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CURRENT ECONOMIC CONDITIONS BY DISTRICT

Prepared for the
Federal Open Market Committee
by the Staff

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SUMMARY*

This month's Red Book reports suggest that economic activity is continuing to expand, but that the upward impetus is narrowly based. The most optimistic sector is retail trade, where Christmas sales as well as automobile sales in several Districts were stronger than expected. However, only a modest recovery in inventory spending is anticipated as retailers maintain tight inventory control and as some durable manufacturers continue to trim excessive stocks. Caution characterizes the capital spending outlook, with weakness expected in some sizable industries. Led by activity in the single-family area, construction is generally expected to continue its modest rate of recovery. Although most respondents did not foresee any near-term acceleration in inflation, some concern was expressed over construction costs and the outcome of the heavier bargaining calendar in 1976. One favorable aspect of the price outlook comes from the agricultural sector where there are generally expected to be increased supplies of pork and beef. Loan demand at commercial banks is generally expected to remain sluggish.

Strong gains in consumer spending were reported throughout the twelve Districts. Sales far exceeded expectations in several districts including New York, Atlanta, Chicago, Minneapolis, and Dallas. Very strong sales were reported even in some areas in the Boston and Cleveland districts where high unemployment was expected to have adverse effects on consumer buying. Some reluctance toward the purchase of "big-ticket" items was reported in New York and Richmond, but Philadelphia, Cleveland, and Minneapolis all reported increases in this category. Auto sales were surprisingly strong in Atlanta, Chicago, St. Louis, Minneapolis, and San Francisco, while tourism was thriving in both the Atlanta and the Minneapolis Districts.

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*Prepared by the Federal Reserve Bank of New York.

While the brisk pace of retail activity has significantly pared stocks, some progress remains to be made in trimming manufacturing inventories. For example, respondents from the Atlanta, Boston, and Chicago Districts reported that Christmas sales were so strong that stocks are now fairly low. However, retailers and purchasing managers in the Minneapolis and Kansas City Districts foresaw fears of overstocking as motivating tight inventory control policies. At the manufacturing level, respondents in the Philadelphia and Richmond Districts noted that durable manufacturing inventory liquidation had yet to be completed. Purchasing agents from the Kansas City District suggested that the rather modest outlook for inflation for most products precluded much in the way of speculative buildups. In view of these considerations, the typical outlook was for only a moderate first-half upturn in inventory spending.

A large measure of caution seems to surround the prospects for a recovery in capital spending in 1976. For example, respondents in the New York and Chicago Districts among others did not foresee more than a modest recovery until at least the second half of the year. One of the problems emphasized in the Dallas and Cleveland Districts was the considerable proportion of capital expenditures represented by pollution abatement requirements in the petroleum refining and steel industries. In the energy sector, Dallas respondents report that fixed investment in the drilling area remains strong. However, investment in petroleum refining is expected to be below last year's level reflecting, in part, refiners' expectations that higher petroleum costs will result in a long-term flattening out in demand for many refinery products. In the San Francisco District another sizable area of concern was the aircraft industry where a decline in new orders for commercial jets has prompted a significant cutback in plant and equipment expenditures for 1976.

Construction and real estate activity remain generally depressed, although there were a few signs of strengthening. Atlanta and Minneapolis both report continued sluggishness in new residential construction but increased interest in the existing housing stock. San Francisco reports that the anticipated improvement in residential construction has not yet materialized. St. Louis presents a somewhat brighter picture, reporting a strengthening in single-family dwellings as well as in non-residential construction. Chicago and Dallas also report a continued improvement in residential construction activity. But commercial construction, with few exceptions, is still weak. Also, a large number of condominiums remain vacant in the Atlanta District, and the construction of multi-family dwellings in the St. Louis District is at a virtual standstill. In a number of Districts, however, sizable inflows to thrift institutions and the possibility of mortgage interest rate declines were cited.

Reports from agricultural areas are generally favorable. Richmond, Atlanta, Minneapolis, and Kansas City all expect increases in hog production and pork supplies. Improved conditions for cattle producers are anticipated in the Atlanta District as they are in Minneapolis, Kansas City, and San Francisco. Only the Dallas District is somewhat pessimistic, expecting placements of fed cattle to fall as their prices continue declining. Minneapolis reports cash farm receipts were up from the first half of the year, led by record prices for dairy products. Cash receipts for grain, however, were below 1974 levels.

The widespread remaining slack in manufacturing coupled with the generally expected near-term sluggishness of capital spending and rather modest inventory rebuilding were often mentioned as factors holding down inflation at least over the first half of the year. Nevertheless, the possibility of uncomfortably large price increases in some sectors was recognized by some respondents. For example, a Cleveland director reported sharply rising costs for concrete and lumber, while one of the nation's largest homebuilders expected a 10 percent rise in new home prices in 1976. Respondents in the Cleveland District also reported that the October 1 rise in steel prices appeared to be sticking fairly well, although divergent views were expressed elsewhere on the firmness of the aluminum price increase. Some concern was voiced over the possible price impact of the potential terms of settlements of major wage negotiations in 1976.

A rather broad consensus emerged that loan demand was weak and that no strong near-term recovery was in the offing. A number of respondents cited tighter inventory control policies as a major reason for the prospective sluggishness in loan demand. Reflecting this outlook, bankers in the Philadelphia District expected the prime rate to edge down somewhat further before starting to move up gradually beginning in the second quarter. Bankers from the Boston and San Francisco Districts, among others, emphasized the much increased concern over quality of credit. With respect to bank earnings, these bankers foresaw a weak profit picture for 1976.

FIRST DISTRICT--BOSTON

Directors of the First District are very encouraged by Christmas retail sales. This spending surge has provided essential confirmation that the recovery has not waned. In spite of the lively retailing atmosphere, the prospects for a solid, continuing recovery remain tenuous since most other areas of activity are sluggish. Once again, many directors report postponing dates of expected rebound in their lines of business.

