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SUMMARY*

Overview

Strength in retail sales continues to be a major factor contributing to economic growth in most parts of the country. Still, for a few isolated regions--the mining areas of northern Minnesota and Michigan, the State of Oregon, and the energy-dependent areas of the Dallas District--the economic recovery has not yet begun. But in many of the regions that bore the brunt of the 1982 recession--Cleveland, Pittsburgh, St. Louis and upstate New York, for example--the recovery is well established.

The 1983 Christmas season looks to be the best for retailers since 1978. In manufacturing the reports are of across-the-board improvement, while real estate sales and construction activity appear to be suffering little more than seasonal slowdowns in some areas and are quite strong in others. On the financial side, business loan demand at banks has been sluggish, reflecting the strong cash position of many firms. Agriculture, however, remains a troubled sector.

Retail Sales

With striking uniformity the twelve Federal Reserve Districts report very strong growth in retail sales. Apparel, home

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*Prepared at the Federal Reserve Bank of New York.

furnishings, and home appliances are most frequently mentioned as the fastest moving items, and automobile sales continue to increase. In Boston and Dallas retail sales are so strong that many stores report especially tight inventories. Only Chicago and Kansas City report a somewhat mixed picture, with the former noting a few areas of weakness and the latter mentioning a general slowdown in sales growth over the past three months.

Despite the continued marked improvement in sales, retailers continue to be cautious. Chicago and San Francisco indicate that retailers have been slow to expand inventories, and only Philadelphia reports much optimism about rapid growth continuing into next spring.

Manufacturing and Employment

Manufacturing activity continues to expand: orders are up, backlogs are increasing, and many firms are implementing capital acquisition plans. Capital spending, however, still appears to be mostly aimed at productivity improvements rather than capacity expansion. Several districts report particularly high levels of activity in the pulp and paper and aluminum products industries. Defense orders have started increasing again in St. Louis, and Cleveland indicates that plants manufacturing flat rolled steel products are now operating at close to capacity.

The capital goods industry is beginning to pick up in New York and Dallas, but continues to lag the recovery. One of Chicago's informants indicated the level of activity in the machine tool industry remains at only about 50 percent of a "good" year. San Francisco and Cleveland report that manufacturers, like retailers, remain quite cautious about accumulating inventory.

The expansion in industry continues to lead to lower unemployment rates nationwide. However, the labor markets in Chicago and parts of New York are still weak, with both employment and unemployment lower than at this time last year.

Real Estate and Construction

Conditions in the real estate market differ somewhat across districts, but sales and construction activity appear to be strong in more places than they are weak. In New York, St. Louis, Dallas and Atlanta levels of activity remain high, especially in the commercial sector, although analysts in Dallas expect a slowdown before long.

Finance

Commercial and industrial loan demand has been sluggish in recent months, and most districts attribute this to strong cash positions in the business sector. Only Cleveland reports a general increase in loan demand, while San Francisco notes an increase in such lending but only by smaller banks. Bankers in the Philadelphia District expect business lending to pick up in the spring as corporations use up their cash and begin to finance plant expansion and inventory accumulation.

Consumer lending is strong in most districts, but the picture is mixed with respect to mortgage lending. Richmond reports that the recent stabilization of mortgage interest rates has led to some increase in demand. Cleveland, however, is still experiencing a slowdown in lending attributable to the earlier rise in mortgage rates.

Agriculture

The PIK program has added to the 1983 incomes of farmers, but not all farmers are out of trouble. Atlanta, Minneapolis and Dallas report that increases in feed prices have narrowed margins on livestock operations.

FIRST DISTRICT - BOSTON

The recovery is gaining in strength and broadening in the First District. Retailers report healthy sales gains in recent months and an optimistic outlook for the critical holiday selling season. Inventories are at planned levels or perhaps a little higher. Manufacturers are also experiencing order increases and are looking forward to a good 1984. The demand for capital goods remains weak overall but signs of an upturn are increasing. In construction, the number of multi-unit housing permits authorized continues to fluctuate sharply from month to month. Permits for single unit housing are holding up despite increases in mortgage rates. Most state governments in New England experienced difficulty balancing their budget in FY83 and increased a variety of smaller taxes. As a group, the six states will move from a small revenue shortfall in FY83 to a small surplus in FY84.

Retail

Merchants in the First District report that recent sales growth has been strong. The results were generally better than expected, although one department store came in slightly below its "very ambitious" plan. Growth occurred across the board, but lines cited as especially strong included telephones, electronics, toys, domestics, and energy-saving do-it-yourself products. Two chains had more growth in Rhode Island than elsewhere in the region, probably because the recession more seriously dampened last year's performance in the state.

Local newspapers recently reported concern among retailers that some products would not be available toward the end of the Christmas season. However, the department stores contacted said they were not worried about product availability (except for widely-expected shortages of Cabbage Patch dolls) In this light, inventories slightly above plan were seen as a positive development. A building goods specialty house, whose business is not at all Christmas-related, also reported satisfactory inventory levels.

