point more than the going New York rates, with an

individual bank's CD inflow reportedly depending on how large a premium it is willing to pay relative to those of local competitors. A few banks expected to add slightly to their CD's after the issuance of revenue sharing checks.

Demand is reported still strong in all major loan categories. Local commercial customers and consumer instalment borrowers (auto paper and credit cards, in particular) were the most frequently mentioned sources of loan demand. Several bankers said that they had been conducting campaigns aimed at increasing instalment loans and noted that consumer attitudes toward instalment buying had improved since earlier this year. Most agreed that the strength of retail activity was probably the major factor. One respondent reported that term loans have been accounting for much of the strength in the bank's lending activity.

Fears of disintermediation were rare among District bankers contacted. However, all respondents felt that somewhat higher lending rates would be justified either now or in the near future.

ELEVENTH DISTRICT - DALLAS

The latest indicators of economic activity in the Eleventh Federal Reserve District were mixed. While total employment, department store sales, and new automobile registrations were all higher, construction activity slowed and the Texas industrial production index edged downward. The rate of growth of total bank credit also slowed slightly in November. A recent survey of business economists in District states, however, revealed them to be quite optimistic about economic conditions in 1973.

Our respondents generally expected economic activity in 1973 to be higher for both the Nation and their states. They were particularly optimistic about the prospects for consumer spending and plant and equipment investment. They also felt that residential construction, both nationally and within their states, would continue strong.

In line with this general optimism, the majority of our respondents expected employment gains in 1973. Most expected growth in employment to be greater in the District than in the Nation. Employment advances were anticipated to be particularly strong in the service industries. Manufacturing and state-local governments were also mentioned as sectors where employment growth was expected to be more rapid. Despite the outlook for rising employment, less than half saw the unemployment rate declining significantly.

The majority of our respondents foresaw continued improvement in corporate profits in 1973. There was also general agreement that wage-price controls would be continued, at least in some form, after April. In fact, over half the respondents felt that controls would be continued into 1974.

Despite the fact that wage and price controls were viewed as continuing, there was almost unanimous agreement that consumer prices would be rising at a higher rate in 1973 than in 1972. Those responding were also in agreement that the deficit for fiscal 1973 would be greater than the Administration's estimate of \$25 billion.

The seasonally adjusted Texas industrial production index eased slightly in October after rising sharply in September. Small increases in the indexes for manufacturing and mining were more than offset by a sharp decline in the index for utilities. Expanding durable goods production enabled manufacturing to post a small gain despite a slowdown in the nondurable sector, notably, petroleum refining. Within the durable goods sector, significant increases were recorded by the transportation equipment and fabricated metal products industries. Mining also edged higher as increased production of natural gas and natural gas liquids outweighed a decrease in crude oil production. The sharp decline in the index for utilities was due primarily to the decreased output of the electric utility sector, probably reflecting a larger than seasonal decline in air conditioning usage.

Harvest of a good cotton crop has been delayed by cold, wet weather across the District in recent weeks. Some loss in quality of cotton is expected but yield prospects continue mostly good. Otherwise, agricultural conditions remain optimistic for a year of record production and incomes.

Regulatory agencies in District states continue to allow maximum oil production. State regulators continue to closely monitor producing conditions, however, and several fields in Texas have had production restricted for conservation reasons. The Texas Railroad Commission has

also held hearings to determine state priorities for natural gas in case rationing should become necessary.

Construction activity in the District states, as measured by the value of contracts awarded, declined in October for the second consecutive month. All major types of construction experienced award decreases, but the largest decline occurred in nonbuilding construction.

Both the manufacturing and nonmanufacturing sectors recorded gains in employment in October and helped to push total employment in the District states to a record level. Still, the unemployment rate remained at 4.4 percent--the same as in September. All major employment categories reported gains except mining. Increases were the largest in the construction, durable goods, trade, and service industries.

Sales of department stores in the District continued to advance in November. Among major metropolitan areas in Texas, sales were strongest in Dallas and Houston. But San Antonio and El Paso also experienced modest gains. New automobile registrations in the four major metropolitan areas of Texas increased in October.

The rate of growth of total loans at weekly reporting banks in the District accelerated sharply in November. Reductions in bank security holdings, however, held the rate of increase in total bank credit to a somewhat slower rate than in October. Time and savings deposits also rose sharply in November due primarily to a large increase in large negotiable CD's outstanding.

TWELFTH DISTRICT - SAN FRANCISCO

In the opinion of our directors, economic activity in the Twelfth District remains strong. Consumer retail spending is expected to reach record levels during December. With the possible exception of construction, most other sectors are maintaining a steady rate of expansion.

Retail sales are reported to be running at 8 to 12 percent above last year's level throughout the District. In some cases, gains of 15 percent are mentioned. The demand for consumer goods is broadly based, but it is strongest in such lines as sporting goods, bicycles, and home furnishings. Some of our respondents also think that there is a tendency to buy higher-priced lines and to upgrade in terms of quality.

A similar situation exists for automobiles. Sales are generally good throughout the District. In a few cases, demand for imported cars is described as weak, but in other areas foreign car dealers are experiencing good sales. The principal problem for domestic car dealers is obtaining deliveries from the manufacturers, and, as a result, low inventories are preventing sales from reaching even higher levels. Dealers expect this strong demand to be maintained into next year.

Construction activity is continuing to hold up, but there are more signs of weakness. Multiple unit construction is falling off because of overbuilding in many areas, but single-family construction and commercial projects are keeping overall demand steady. For example, in Seattle, construction has started on the first large downtown department store in thirty years. Current rates of construction may not be maintained, however, and one large California bank has forecast a 25-percent decrease in the state's building activity in 1973.

In California, recent court decisions requiring environmental impact studies on large projects and the passage of a constitutional amendment in November imposing controls on use of coastal areas are causing some uncertainty. A few banks are reported to be restricting construction loan funding on affected projects until the legal picture is clarified. But at the moment, even in California, construction overall is still showing considerable strength.

The timber industry is showing no signs of any slackening in activity. Lumber prices are higher, and mills in Oregon and Washington are working full time. According to one director, the demand for timber will be maintained in the coming year because of the need to build up inventories which presently are very low.

Good crops and prices are expected in most agricultural areas of the District. Fall planting has been completed, and the crop prospects for wheat are excellent. Beef prices are holding steady, although the existing levels may not cover the costs for some feedlot operations. As a result of record crops and prices in 1972, farmers are making heavy purchases of new equipment and adding to strong retail demand.

District banks report that demand for loans to support inventories is quite strong, but as yet there are no signs of a general jump in consumer installment credit demand. Some banks report record increases but others have experienced no major increase. Several bankers suggest current spending is being financed by heavier reliance upon past savings than upon credit. On the other hand, many purchases are being made through bank credit cards and the effects on credit demand will not be fully apparent until January when customers decide upon the proportion of their balances to repay.