The retailing experience for December is typically described as excellent. Volume at large urban stores rose 12 percent, despite the high unemployment rate and particularly bad weather just before Christmas. Many retail trade associations and bankers comment that the increased volume was not accompanied by a comparable increase in consumer financing throughout the District. Unit volume significantly depleted inventories during the month, and manufacturers reported unusually strong December orders. Retailers are more optimistic than last month; their biggest problem is finding stock for January clearance sales.

Banking directors continue to report no activity in loan demands; all categories are seasonally weak. Banks are beginning to look for business, but they seek quality customers. The workouts are so numerous, and profits have been burned so badly, that loan officers remain very discriminating. One director reports that other banks are beginning to compete actively for his customers' business. Furthermore, banks are competing much more widely to place international loans; spreads are narrowing, and qualified personnel are being hired away from established lenders by banks seeking to expand their activities abroad.

One banking director also reports that increased costs of doing business are leading to reinstituting service charges on individual checking accounts, which comprise 25 percent of demand deposits. Also, thrift institutions' entry into the personal loan market is placing downward pressure on instalment rates. The outlook for bank profits foretells that this source of demand for municipal securities will remain weak into 1977 at least.

The machine tool industry will be worse in 1976 than 1975. Production of tools which require long planning leads is being reduced. Although it is expected that orders for the short-lead tools will recover in the first quarter, overall output will continue to decline for some time.

There is a wide disparity in the policy prescriptions of the Boston Bank's academic advisers. For the first time in eighteen years, Professor Eckstein feels that monetary policy is too easy. Specifically, he opposes lowering the Federal funds rate below 5 percent. Eckstein argues that the major uncertainties of 1975--energy legislation, the New York City financial crisis, the tax cut extension, the reemergence of double-digit inflation--have all been resolved on the side of prosperity. As a result, he is confident that the economy will be strong in 1976 and therefore will not require additional monetary stimulus. He is skeptical about the accuracy of the money stock figures and regards a monetarist approach as a highly risky one in this environment.

Professors Houthakker, Samuelson, Solow, and Tobin feel that monetary policy is overly restrictive. Houthakker and Tobin want the Federal funds rate lowered to 4 percent. Houthakker is worried about the outlook for 1976. Because of lagging money growth, he feels the prospect is for only 8 percent gross national product growth in 1976, with a maximum of 4 1/2 percent real growth. Professor Tobin feels it is disgraceful to settle for a recovery that takes five years to make up the ground lost in one year. He criticizes real growth targets as low as 6 to 7 percent and advocates a target of up to 10 percent in the early stage of the recovery from such a severe recession. There is no evidence, Tobin points out, that so rapid a recovery would ignite inflationary pressures in view of the amount of excess capacity available, according to all possible measures.

Professor Samuelson favors aiming money growth at the top end of the target range and does not fear exceeding that limit over the next few months. He points out that the moderate consensus forecast assumes money growth at the high end of the range or above. Policy should not remain tight under the illusion that it would lessen the settlements reached in the labor contract negotiations this year. Professor Solow feels that 6 percent growth in 1976 is a good prospect but that the major risks are on the down side. He favors short-term money growth targets of 6 to 10 percent and feels that a Federal funds rate below 5 percent would be necessary to achieve that range.

Professor Houthakker was puzzled by the recent weakness of the dollar and still expects it to strengthen in 1976. He argues that domestic policy should have priority in the present circumstances.

SECOND DISTRICT--NEW YORK

The business outlook for 1976 on balance is relatively good, in the views of Second District directors, other business leaders, and financial economists who were contacted recently. Real gross national product (GNP) is expected to grow over the year. The Christmas and post-Christmas retail selling seasons have been successful. While retail sales continue to provide the main prop under the recovery, some respondents expected some reinforcement from the inventory accummulation now underway and, after mid-year, from business capital spending. The outlook for corporate profits was, for the most part, regarded as good.

We recently requested our directors and a number of financial economists for their appraisal of the business outlook for 1976. In varying degrees, the respondents in general were cautiously optimistic. Among others, the president of a large nationwide department store chain expected real GNP to grow by about 5 1/2 percent over the year. He expected consumer spending to continue to provide the principal stimulus during the first half of 1976, and to be reinforced by a pickup in capital spending by mid-year. He felt unemployment would decline throughout the year, but would remain above 7 percent. In his view, barring poor crops, there was hope that the rise in consumer prices could be held in a 5 to 7 percent range. The chairman of a large New York City bank also felt business capital spending might pick up after mid-1976. The Buffalo branch directors generally agreed that the business outlook was reasonably good at this time, with "attractive interest rates" and generally good consumer confidence as factors supporting this favorable outlook. A senior economist at a large New York City bank expected a "good, balanced, and sustainable" expansion this year, with real GNP growing by 5 to 5 1/2 percent. As yet, however, he saw no evidence of any significant pickup in capital spending in real terms. He expected such outlays to rise by 8 to 10 percent in dollar terms, with a token increase in real terms in the last part of the year. This economist also expressed "some worry" over the possible impact on inflation of the potential terms of the settlements of the many wage negotiations coming up in 1976. Another bank economist stated he was cautiously optimistic on 1976, and that the recovery was taking hold and should result in a rate of real growth of 5 to 6 percent, in his view a very reasonable performance under present conditions.

As noted, consumer spending continues to provide the main thrust to the current economic recovery. In this regard, the president of the large chain of retail stores mentioned above reported that the Christmas selling season had been "good to excellent," with sales exceeding expectations, even in New York City where sales have lagged behind the nationwide performance. The chairman of a large New York City department store reported the holiday season had ended on a very strong note, with sales intensifying the closer Christmas approached. Similar observations were made by a number of other New York City retailers. A survey of large New York City department stores revealed that Christmas and post-holiday consumer buying had lifted their December sales to a level 8 percent above December 1974, the largest increase in 16 months. The performance in the suburbs was even better, with sales in the metropolitan area nearly 11 percent over the comparable period of 1974--the biggest increase in 23 months. District sales outside the New York City area were also strong. An upstate banker noted that holiday sales in his area had substantially exceeded expectations. The Buffalo branch directors were in general agreement that the Christmas selling season in Western New York had been good, with sales, in dollar terms, running 8-10 percent above year-earlier levels. These directors, moreover, reported that the holiday season increase in retail buying has been followed by good sales so far in 1976. In their view, however, the mood of consumers appears to be mixed. Consumers have discretionary spending money and seem to show little resistence to spending for recreation, travel, and small-ticket items. Inflation, job insecurity, and economic uncertainties in general, however, tend to be reflected in a more cautious attitude toward the demand for big-ticket items.