In spite of a slow start because of bad weather the day after Thanksgiving, the Christmas season is expected to be very good. One merchant said consumers are "getting back into the swing of buying" now that the uncertainty and instability of the recession appear to be behind.

Manufacturers

Manufacturers in the First District report increasing activity. Areas that were strong before continue to do well - defense, consumer goods, housing-related products, consumable supplies and components. The demand for capital goods is still weak overall, but signs that an upturn is near are increasing. Some capital goods manufacturers have seen substantial order increases in recent months; most report more requests for quotations. The emphasis in capital spending is on modernization and productivity enhancement rather than expansion. Most firms are hiring, but a few are still cutting back. Those being hired are direct labor, sales people and engineers. No one plans to increase indirect and support staff.

All the firms contacted are optimistic about 1984 - even firms that have seen little pickup to date. However, one machine tool representative noted that 1985 would also have to be good for the firm to experience a real recovery, and several in this same industry said that foreign competitors have made permanent gains in market share. Much of the optimism about next year is based on the expectation that the auto industry will make some very serious capital commitments. Materials prices are expected to increase only modestly with the exception of some metals (aluminum, brass, zinc) and possibly pulp.

Construction

The number of housing permits authorized in New England declined in September. Most of the decrease was in multi-unit permits, which have fluctuated considerably during the past year. Single unit permits fell only slightly and remain at approximately the same high level as in the spring before mortgage rates increased. The effective rate on regular 25 year mortgages in New England averaged just above 14 percent in September, compared to just below 14 percent in mid-summer. A building materials specialty house reported sales to contractors have been very strong all year, with 30 to 50 percent year-over-year growth month after month.

State Government Finances

Most of the New England states experienced budget difficulties in FY83; New Hampshire, Vermont and Connecticut ended the year with deficits. All states have based FY84 budgets on projections of a moderate economic recovery. Most have increased combinations of corporate, cigarette, gasoline and alcohol taxes. Rhode Island increased its personal income tax. Massachusetts is stepping up the enforcement of tax collections. For all six states together, total state revenues are projected to increase 8 1/2 percent, expenditures 7 percent, and the region will move from a small overall deficit to a small surplus.

Banking

The rush to interstate banking continues. Bank of Boston, the largest bank in Massachusetts and the New England region has agreed to acquire Rhode Island's third largest bank. This plus other recent acquisition agreements will give Bank of Boston a presence in five of the six New England states.

SECOND DISTRICT--NEW YORK

Introduction

The pace of the recovery seems to be picking up a bit in the Second District. Consumer spending is strong, and retailers say that early indications point to a good holiday season. Manufacturing activity continues to expand at a moderate pace, and observers of the upstate economy feel that the worst is finally over. Homebuilders are working at capacity, and have become more optimistic about the outlook for next year. Office construction remains strong and leasing activity continues to grow in much of the District. Spending on infrastructure should be substantial in the months ahead since voters in New York and New Jersey recently approved the issuance of $1.4 billion of transportation bonds. On the financial side, consumer borrowing strengthened somewhat, in part due to stronger demand for auto loans.

Consumer Spending

Retail spending improved further in late October and November and the gains at District stores were broadly based. Several chains, running the gamut from high-income to discount stores, reported double-digit increases over the comparable period a year ago. The sharpest improvement occurred in an upstate chain which had been doing poorly most of the year. Sales at most stores were reported at planned levels or even higher, with only one respondent noting a weaker than expected increase. Furniture and various kinds of apparel were mentioned as products in strong demand. Inventories were generally reported at satisfactory levels, increasing only in line with sales. However, one chain mentioned problems in keeping up with demand for a few hot items. Most District retailers anticipate that this Christmas season will be stronger than last year's. Consumers have begun their buying earlier, and sales for the first few days of the season have been quite encouraging.

Construction and Real Estate

Residential construction remains strong throughout the District, aided by unseasonably mild weather. However, shortages of skilled labor and some materials continue to delay building activity in New York City suburban areas. Homebuilders remain booked through the spring and the outlook for next summer is generally improving. Customer traffic has been heavy and increasingly composed of serious buyers. Nevertheless, a few builders, fearing higher interest rates, are concerned about possible reduced demand in the months ahead.

The nonresidential real estate market remains active and has shown further improvement. New leasing commitments are being made around the District at a rapid pace. Manhattan is particularly strong, and as a result, confidence is now growing in the ability of this market to absorb the new office space currently under construction. However, some concern has developed about possible overbuilding in parts of New Jersey and Connecticut.

The State governments of New York and New Jersey have received voter approval for increased borrowing for infrastructure renewal. In November's elections a total for the two states of $1.4 billion was authorized for extensive upgrading of roads, bridges and public transportation.

Business Activity

A further moderate expansion in District manufacturing activity occurred during recent weeks. The automotive sector continues strong with some firms, which had been using their existing workforce overtime, now reporting sufficient demand to allow new hiring. Capital goods manufacturers have also begun to show some improvement. Several have now returned to full workweeks after months of operating on shortened schedules. In addition, spending for plant and equipment is underway or planned by various industries such as computers, medical equipment, and health and beauty products.

Some upstate areas that were particularly hard hit by the recession now report a much more optimistic outlook and a feeling that the worst is over. In Buffalo, for example, the latest survey of purchasing managers showed the highest percentages reporting increased new orders and employment in several years.

Unemployment rates in most District labor market areas are generally below their levels of a year ago. However, while employment has been increasing in recent months, it still remains well below year-ago levels in several areas.

Financial Developments

Consumer borrowing has strengthened somewhat in the region. Discussions with bank representatives in the Second District indicate that most institutions are becoming more aggressive in the consumer loan market by reducing rates and increasing advertising. The demand for auto loans, in particular, has been up sharply because of bank promotions, termination of auto finance company incentives, and introduction of new car models. Some banks also report increased issuance of bank credit cards and higher outstanding balances on these accounts.

In line with the national trend, District banks have been stressing adjustable rate mortgages (ARMs). About half of new mortgages are ARMs, and several institutions report that all their new mortgages are adjustable rate. However, portfolios still remain heavily weighted with fixed rate instruments. The spread between interest rates on fixed rate and adjustable rate contracts is currently at about 2 percentage points. This spread has narrowed only slightly in recent months.

THIRD DISTRICT - PHILADELPHIA

Third District contacts report that the regional economy has posted mixed gains in November. Local manufacturing continues to expand despite some downward seasonal pressure, and retailers report yet another strong month in November. The financial picture has been mixed; commercial loan demand remains disappointingly weak, while retail lending continues to make significant advances. In housing, contacts report that continued high mortgage rates are resulting in a dip in November sales.

The outlook for the Third District economy is for continued expansion into the Spring. Manufacturers expect to make significant capital investments and retailers anticipate very strong sales over the next six months. Bankers are forecasting a long awaited pickup in C&I loan activity.

Real Estate and Construction

Third District housing activity, except for that in downtown Philadelphia, has decreased slightly in November from October levels. Although business remains ahead of the depressed levels of a year ago, most contacts report spotty or declining sales over the last six weeks. The most often cited explanation for recent poor sales performance is that higher mortgage interest rates, and uncertainty over future rates, are keeping all but the most pressured buyers out of the market. New starts are also very slow this month, owing to both declining sales and seasonal conditions.

Manufacturing

Although seasonal factors had a damping effect on area industry this month, responses to the most recent Business Outlook Survey still indicate that local factories continued to post gains. About 40 percent of the executives surveyed report improved conditions in November while only 6 percent indicate a decline. New orders and shipments have shown widespread growth, and unfilled orders and delivery times have advanced slightly as well. Inventories, led by a significant buildup in durables, appear to have leveled off from a two-year decline. Employment also has also improved in November, and both payrolls and the length of the average workweek have been increased.

Despite the continued strength of the expansion, respondents have tempered their outlooks somewhat this month. While 62 percent of the executives polled predict that the recovery will continue into next Spring, November's survey records the smallest group of optimists so far this year. Nevertheless, solid increases are still anticipated in both new orders and shipments, and manufacturers expect to hire more workers and to expand working hours between now and April. Additionally, the percentage of respondents planning to increase plant and equipment expenditures over the next six months is the highest it has been in two years. In short, the outlook is for continued growth.

Industrial prices have climbed again this month. Input price increases have been significant in November, but slightly less so than in October, reflecting the mild seasonal easing of producer activity. Prices received for finished goods, on the other hand, have posted more widespread gains this month than last. Looking ahead, 70 percent of the manufacturers surveyed predict higher materials costs in the next six months, while 60 percent expect to receive higher prices for finished goods over the same period.

Retail

Retail sales in the Third District have shown steady improvement over the last six weeks. As contacts had anticipated, year-over-year gains are running about 10 percent in November, and they are expected to maintain that pace throughout the holiday shopping season. "Black Friday" was an exceptionally good day, despite an early snow, with some stores showing increases of 20 percent from a year ago. Higher consumer confidence levels and higher real incomes prompted an early opening of the Christmas shopping season this year, according to contacts, which could well turn out to be the best season since 1978. Retailers report their heaviest sales to be in personal computers and related equipment, entertainment electronics, and home furnishings. Due to a significantly reduced need for promotional activity, profit margins in area stores have risen from October levels.

Merchants remain confident about sales over the next six months and currently are forecasting increases of 8 percent to 9 percent over strong Spring 1983 figures. Accordingly, retailers plan to allow their inventory levels to remain well above those of a year ago. Stores have built up stock over the last six weeks in preparation for the holiday surge, and contacts say inventories will remain 2 percent to 10 percent higher than a year earlier into the Spring.