Regarding corporate profits, the great majority of the respondents looked for an increase in 1976. Among others, the president of the retail chain stated that the outlook for such profits was "excellent", as productivity was improving dramatically while the volume of sales was rising. Against this background, he expected profits after taxes to gain about 30 percent next year. For the same reasons, one of the bank economists expected profits to rise throughout 1976, also by 30 percent for the year. All of the Buffalo branch directors also expected corporate profits to increase in 1976, in reflection of emphasis on expense control coupled with increased consumer spending. Their estimates, however, ranged from rather modest increases to as high as 25 percent above 1975. Exceptions to the rather optimistic profit outlook were voiced by directors associated with the petroleum and the metal industries, who did not expect these industries to fare well during 1976.

THIRD DISTRICT--PHILADELPHIA

Economic recovery in the Third District has still not developed any consistent strength. The manufacturing sector reports business activity virtually unchanged from last month, while retailers are enjoying brisk sales. Area manufacturers note that new orders are about the same as in December, and there is no measurable expansion or contraction in employment or the average workweek. Prices paid and received in this sector are higher, however, and there is some evidence that the rise in price is picking up. Despite the current sluggishness in business activity, manufacturers are optimistic in their outlook for the next two quarters. Retailers report very good sales, and they expect this to continue in the first quarter. Bankers in the area indicate that deposits are growing at more than a seasonal pace, but loan volume is soft.

Manufacturers responding to this month's business outlook survey report that business conditions are unchanged from last month. This represents a substantial slowdown from the pace of recovery in the regional economy last summer and early fall. In November 42 percent of the respondents reported an improved business climate, but in December this declined to 24 percent. This month only 14 percent of the executives surveyed feel that economic activity is at a higher level, while 66 percent observe no change. New orders are holding steady, with over half of the respondents indicating no change during the last month. Both employment and the length of the average workweek are also the same as last month. At the same time, liquidation of inventories--especially durables--continues, with over a third of those polled reporting fewer stocks on their shelves.

Despite the sluggishness in current activity, manufacturers remain optimistic for the next six months. Three fourths of the businessmen surveyed anticipate expansion. New orders are expected to be higher by July, and net accumulation of inventories is projected. The proportion of respondents looking for higher levels of inventories exceeds those expecting lower levels by 23 percentage points. This "net increase" in the six-month outlook is the largest since the middle of 1973. At the same time, employment is expected to grow as well. More than a third of the respondents plan to add to their work forces, and one fifth expect to lengthen the average workweek. In addition, one out of every three businessmen surveyed plans to increase spending for plant and equipment over the period.

Retailers in the area report that the strong surge experienced in Christmas sales has carried over into this month, and all of the merchants contacted expected it to continue at least through March. Traditional promotions on white goods and furniture are taking place, but all of the merchants contacted agree that the markdowns on many nontraditional lines that took place at this point last year are not necessary this year since sales are stronger and inventories are in better shape. One merchant notes that there is little evidence that shoppers are concentrating on lower priced items. "It's hard to believe, but we have sport shirts priced at $34 and they're selling like hot cakes". Some big-ticket items such as color TVs are also reported to be selling well.

On the inflation front, manufacturers report paying and charging higher prices this month, and the pace of inflation in this sector may be picking up. One half of the manufacturers polled report paying higher prices for their supplies this month, compared with a third noting increases last month. On the output side, 37 percent of those surveyed report receiving higher prices this month, compared with 28 percent in December.

The outlook for the next two quarters is for additional inflation. Almost 90 percent of the respondents expect to be paying more for their supplies over the period, and 60 percent anticipate higher price tags for the products they sell. Retailers report that prices continue to move up but at a moderate pace, and they look for this trend to continue over the next few months.

Area bankers report that loan volume remains sluggish. As one contact put it, "Loan volume is as soft as at any time in 1975". There is general agreement that no big pickup is in the cards through the first half of 1976. One banker expects total loans at his bank to grow about 7 percent this year. Bankers look for short-term interest rates to decline and then start moving up gradually around March. They anticipate a drop in the prime rate to 7 percent or below within the next few weeks before turning back up. The consensus is for this rate to average in the 7.75 to 8 percent range for the year as a whole. None of the bankers contacted foresee any problems in accommodating the expected increase in the demand for credit as the recovery proceeds. There is agreement that uncertainty over the staying power of the recovery is inhibiting many customers from making long-range borrowing commitments at this time. However, one banker reports that some of this uncertainty appears to be dissipating among his bank's corporate customers.

FOURTH DISTRICT--CLEVELAND

Our directors and businessmen in the District are still cautious about prospects for business spending in the year ahead. Steel operations are recovering, and retail sales rose strongly during the Christmas season. Recovery in employment in the District remains weak. Deposit inflows continue strong, while loan demand--especially for business and mortgage loans-- is still weak.

Capital goods producers report conditions are generally soft, although they note some improvement from lows early last year. One director and chief executive officer of an electrical machinery firm expects capital equipment markets will remain sluggish in 1976, and another director reports both capital goods and construction equipment markets are weak. Demand for mining machinery and other energy related equipment is still good. A bearings producer reports their business, which held up relatively well through the recession, has softened because of weaknesses in capital equipment, freight cars, and more recently energy-related markets. Heavy duty truck orders have picked up mildly from depressed levels of last year, but no significant improvement is expected until later this year. Several directors associated with manufacturing firms see little need for speculative buildup of inventories in 1976. A director associated with consumer products reports his inventories are back to normal.

Steel orders and production are recovering from the lows of last quarter. Steel economists expect orders this quarter will be at least 15 percent higher than last quarter.

Hedging against the February 1 increase in the tin plate prices, strengthened demand from auto producers, and a reduced rate of inventory liquidation are among factors that should boost steel operations this quarter.