Financial

Area banks continue to report mixed loan activity in November. Commercial loan volume has risen only slightly in the last six weeks, far below the anticipated level. Once again, many bankers feel that the improved internal cash flow of area companies is weakening loan demand. Reports on year-over-year loan volume vary from 12 percent below to 20 percent above November '82 levels. Although banks are struggling with C&I loans, they are enjoying consistently steady growth in retail lending. Led by the aggressive marketing of credit cards, consumer loan volume currently stands between 5 percent and 13 percent above levels of a year ago.

Third District bankers are optimistic about loan demand for the next six months. They believe that companies will soon exhaust their internal funds and turn to borrowing to support investment in inventories, plant, and equipment. Consumer lending is also expected to be very active through Spring, and bankers plan to continue heavy promotion of retail loans and credit card accounts.

The prime lending rate remains at 11 percent at major banks in the Third District, reflecting what bankers feel is an "air of economic stability." Consequently, contacts foresee little change in interest rates between now and the second quarter of 1984. Some bankers expect short-term rates to ease slightly over the next two or three months, and then to rise again after the first quarter as overall borrowing continues to increase.

Deposit flows in the Third District are reported to be rather sluggish in November. Demand deposits, although fairly volatile in recent weeks, show little net change from October. November's levels range from 2 percent below to 10 percent above those of a year ago. Time deposit growth is flat this month, according to area bankers, but levels remain about 30 percent ahead of November '82.

FOURTH DISTRICT - CLEVELAND

Summary. Economic conditions continue to improve in the Fourth District. Employment is rising and unemployment is falling, but the unemployment rate remains well above the national average. Retail sales gains continue and merchants are optimistic about Christmas sales. Manufacturing activity continues to increase. Steel and capital goods output is increasing slowly. Sales of existing houses continue to be hurt by the level of interest rates and customer confusion about rates, but sales of new houses have improved recently. Commercial banks have become less liquid as deposit growth slowed and loan volume increased sharply.

Labor Market Conditions. Labor market conditions in the District improved further in October, although unemployment remains high and substantially above the national average. The number of unemployed workers fell, cutting the unemployment rate to 10.6% (nsa), which is 2.2 percentage points above the national (nsa) rate. Nevertheless, Ohio's unemployment rate has improved substantially from the 13.2% rate of a year earlier. Unemployment rates in eleven major SMSAs in the Fourth District in September ranged from 8.5% (nsa) in Columbus to 14.5% in Youngstown.

Local indexes of leading indicators for Pittsburgh and Cleveland continue to rise, although less rapidly than earlier in the year, suggesting that further improvement in labor market conditions lies ahead.

Despite the substantial pool of unemployed workers, some smaller firms report evidence of a tightening in markets for some skilled employees--an event which some expect to lead to a quickening in the pace of wage increases over the next year.

Prices, Wages, and Earnings. Real earnings of workers in manufacturing have risen sharply in the last year. Average weekly earnings for production workers in manufacturing increased 11.4% from a year earlier in Cleveland, 11.4% in Pittsburgh, and 9.6% in Cincinnati. The Consumer Price Index for urban wage earners rose only 1.1% from a year earlier in Cleveland, 1.5% in Pittsburgh, and 2.8% in Cincinnati.

Retail Sales. A survey of Fourth District retailers indicates sales gains continued into November, although the pace of domestic new and used car sales showed a normal, seasonal slowdown between October and November. Three major general merchandisers report November sales increases of roughly 9%-13% from year earlier sales, which compares favorably with the national average of 9.4% over the same period. The retailers report a rather broad-based sales improvement, although most hardgoods and apparel items are selling unusually well. New and used car dealers in the District report a moderate sales slowdown from October, which is typical for the season. Of the domestic new-auto retailers reporting, all indicate inventories are within an intended 40 to 50 day range. Import car dealers, however, continue to lose sales because of quota-induced availability problems. Most retailers contacted are optimistic about holiday-season sales prospects.

Manufacturing. Manufacturing activity continues to expand in this District. A survey of purchasing managers in the Cleveland area indicates solid gains in production and new orders in October; no respondent reported declines. Raw materials inventories are being increased and a slight decline in finished goods inventories is attributed to strong shipments. Employment expanded as firms reported callbacks, new hiring, overtime, and shift expansions. Respondents are bullish for the remainder of 1983 and the first half of 1984.

A survey of Cincinnati area purchasing managers reveals production and new orders rose more rapidly in October than in September. Backlogs and employment also rose. Prices paid rose more rapidly in October than in September.

This Bank's survey of Fourth District manufacturers reveals new orders and backlogs increased again in October and are expected to increase in November. Shipments expanded in October but no further gains are expected in November. Inventories are expected to decline in November.

Steel. A major steel firm reports that demand for steel is rising but not rapidly enough to strengthen prices very much. Because of cash flow pressures, steel producers are reluctant to build inventory despite the prospect of rising sales in 1984. The industry is operating at about 60% of reported capacity, up from 25%-30% for many producers last December. Actual operating rates are somewhat higher; one firm estimates actual industry capacity at 143 million tons, instead of the reported 151 million tons. Despite slack in the industry, there are some bottlenecks in finishing capacity, as some mills that produce flat rolled products are operating virtually at capacity.