Last fall's steel price increases are holding well, with only scattered deviations from published prices by some small steel producers. Some steel economists apparently have adjusted their 1976 forecasts downward because of an expected slow recovery in capital goods. High costs of pollution equipment and uncertainty over environmental regulations that affect steel and some of its major customers, such as utilities, are hindering recovery in capital goods industries, according to one economist.

Recovery in manufacturing employment in the District is as about as slow as it was in the early stages of the 1971 recovery. There are still some scattered layoffs in the steel industry, but economists for major steel producers expect a steady but modest pickup in employment this quarter. Layoffs among capital-goods-producing industries appear to have stabilized, but one large producer, lacking orders, furloughed several hundred workers from late December to late January. The bulk of improvement in manufacturing employment has been in the rubber and plastics, glass, metal stamping, and automotive industries.

Retail sales during the Christmas season are described as very strong and best since 1973. Retailers in Youngstown, which has one of the highest unemployment rates in the District, report that the dollar volume of sales was at least 15 percent higher than a year earlier. A director associated with a major retail chain stated a sharp pickup in sales had reduced its inventories, and an economist with a national department store chain reported sales for December were very strong and, in real terms, equal to the December 1973 volume. He noted a pickup for appliances and furniture as well as further improvement in apparel. According to a financial officer with a $500 million discount chain, sales last month were higher than in 1974 but not back to prerecession levels. He commented that major appliances picked up for the first time since the decline late in 1973.

Net deposit inflows into banks and savings and loan associations were strong again in December, while business and mortgage loan demand was generally weak. A large mortgage banker and a production loan officer with one of the nation's largest banks commented that the supply of mortgage funds exceeds demand and that their lending rates are likely to be pared shortly. An officer with a large savings and loan expects mortgage lending to be slow for most of 1976 and also anticipates a reduction in their 8 3/4 percent lending rate in order to attract borrowers. One of the nation's largest builders of houses expects that new starts in the U.S. will rise to about 1.3 million to 1.5 million units in 1976 and that the average price of new houses will be up by about 10 percent from last year. A director reports construction costs, especially for concrete and lumber, have been rising sharply.

FIFTH DISTRICT--RICHMOND

Our January survey of Fifth District business conditions yielded mixed results. Manufacturers' responses indicate little or no change in their level of activity during December, while retailers were unanimous in reporting increased sales. Among manufacturing firms, shipments and new orders were essentially unchanged from the previous month while backlogs of orders were down somewhat. Inventories of both manufacturers and retailers showed little change in December. Inventories at retail have apparently been brought into line with desired levels, while among manufacturers they remain in excess. Prices, including employee compensation, continued to rise across a broad front. The outlook for business during the next six months remains bright, as most respondents expect improvement over that time period. Our directors also noted improvement in the confidence of consumers as well as of businessmen in the District. Bank credit in the Fifth District advanced moderatly in December, with a slight negative movement in loans offset by continued investment in United States Government securities. Gains were posted in both demand and time deposits, and purchases of large certificates of deposit (CDs) showed special strength. District farmers' cash receipts from marketings during January-October 1975 recorded a 3 percent increase over a year earlier, compared with a 3 percent decline nationally.

Of manufacturers responding to our January survey, slightly over 30 percent reported an increase in sales while almost as many reported a decrease. Among individual industries, the increases in shipments were concentrated in textile mill products, apparel, and lumber and wood products. Reductions occurred primarily in chemicals and machinery and equipment. Overall, the volume of new orders looked much the same as shipments, although manufacturers reporting declines slightly outnumbered those reporting increases. Industries showing increases in new orders include primary metals and apparel, while declines were noted in transportation equipment. Overall, machinery and equipment manufacturers showed some decline in new orders, but some firms in this industry reported gains. Backlogs of orders declined somewhat at District manufacturing concerns. Inventories were essentially unchanged, although materials seem to have declined slightly, while finished goods edged upward. One third of our respondents continue to view current inventory levels as excessive.

Responses suggest a slight decline in manufacturing employment, the first since May. Hours worked per week held firm, while employee compensation--in terms of average hourly earnings--rose at nearly one third of the firms responding. Prices paid and received were also up across a broad range. Nearly one third of the manufacturers continue to view current plant and equipment as excessive, but nearly all are satisfied with current expansion plans.

District retailers apparently had a very good Christmas season. One branch director called it "exceptional". All survey respondents reported increased sales in December; one called it the greatest change noted in a number of years. The improvement in total sales has not spread to big-ticket items, however. Retail inventories were unchanged from a month earlier and are now in line with desired levels. Retailers are generally optimistic about the near future, hoping that the recent surge in sales will carry over into 1976.

Commercial and industrial loans at weekly reporting banks declined from November, primarily reflecting seasonal influences such as repayment of loans by retailers. Loans to durable goods manufacturers showed small but steady increases, but these were offset by declines in loans to nondurable goods manufacturers. Business loans in December were 7.7 percent below the year-ago level. Consumer loans recently have advanced at a very gradual rate, while real estate loans here declined. Total investments by weekly reporting banks posted strong gains in December, led by a surge in purchases of Treasury bills and longer maturity Treasury issues. Holdings of municipals fell slightly from November. Total investments in December were 19.5 percent above a year ago, while total assets posted a year-to-year gain of 3.3 percent. Steady gains in time deposits continued during December, and CDs increased by 3.5 percent from the previous month. Demand deposits were 3.2 percent above the year-earlier level. Net purchases of Federal funds by member banks over the first four weeks of December dropped to their lowest level since January 1973. Discount window borrowings by member banks remained at the near zero level reached in November.

In the agricultural sector, a buildup in the inventory of hogs held for breeding purposes and a sizable upturn in intended farrowings during the December 1975-May 1976 period strengthen prospects for larger pork supplies in the second half of 1976. Indications point to a somewhat larger increase in the Fifth District than in the nation.

SIX DISTRICT--ATLANTA

Reports from directors, purchasing agents, and other contacts confirm a brightening in the Southeast's economy. At the year-end, department store and auto sales are strong throughout the Sixth District. Tourism is the most vibrant sector. Construction and real estate activity remain depressed, but various manufacturing industries are experiencing greater strength. Developments in the agricultural sector offer hope for continued moderation of price increases.