Capital goods. Capital goods producers report increasing orders and output, but from a very low base. Machinery producers note that capital goods production is growing slower here than in the nation because the District has a very small share of the rapidly growing electronic, high-tech equipment industry. Traditional capital goods industries, including machine tools, heavy-duty trucks and industrial and electrical equipment, have been reviving in recent months but operating rates are generally well below those of the high-growth industries.

Real Estate. Realtors report home sales in recent months have fallen about 30% from last spring. Most of the decline is attributed to the midyear increase in mortgage interest rates. Realtors attribute part of the decline to recent changes in FHA and VA rates, which have caused customer confusion about the direction and level of rates. The inventory of listings is rising because of the slowdown in sales. Nominal transactions prices have not yet fallen but are expected to decline next spring if demand doesn't recover by then. Realtors report a recent increase in use of alternative financing arrangements.

Builders report that sales of new homes picked up in October and November following a third quarter slump, but sales are 13% below this time last year. Overall, 1983 will prove to be a profitable year for most builders, and builders expect the same level of activity in 1984 if mortgage interest rates do not increase.

Commercial Banking. In recent weeks, commercial banks in the Fourth District have become somewhat less liquid as deposit growth has slowed and loan demand has strengthened. Demand deposits declined slightly, while savings and small time deposits increased by small amounts. Loan volume increased sharply. The bulk of the increase in loans went to banks in foreign countries, commercial and industrial borrowers, and brokers and dealers. Banks apparently financed the increase in loans by reducing their holdings of other earning assets and by issuing large denomination CD's. In particular, declines were evident in bank holdings of cash, U.S. Treasury and agency securities, municipal securities and federal funds sales.

COMMENTARY ON ECONOMIC CONDITIONS

FIFTH DISTRICT - RICHMOND

Overview

There is little indication that the pace of recovery in the Fifth District has slowed. Expansion continues in virtually every sector, with month to month and year to year gains being reported nearly across the board. Absence of such gains in particular activities is generally attributed to special factors. Food processors, for instance, are encountering the relatively small agricultural output of the past season. Such special factors have resulted in some seasonally depressed employment and unemployment numbers, but, generally, employment is recovering sharply in most parts of the District. Retail sales remain among the sectors leading the recovery. Most areas are reporting sharp gains in sales. Credit demands remain modest as both consumers and businesses seem to be funding purchases from current or past income. Expectations of continued improvement in activity are widespread, with only retailers sensing that little further progress is likely.

Manufacturing

Total manufacturing activity continues to show improvement by nearly every measure. Shipments, orders, and order backlogs were up over the past month. Inventories were nearly unchanged as a slight drop in finished goods offset a small rise in materials on hand. Total stocks are still considered at or somewhat above desired levels, as is current plant and equipment capacity. Employment, average weekly hours, and weekly earnings also continued to advance in recent weeks.

Employment gains were recorded in most sectors, particularly textiles, furniture, and seasonal agriculture related industries. In the last mentioned category, gains were less than normal, however, and seasonally adjusted levels were accordingly down. Durable goods manufacturing, apart from the consumer areas such as furniture, continued to show mixed results.

Manufacturers responding to our survey report little change in prices they are receiving, but some scattered increases in prices paid. Respondents remain broadly optimistic. Nearly every one expects further gains in activity, nationally, locally, and in his respective market, over the next two quarters.

Consumer Spending

By all accounts, retail sales are still very strong and rising. Big ticket items are at least holding their own. With sales building into the holiday season the way they have, prospects for the final quarter are excellent. Retailers' expectations of a good season have apparently been substantiated during the first few days. The first weekend of the selling season was generally characterized as the best in years. Thus, while retailers do not seem to foresee much in way of further gains, apart from seasonal factors, they do not expect any near term losses. Automobiles sales also seem to be holding the substantial gains of recent months.

Housing and Construction

Sales of residential real estate are generally reported to have picked up again in recent weeks as mortgage interest rates stabilized or even edged downward. Construction of new units continues at a good pace in most areas. No significant decline, other than seasonal, is expected before spring, and will be unlikely, even then, if current sales rates hold up.

There has been little apparent change in the commercial and industrial sector where activity continues to improve, but only at rather modest rates. Expectations remain generally positive, but somewhat less robust than in many other sectors.

Banking and Finance

Loan demand still does not seem to be keeping pace with economic activity. Lenders have observed only modest increases in consumer lending, particularly non-auto related lending. Business loan demand also remains soft. This relatively weak loan demand and the recent strong growth of liabilities of financial institutions are still thought to be causing some deterioration of overall credit quality. Also, District financial institutions generally seem to expect the slow growth of loan demand to continue for some time.