Consumer spending is leading the recovery. Department store holiday sales have surpassed expectations. Many merchants reported the finest Christmas season in their experience, including such banner years as 1972 and 1973, although in some areas sales did not equal 1974's. Inventories of many stores were so depleted by the rapid pace of holiday selling that merchandise for post-Christmas sales was scarce. There were no indications of overstocking and several sources report strong reordering of merchandise. The most successful retailers seemed to be those who used active promotions. The proportion of cash sales was reportedly up from 1974.

Auto dealers likewise reported a sharp increase in sales--the best December in years for certain dealerships--and in some areas inventories were depleted. Aggressive promotion was again mentioned as a key element of success, and a high proportion of cash sales were reported. Several lenders expressed disapproval of the trend toward longer maturities on automobile instalment credit contracts.

Tourism remained the most ebullient sector in the Southeast's economy, even exceeding retail sales activity. Record numbers of tourists were reported at Louisiana, Tennessee, and Florida tourist attractions, hotels, and motels. Trailer and camping facilities in southern and central Florida were operating at maximum capacity. In late December, the influx of visitors to Florida caused major traffic congestion as far north as Atlanta. Crowded conditions forced major Florida tourist attractions to close their gates from time to time.

In contrast to tourism, construction and real estate remain depressed, particularly in Florida. The resale of existing single-family residences was the only segment showing significant improvement. New home construction remained in a slump in most areas, and nonresidential construction was generally dormant except for sporadic plant or public sector construction. Scattered reports of gains in residential construction were received, but they were mostly interpreted as evidence of bottoming out. A large overhang of available new residential units persists in Florida. Many major projects remain in financial distress. Some slight reduction of the inventory of houses and condominiums was reported, but the absorption rate is low relative to remaining stock. This is particularly true for condominiums, of which 37,000 units in south Florida remain in stock; 3 percent are sold each month. The vacancy rate is reportedly greatest for expensive units. Various sources indicate that the speculative and second-home market segments have largely evaporated, leaving primary residences as the only source of demand. Experienced construction laborers are migrating from Florida to Louisiana in response to job opportunities.

Demand, prices, and output in various manufacturing industries have improved. A major aluminum producer is maintaining a recent price increase and expects increased production. Demand for forest products, including poles, paper, boxes and lumber, continues to improve. Contrary to the usual seasonal pattern, lumber demand increased steadily from October through December. Increased prices for paper products are being maintained successfully. Wholesale prices for spring and summer apparel merchandise are steady but are expected to rise this fall. Demand is reportedly good for a manufacturer of pleasure boats and a maker of appliance timers. A major railroad company reports the return to service of railroad cars and engines withdrawn to storage in the first half of 1975. A large steel manufacturer reports some growth in orders but expects no sizable increases until late in the year.

Georgia purchasing agents, responding to a survey in November and December, indicate expectations consistent with a continuing slow economic recovery. Higher prices are unanimously anticipated. A large and growing proportion expects no change in delivery times on orders. A large majority plans to keep finished good inventories unchanged, while the proportions expecting larger, the same, or smaller raw material inventories are about equal. The number of respondents expecting lower production has steadily declined, while the proportion looking forward to higher sales and profits has risen. Employment is reported to be essentially stable, while indications of constant or declining order backlogs are evenly balanced. Delivery lead times are evenly divided between thirty days and sixty days.

In the agricultural sector, lower feed costs offer some hope for improved conditions to hard-pressed cattle producers, so that the size of the cattle herd should cease declining. Hog production is described as "the only bright spot in agriculture". Larger supplies of inputs, including fertilizer, fuel, pesticides, and agricultural equipment, should cause a further slackening of price increases. However, the higher minimum wage will exert some upward cost pressure. Food procesing and retailing industries in recent years have been unable to offset rising costs of fuel, labor, machinery, and packaging through productivity increases; in the 1950's and early 1960's, substantial productivity gains helped to limit price increases. One director notes that the average price per ton of sugar cane declined from $47 in 1974 to $15 in 1975 but that this differential has not been felt by the consumer.

SEVENTH DISTRICT--CHICAGO

Although great caution prevails among business executives and lenders in the Seventh District, there is general acceptance of the view that activity will be substantially higher in 1976 than in 1975. The big news of the past several weeks has been the strength of retail buying in the Christmas period and also in the post-Christmas period. Layoffs of workers are at a much reduced rate in virtually all centers, but new hiring is still at a slow pace. Sales of autos and some other hard goods have been better than expected. Steel shipments are expected to improve significantly this quarter. Capital expenditures are likely to remain slow, overall, in the first half. Real estate transactions, mainly on residential properties, have increased substantially in recent months.

Despite widespread uneasiness, virtually all observers appear to accept the view that the general economy will improve throughout 1976, with real gross national product (GNP) up about 6 percent. Various surveys indicate that the expansion is expected to continue at a disappointingly slow pace in the first half with a significant acceleration in the second half. Among the specific recent projections by District business leaders for 1976 are: airline passenger traffic up 6.5 percent, steel shipments up 22 percent, color TV up 20 percent, major appliances up 15 to 20 percent, autos up 10 percent, trucks up 20 percent, and housing starts up 25 percent, all in physical terms. A big boost is expected for recreational vehicles and mobile homes. None of these projections suggest that new record highs will be achieved. Producers of most capital goods are very reluctant to offer specific forecasts.

Gains in Christmas sales over year-ago levels were large and exceeded the expectations of most retailers. In fact, a number of reports suggested that sales would have been even stronger if retailers had not"run out of goods".

The post-Christmas period has not witnessed the heavy markdowns noted last year. Nevertheless, dollar volume apparently has continued at a relatively high level.

New layoffs have been at much lower levels in recent weeks than last year. However, a larger number of plants than usual were shut down for two weeks or so of "vacation" over the holidays to help bring inventories into line. Most employers are very cautious on new hiring. One exception is a major airline, which is actively recruiting new cabin attendants for the first time in three years.