SIXTH DISTRICT - ATLANTA

The southeastern economy continues to strengthen. Employment and orders are up in regionally important industries. Vigorous retail sales during the Thanksgiving weekend have made merchants optimistic regarding the Christmas season. Housing sales have increased since the FHA/VA rate dropped, and commercial real estate investment is lively. Business lending by major banks has improved markedly, and the growth in consumer lending remains healthy. Tourist trade is picking up in several major convention cities. The Payment-In-Kind (PIK) program has aided many farmers, but heavy debt burdens presage difficulties for marginal operations.

Employment and Industry. A poll of southeastern manufacturers indicates that employment and orders continue to improve even though the latest available labor market statistics for October show mixed signs. Employment losses in the petrochemical industry have ceased, and economizing measures have enabled firms to earn profits despite low utilization rates. Oil and gas drilling is increasing in Louisiana and Alabama. Corporate executives, anticipating rising energy prices over the next two to three years, are optimistic about prospects for 1984. Brisk sales of new cars have spurred demand for tires. In response, Alabama tire manufacturers, who produce 15 percent of the nation's supply, are expanding capacity by as much as 10 percent. Government contracts for military clothing are boosting production in the apparel industry. Pulp and paper mills are now operating at over 90 percent of capacity, almost 10 percentage points higher than last year. Demand for computer paper has been especially strong. Southern mills produce 52 percent of the nation's paper. Timber industry representatives report continuing upward momentum and expect production levels by year-end to approach peak 1979 levels. However, the effect of the upturn in housing has yet to reach some areas of Mississippi that depend heavily on lumber manufacturing.

Consumer Spending. Major southeastern retailers polled about Thanksgiving weekend sales report double-digit increases over last year's levels. Sales of apparel, toys, electronic goods, and home appliances have been especially strong despite limited price discounting. Most merchants, encouraged by the high levels of activity over the holiday weekend, are optimistic that consumer spending will reach a new peak by year-end. New motor vehicle sales continue to grow at a crisp pace. Truck and van sales are outperforming car sales, in part because dealers have had an abnormally low inventory of new cars.

Construction. The drop in the FHA/VA rate to 12.5 percent in early November stimulated housing sales by decreasing buyers' monthly mortgage payments, in the view of most realtors polled. Nonetheless, many potential buyers may be delaying purchases in anticipation of further decreases, and Atlanta lenders believe the increase in discount points that generally accompanies a decrease in FHA/VA rates may have motivated some sellers to leave the market rather than pay the additional fees. Orlando and Nashville realtors report increases in new-home sales, and Atlanta real estate agents indicate improvement in the used-home market. However, the cancellation of the Clinch River Breeder Reactor has dampened sales of single-family houses in Oak Ridge, Tennessee.

Commercial real estate development in Tampa and Miami is proceeding swiftly. Tampa city officials are evaluating designs for a large multi-purpose convention center, and the city's first billion dollar project is under construction. Contacts indicate that Miami is undergoing an office-building "boom" fueled by developers' expectations of the legalization of interstate banking and attendant increases in demand for office space. Rapidly growing areas such as Atlanta and Jacksonville are also experiencing heavy investment in commercial real estate.

Financial Services. Deposits at large commercial banks advanced from September to October by 1.5 percent, slightly below the previous month's rate of increase. The slowing resulted from a decline in the growth rate of time deposits, which represent over half of southeastern bank deposits. Loans at large commercial banks increased 3.4 percent from September to October. Business and real estate lending grew markedly faster, while consumer lending sustained the strong pace of previous months. Some large southeastern banks have begun investing in one another's stock, building relationships which they could quickly expand if interstate banking wins legislative approval.

Tourism. Lodging tax revenues increased in October relative to year-earlier levels in all states except Tennessee, but hotel occupancy is still down in most cities except Orlando. Contacts in Atlanta and New Orleans report that the addition of new facilities has ameliorated convention trade. The first phase of the Georgia World Congress Center expansion, adding 65,000 square feet of exhibition space, opened in early October. Attendance at southeastern attractions continues to outpace year-earlier levels, and most of those surveyed plan to invest in expanded facilities in hopes of drawing visitors to the 1984 World's Fair in New Orleans. More than 15,000 people applied for 8,000 jobs at the Fair during the two weeks after applications were first accepted in November. The number of passengers at most of the District's major airports continues to increase over year-ago levels. Both large and small carriers are adding service to smaller cities.

Agriculture. Crop farmers' net income for the year has increased 10-15 percent above 1982, primarily because of PIK commodity payments. Profit margins of livestock operations have diminished steadily in 1983 as rising production coincided with sharp increases in feed costs, leading to a classic price-cost squeeze. In the broiler and egg industry 1983 was better than 1982, but the improvement would have been greater if the climb in feed costs had not offset much of the gain offered by rising prices.

Nevertheless, the increase in net revenue signals a reprieve, not a turnaround in the farm economy. According to reports from the Farm Credit System and commercial banks, conditions are improving for the more conservative, financially sound farmers who constitute most of their borrowers and who are poised for recovery. In contrast, borrowers from the Farmers Home Administration (FmHA), who tend to operate marginal and/or highly leveraged farms, found only a temporary respite, if that, in 1983. In every District state except Tennessee, FmHA delinquency rates have edged higher compared to a year ago. The delinquency rate of Georgia's borrowers from FmHA is 56 percent, the highest rate in the nation. Only in Tennessee is the rate less than one-third. Many farmers in this group can do little better than hope to continue in business. Agribusinesses, particularly those which supply farm inputs such as fertilizer, have experienced trade declines of a third or more, although equipment repair work reportedly has increased.

SEVENTH DISTRICT--CHICAGO

Summary. The tone of business and consumer sentiment in the Seventh District is much improved compared to the situation six to 12 months ago, but the firm confidence of several years ago has not returned. Gains in activity are widely expected to continue into 1984, with additional lagging sectors participating. Estimates of demand for most consumer durables have been raised periodically in the past several months, in contrast to downward revisions in 1982. Retailers anticipate the best Christmas in five years, but are stocking and hiring cautiously. The strength of demand for workers in the District continues to fall far short of the national experience, despite substantial recovery in the auto industry. The pickup in demand for heavy capital goods remains spotty. Inventories, generally, continue under close control. Shipments of household appliances and paperboard were at record levels in the third quarter, but volume of most durable goods industries remains far below earlier peaks, and is not expected to regain those peaks in the year ahead. Heavy inroads of foreign competition have intensified. Residential builders are entering the slow winter season with dampened spirits relative to last spring. Farmers are beginning to increase purchases of supplies and equipment slightly, reflecting improved income and expectations of larger plantings in 1984.

Confidence Surveys. Formal and informal surveys of executive and consumer attitudes in the District show substantial improvement compared with dismal reports early this year. Professional pollsters at the University of Michigan emphasize that indexes of sentiment reflect the direction rather than level of activity. Substantial gains in such measures in this region indicate more a feeling of relief that the long decline in activity has come to an end--and has been reversed in some sectors--rather than the old time ebullience.

Retail Trade. Most general merchandise retailers (not all) have reported improved sales and are counting on substantial increases in Christmas volume. Gains are projected in the 6-12 percent range over last year's results, which were disappointing. Most of the rise will be real because prices average only 1-3 percent higher. Merchants speak of "pent-up demand." Actual total sales volume may never be known accurately because of the growth of discounters, off-price specialty stores, and catalog houses that are not adequately tabulated. Credit use is up. Among the strongest lines are furniture, appliances (especially microwaves), some types of home computers, video recorders, some clothing, and various luxuries such as expensive dolls and cordless telephones. Merchants have been stocking cautiously for Christmas, preferring the chance of some stockouts to general excess. Hirings of temporary or part-time clerks are said to be much less frequent than in past years of rising sales.

Employment. In September, payroll employment in Illinois, Indiana, Iowa, and Wisconsin was still below a year earlier. It appears that little improvement occurred in October. Michigan showed a gain in employment from September 1982, reflecting motor industry recalls of workers. Despite lack of employment gains, all states reported substantial declines in estimated unemployment. In the 5-state area, employment was 25,000 below year-ago in September, while unemployment was estimated to be down 370,000. (Nationally, the gain in employment in this period was much larger than the decline in unemployment.) In Illinois, seasonally adjusted employment in October was the same as in December 1982. In this period the state's reported unemployment rate dropped from 12.8 to 9.7 percent.

The dichotomy between stable employment and declining unemployment is explained as "outmigration", and "withdrawals from the labor force." In any case, job markets are still weak. Help-wanted ads and hiring intentions are up significantly, and lay-offs have been reduced, but these gains are offset by additional establishment closings and employment cutbacks, often through attrition. Some employers are offering generous incentives for early retirement to reduce "redundancies." Others are using overtime to handle increased output to such an extent that worker unrest has increased.

Autos and Appliances. Both auto and appliance producers substantially underestimated demand for certain models in 1983, reversing the tendency to overestimate noted in earlier years. As a result, inventories are too low. Auto output will be 60 percent above last year in the fourth quarter, with strong pressure to build more large cars. Output has been restrained by a desire to avoid quality problems. First quarter auto output is scheduled to be up 50 percent above the year earlier total. Appliance shipments, in units, were up 34 percent in the third quarter to a new alltime high. Industry analysts had projected appliance shipments to rise 7 percent in 1983, but the actual gain is likely to exceed 15 percent.

Capital Goods. Demand for capital equipment produced in the District has increased somewhat, but in a highly uneven manner. Output of replacement parts has increased on a fairly broad front. Machine tool orders are far above last year, but only 40 percent of the rate of early 1980. A diversified producer of capital goods reports bookings at only 50 percent of a "good level." Demand for steel for capital goods and construction remains near the recession low. Orders for steel castings for equipment are at only 40 percent of capacity. Production of heavy trucks will rise in early 1984, but only to 50 percent of the 1979 level. Truck trailers, almost unique among capital goods, are being produced at capacity because of increased size limits. Railroad equipment orders are few and small. Demand for construction equipment has picked up slightly. Farm equipment sales are expected to improve soon, but large inventories can accommodate most needs. Some District electric utilities have further slowed work on nuclear generating plants, partly because of soaring costs which may exceed original estimates ten-fold. A large number of District capital goods plants are closed or scheduled for closing, including plants producing rail cars, trucks, materials handling equipment, construction equipment, and farm equipment. In some cases companies headquartered here have alternative sources, either in other regions, especially the South, or abroad.