Sales of new autos were larger than expected in December, but there was great variation by model. Some models are virtually out of stock. The 2.1 million car production schedule for the first quarter is said to be "very tentative", with a close rein on shipments from suppliers of components. Motor vehicle employment may rise somewhat further, but unemployment in the manufacturing centers is almost certain to remain very large.

Demand for major appliances and TV sets was below expectations in November and December, but some improvement was reported in recent weeks. Producers are fairly confident of substantial gains in sales in 1976. Inventories are low, especially if sales pick up.

Recreational vehicle (RV) producers enjoyed a surge in orders late in 1975, as dealers decided to start rebuilding depleted inventories. Some of the RV producers who survived the severe "shake-out" of the past two years are now operating at full capacity.

Steel shipments were low in the fourth quarter, partly because of the October 1 price boost and partly because of a reluctance to build inventories before the turn of the year. Orders booked for the first quarter indicate that shipments will rise substantially, especially for lighter steel products.

Capital goods producers report some improvement in orders recently, especially for products that were very depressed last year, such as light construction equipment and materials handling equipment. No general turnaround in capital goods is expected until after midyear. Many firms are re-evaluating capital expenditure programs with an eye to cancellations or delays. Unprofitable operations often have been sold or are slated for sale liquidation. Retail chains have stepped up closing of marginal stores, especially smaller stores in older sections. Auto producers will be ordering a large amount of equipment to make smaller cars in 1976 and in the next several years, but this equipment will be installed, almost entirely, in existing plants.

Real estate circles are encouraged by the continued strong inflow of savings to the savings and loan associations. Loans are more available, and prices of existing residential properties have remained firm. A large title company reports that its title volume (in dollars) returned to the May 1973 level late last year. Business is weakest in the Southeast and strongest on the West Coast.

EIGHTH DISTRICT--ST. LOUIS

The economy continues to expand moderately, according to recent reports from District businessmen. Considerable optimism and confidence about further economic gains in 1976 were expressed, although boom conditions are not expected. Retailers reported a sharp increase in sales during the recent Christmas season from year-ago levels, and most manufacturing firms have experienced improvement in orders. Construction activity has also strengthened in recent months, and prospects for construction in 1976 have improved. Although employment continues to increase and unemployment rates are somewhat below peak levels in 1975, resource use in many industries remains well below capacity levels. Bank loan demand remains sluggish, but demand for mortgage funds at savings and loan associations is reported to be increasing moderately.

Consumer spending has increased significantly in recent weeks. Department store representatives described their sales as very good during the Christmas season. December sales of a wide range of items were generally well above year-earlier levels. Appliance dealers noted improvement in their sales, and automobile sales have continued to improve recently, although a few reports were counter to the general upturn. Despite the generally brighter retail picture during the Christmas season, however, some businessmen are not expecting much strength in consumer durables expenditures this year.

Most manufacturing activity in the District continues upward. Representatives of the steel, chemicals, metal fabrication, wood, shoe, and furniture industries reported improvement in business activity, and most of those interviewed were generally optimistic about prospects for 1976. Aircraft output is also expected to be strong this year on the basis of private and government contracts. In contrast to these reports, a manufacturer of capital equipment reported orders were on the decline, with not much prospect for improvement until the second half of the year. District businessmen indicate that employment has continued to increase in recent weeks. Unemployment rates have moderated from their peaks last year in most parts of the District but remain considerably higher than in previous years. Most firms also reported rising productivity.

Construction industry representatives have recently become more optimistic about prospects for 1976. Single-family home construction has strengthened somewhat, although building activity is in a seasonal decline at the present time. A St. Louis representative of the home-building industry expects a 20 percent increase in construction of single-family units in 1976. On the other hand, construction of multifamily units was virtually at a standstill last year. Government programs aimed at improving this sector are expected to have only a small impact.

Other kinds of construction are also showing expansion. Some projects shelved for the past couple of years, such as shopping centers, hospitals, and industrial plants, are beginning to move forward again according to construction industry representatives. It was noted that with the slack in construction, contractors are generally very competitive and are operating on substantially lower margins than normal.

Financial institutions continue to report rising deposits but only weak to moderate loan demand. Bank loan demand remains sluggish, partially reflecting the reluctance of many businessmen to expand inventories. Savings and loan associations report moderate loan demand, with demand for financing older homes the strongest.

NINTH DISTRICT--MINNEAPOLIS

Year-end economic indicators in the Ninth District remained mixed. Consumer spending advanced, but recovery was not evident in the District's manufacturing sector. Overall employment increased through the second half, but growth in the labor force kept the unemployment rate high. Savings inflows into financial institutions were strong, but business lending was weak and much mortgage lending was being used to finance existing housing. Consumer instalment credit turned up from the low levels of early 1975, and real personal income growth improved as a result of a slowdown in the rate of price increase. Tourist spending was good; auto sales were up sharply from 1974. New residential construction was still sluggish. Cash farm receipts were up from the first half but down from 1974's pace.

Most retailers say that December retail sales were good. Increases over December 1975 reportedly ranged from 10 percent to 35 percent. Many retailers characterized December sales in such terms as "better than expected", or "very good". One said that sales during Christmas week were especially "heavy". Another reported good sales of big-ticket items.

But not all retail lines experienced strong sales. Winter apparel sales lagged until late in the year because of warm weather. Many retailers say that consumers were "value-conscious" and "very practical" in their purchasing decisions. Retail inventories were kept tight through the Christmas season. Even retailers experiencing good sales were hesitant to rebuild inventories; many appeared content to run out of some items rather than risk extensive overstocking.

Consumer spending also appeared strong in the tourist industries, except in winter resort areas with only light snow covers. Montana resorts say that sales of ski lift tickets were good to excellent, and a Minnesota resort says that current-dollar sales were up 10 to 15 percent over last year.

All auto dealers surveyed by this bank reported better sales than in 1974's depressed fourth quarter. Increases ranged from 8 percent to better than 100 percent. Buyers showed renewed interest in both intermediate and full-sized models. Inventories of automobiles on dealer lots were being kept at normal or low levels.

There was little evidence of recovery in the District's manufacturing sector. Manufacturing employment bottomed out in June 1975 and has been virtually flat since then. Nonetheless, survey results indicate that manufacturing sales expectations are improving.

The overall employment picture was somewhat brighter than in the manufacturing sector. Since June, employment has been increasing steadily. Nonetheless, the year-end unemployment rate remained high due to labor force fluctuations.

The construction sector was giving little impetus to the economic recovery. Home-building activity, as measured by new permits issued, failed to sustain earlier strength, and total 1975 permits seemed likely to fall short of even the low 1974 level. Nor was there much activity in nonresidential construction; the only bright spot in the District was accounted for by power and light projects or other public projects.

Gross cash farm marketings held strong throughout the second half following a slow first half. At the year-end, cash receipts were running only slightly below 1974's pace. Livestock receipts were increasing, but cash receipts for grain continued to run below 1974 levels. The record prices being paid farmers for dairy products have bolstered farm incomes in the District. Prices of slaughter hogs and slaughter cattle, though down from midsummer peaks, are still better than last year. Feeder cattle prices remain fairly low, though demand in the fourth quarter picked up somewhat from earlier rates.

As had been true throughout 1975, savings inflows at District banks and savings and loan associations remained substantial in the fourth quarter due in part to high levels of savings in both the consumer and business sectors.

Business lending by commercial banks in the District closed the year on a flat note. Savings and loan associations' mortgage loans made and loan commitments rose sharply during the year, even though new home construction remained depressed. Much new mortgage lending was apparently being made on existing housing; another factor was a higher rate of spending on home improvements.

TENTH DISTRICT--KANSAS CITY

Judging from the responses of bankers and of manufacturers' purchasing agents, little has developed of late in the economy that gives cause for either excitement or concern. Bankers once again report flat loan demand except for seasonal increases. Over the first quarter, they expect real estate loans to weaken, consumer loans to improve moderately, and business loans to change little. They see continued strong consumer saving and moderate business saving. For some responding bankers, this all adds up to further declines in interest rates, although others foresee small increases in the coming months. The word on materials inventories from purchasing managers is "low". Buyers for major manufacturers expect to be able to find materials easily this year at prices pretty near where they are now. With a heavier collective bargaining calendar ahead, the usual preliminaries to negotiations have picked up, but little talk of strikes is heard. In the agricultural sector, the cattle feeding and hog industries are expanding, so that supplies of beef and pork are likely to rise.

Purchasing managers plan to hold down inventories of all materials in the year ahead, reflecting their expectations of plentiful supplies and only modest price increases in 1976. Without exception, buyers are sticking to very tight inventory control policies. A sample of responses: "We are keeping our inventories as low as we possibly can" (luggage, folding furniture); "our inventories are very tight although we expect a great year" (audio and visual tape equipment); and "we dropped our materials inventories way down last year and we will keep them there" (greeting cards). Purchasing agents expect price increases to average between 5 and 6 percent. They see the future trend of petrochemical prices as the big question mark. The prices of textiles, expecially cotton, will rise at double-digit rates, say the agents, and plastics will show sizable gains. But only minor increases are expected in papers and metals. Said one purchasing manager, "Aluminum has just gone up 5 percent, but they may not be able to make that stick". The buyers see no crunches developing in materials, citing "excess capacity" and "soft markets" in most supplies.

The local bargaining calendar, as well as the national, is heavier this year. The contract of a local carpenters' union expires April 1. About 6,000 carpenters in two states are affected. The union spokesmen already have begun jockeying for bargaining position, with statements like "we are now behind with the crafts". Contracts with utility workers are due to be renegotiated later this year, with higher rates a foregone conclusion. The upcoming auto negotiations will affect 10,000 workers at three major plants in the Kansas City area.

Recent reports continue to provide evidence of a strong expansion in the cattle-feeding industry. As of December 1, the seven major feeding states had 25 percent more cattle on feed than a year ago, due largely to a 47 percent increase in November placements. Furthermore, the hog industry apparently has entered the expansion phase. Hog producers recently reported that they plan to increase December-May farrowings by 8 percent above year-ago levels, the first such increase for this six-month period since 1971. These developments signal a return to larger red meat supplies during the second half of 1976. although a likely reduction in nonfeed cattle marketings will temper the increase in beef output. Livestock prices are presently relatively low and may stay that way, but the significant drop in feed costs during the past year should permit producers to expand red meat output at a profit.

Tenth District bankers report little change in loan demand in December. Business loan demand increased seasonally with gains in loans to retailers, agribusinesses, and others. Few bankers expect any marked improvement in business loans in the first quarter of 1976. Consumer loan growth in December was also about seasonal, but signs of a pickup are appearing in loans for autos and other consumer durables. Moderate improvement in consumer loans is expected in the first quarter. Further weakness in real estate loans, however, is anticipated as existing projects near completion.

Bankers expect either further declines or only small increases in market interest rates in coming months. Because of this and their belief that consumer spending will rise only moderately, most expect continued strong inflows of consumer savings. Moderate inflows of business savings are also anticipated. Reflecting these expectations, the bankers contacted are not attempting to lengthen further their CD maturity structures at this time.

ELEVENTH DISTRICT--DALLAS

The year-long recovery in department store sales in the Eleventh District was capped by a big surge in Christmas buying. Most merchants found December sales far exceeded their earlier expectations and, as a result, unit sales were up significantly. Sales statistics were especially robust in Dallas and Houston, where many outlets reported sales revenues were up a fifth or more from a year earlier. In general, stores selling better quality merchandise recorded the biggest sales increases. Retailers also noted cash sales were abnormally high. For example, many stores reported half their sales were in cash, or more than twice the normal share. The current wave of buying is expected to continue into spring, with merchants expressing sales prospects as good to very good. Current inventory levels are generally considered to be adequate in light of current sales forecasts.

Lending activity at District savings and loan associations continues to increase. The volume of mortgage loans rose steadily last year, and loan officers expect continued growth throughout 1976. In addition, several associations recently reported substantial increases in interim construction lending to home builders.

Mortgage lenders see no letup in the strong pace of savings inflows that they have experienced since early 1975. Thus, they expect to be able to accommodate increased loan demand without tightening lending terms. In fact, nearly half of the associations contacted predicted conventional loan rates will drop a quarter of a point by April. A leveling-off in the overall cost of savings also eased the upward pressure on loan rates, as maturing certificates of deposit are being rolled over at substantially lower interest rates. Mortgage lenders expressed optimism that their cost of funds would remain relatively stable throughout the year.

Changes in the petrochemical industry are having diverse effects on capital spending by the District's largest industrial complex. Despite the rollback in domestic oil prices, the drilling boom and heavy demand for oil field equipment should continue in 1976. Manufacturers of this equipment are operating near peak capacity and plan to step up outlays for plant and equipment. Two large equipment producers have announced major plant expansions, while several other firms will modernize existing facilities.

Chemical producers will also continue to invest heavily. Although chemical plants valued at an estimated $3 billion are currently under construction on the Texas Gulf Coast, the strength of the current recovery is expected to strain existing facilities by the year-end. Capacity utilization by the largest chemical firm, for example, is expected to reach 84 percent, up from 72 percent in early 1974. When capacity utilization was above 85 percent in 1973, widespread production bottlenecks occurred.

Investment by refiners, on the other hand, will be below last year's level of spending. As a result of higher costs for petroleum products, particularly gasoline, refiners see a long-term flattening-out in demand for many refinery products, and this has led to the downward revision in future refinery capacity needs. A number of expansion projects announced over the past few years have been canceled. Moreover, a sizable share of this year's outlays are for pollution-abatement equipment rather than for expanding production facilities.

Although steel manufacturers are planning large capital outlays in 1976, most spending will be to comply with EPA guidelines, rather than for much needed improvements in production facilities. The District's largest producer, for example, will not spend anything for "productive purposes" this year but will continue to spend $1 million a month for pollution-control equipment. A Fort Worth mill scrapped plans for a new furnace but will lay out $3 million for pollution-abatement equipment.

A recent severe cold snap forced natural gas utilities to cut off supplies to low-priority industrial users throughout a wide area of the Southwest. Gas supplies to high-priority customers, such as residential and commercial users, were largely unaffected, although schools were forced to close in one large service area. Almost all of the industrial plants affected by the cutback in gas service were able to switch to standby energy supplies, and very few facilities opted to shut down their operations temporarily. With a return to more seasonable temperatures, full gas service was restored to all customers.

Placements of calves in Southwestern feedlots were up nearly 50 percent in late 1975 over the level of the year before. But bankers engaged in financing cattle feeders expect placements to fall throughout the first half of 1976, because feed cattle prices have continued to edge downward since mid-1975. In the past, declining prices would have only a modest effect on placements, since many feeders would speculate that prices might improve while their calves were on feed. But following the turbulent developments in the industry during the past two years, cattle feeders and their bankers are much more cautious. A shortage of feeders' calves is also expected to hold down future placements. Fall and winter grazing has been extremely limited, forcing ranchers to market or slaughter calves earlier than normal and thus laying the foundation for the future shortage.

TWELFTH DISTRICT--SAN FRANCISCO

In the opinion of our directors, the recovery is proceeding unevenly, with caution still the common attitude. Even though the strong burst of holiday consumer spending was in line with sales expectations, the pickup in new orders has been slow, especially for forest products and transportation equipment. A brighter pace of activity is reported in the food-processing, chemicals, steel, and petroleum industries. Agriculture is doing well, with lower feed costs reversing the profit picture for calf-cattle operators. Twelfth District banks have recently experienced good business loan demand in the fields of energy, utilities, agriculture, and consumer finance.

Retail sales rose to all-time highs in many areas over the holidays. Demand for new automobiles was exceptionally strong, and the market is expected to remain active. One large food chain reported that it ran short of inventory last month. Cautious inventory policy continues to hold sway, however, as retailers attempt to assess consumer sentiment.

On the industry level, inventories are reported to be back to normal rates except for wood pulp where a large overhang remains. Demand for forest products as a whole bottomed out in April-May 1975 and is now showing slow improvement as it responds to orders from the construction industry. Another area of concern is the manufacture of aircraft. A director from Boeing Co. reports that his company laid off some 8,000 people last year, despite the fact that it sold over half the share of market on commercial jets, 75 percent of which were sold overseas. A decline in new orders for commercial jets has prompted a significant cutback in plant and equipment expenditures for 1976. On the other hand, business is expanding at satisfactory rates in the food processing, chemicals, steel, and petroleum industries, although all express concern over rising costs. Demand for aluminum is increasing at a modest rate, and a director reports that aluminum shipments in 1976 are expected to be 30 percent higher than in 1975. The same director anticipates plant and equipment expansion of 25 percent this year. Copper demand, however, remains in the doldrums.

The construction industry appears to be looking forward to another slow year. In southern California, expenditures are expected to be off 5 to 10 percent from 1975. Although improvement in residential construction has been anticipated, there have as yet been no signs of a pickup. Costs of materials, however, are steadily on the rise. In Orange County, California, the average home sale price increased to $55,950 by the end of 1975, up $5,120 from the first quarter of that year.

For agriculture, the 1976 outlook has improved because of cheaper feed. The cow-calf operators are on a break-even level. Some profit is being shown in feeder cattle, and feedlot operators have picked up a substantial part of their last two years' loss. There is great demand for farm land-development money which is used for clearing land, irrigation water, sprinkler systems, and operating expense.

Overall loan demand by business has held steady over the past two months, as increased cash flow lowered borrowing requirements or resort was made to the commercial paper market and because of cautious inventory policy. Consumer and mortgage loans are increasing in number and size. Special areas of recent strength in business loan demand would include energy, utility, agricultural and consumer finance industries, whereas general manufacturing and other industries, particularly transportation, have continued static or have shown recent weakness.

Concerning banking as an industry, a director from the West's largest bank predicts that 1976 will probably be the worst year from a profit standpoint since the depression. There is speculation as to just how many banks will have to cut dividends. Price-earnings ratios will stay down, making if difficult for banks to access the equity market. The slower growth pattern envisaged for the economy as a whole should help the industry in working out its problems. However, this director cautions against backing away from loans. He favors greater emphasis on determining the quality of the loan and pricing it according to its risk.