Foreign Competition. The current plight of producers of capital goods partly reflects slow demand world-wide. However, they complain bitterly of the ever-growing threat of foreign competition, which they attribute to the high value of the dollar, subsidies by foreign governments (including financing), and trade barriers abroad that hamper exports. Increasingly, capital goods producers are following the lead of the auto companies by arranging foreign sources for components including fasteners, castings, and engines, and complete products such as machine tools and construction equipment. In some cases this has resulted in the closing and dismantling of domestic plants.

EIGHTH DISTRICT - ST. LOUIS

Economic expansion continued on a broad front during October and November in the Eighth District, and most respondents anticipate further gains during the winter. Retail sales were strong in the early Christmas season. Factory orders and production continued to rise, and inventories expanded moderately. Some capital spending for the purpose of increasing efficiency has been reported. Employment continued to rise. Construction activity, adjusted for seasonal influences, remained vigorous.

Outlook

Seven business economists surveyed expect the economic expansion to continue in the first half of 1984, but at a reduced pace. The average expansion for real GNP is expected to be at an annual rate of about 4 percent, with the first quarter being slightly greater and the second quarter weaker. They anticipate that their own firms will expand at a pace consistent with this national projection. Most feel that a slowing to a more sustainable pace is desirable; one, however, believes the slowdown will be excessive because of the relatively slow rate of monetary expansion since summer. All respondents project prices to rise slightly faster in the first half of 1984 than during 1983; the median forecast is at a 5 1/4 percent rate. Yet, for their own company's prices, the median forecast is just below a 4 percent rate.

Consumer Spending

Department stores, discount houses and small shops throughout the District report continued favorable year-over-year sales in October and November. For many stores the gains were in double digits. Most items have been moving well, especially apparel, footwear, fashion accessories and home furnishings. Merchants, optimistic about the Christmas season, have enlarged sales forces to handle the business. Consumers, with rising incomes and a large amount of liquid savings, seem to be in a mood to spend.

Automobile sales were mixed. Four dealers reported that October-November sales averaged 14 percent above the same months in 1982, while three other dealers had small declines-- averaging 5 percent. Both used cars and trucks sold moderately well. Dealers report that adequate financing is available, and buyers do not seem to be as concerned about the level of interest rates as they had been earlier.

Home sales have slowed seasonally; however, they continue to be considerably above year-ago rates. In the St. Louis area, sales of homes through November 1983 were 2 1/2 times those in the same period of 1982, and industry spokesmen expect that sales will rise another 15 percent from 1983 to 1984. Greatest strength is among first-time buyers purchasing lower priced homes. Demand for apartments has been strong; in one major county, nearly twice as many apartments have been constructed recently as in the corresponding period a year ago, and plans have been made to start building 600 more to satisfy the demand. Demand for new office buildings remains strong despite a rise in vacancy rates due to the substantial amount of new space coming into the market.

Manufacturing

Manufacturing activity continued to expand at a rapid pace in October and November. Expenditures for capital equipment accelerated, but most of the outlays were for replacement and modernization rather than for increased capacity. Orders and production of consumer goods continued to rise, but at a somewhat slower pace than during the spring and summer. Defense business rose again after slowing in the early fall. Some manufacturers and distributers have been accumulating inventories to handle the increased volume. Most prices in the manufacturing sector have been steady, but a few have begun to rise.

Employment

Reflecting the improved pace of economic activity, employment in the District rose in October and November, and the average workweek in manufacturing lengthened slightly. Unemployment rates in the District declined moderately. Major hirings have been in the manufacturing sector, particularly for nonelectrical machinery and appliance production. Also, many retail and service firms expanded their workforces. On the other hand, the number of construction workers declined seasonally, and a service firm made a sizable reduction in its staff. The outlook is bright for further gains in employment during the winter.

Finance

At ten of the larger commercial banks in the District, loans rose moderately during October and the first three weeks of November. Consumer installment loans increased $62 million, while real estate loans declined $35 million. Commercial and industrial loans rose $200 million, but much of the gain was seasonal. Several bankers reported that the relatively weak loan demand stemmed from large business cash flows, thereby reducing the need for short-term credit.

Liquidity of the banks improved as funds continued to flow in. Demand deposits jumped 14 percent in October and early November, and savings deposits increased 4 percent. Part of the expansion in demand deposits was seasonal; in the comparable period of the two previous years they rose an average of 6 percent.

NINTH DISTRICT - MINNEAPOLIS

The Ninth District economy has settled in for the winter with more of the moderate growth reported last month. Unemployment generally continues to fall, while consumer spending continues to strengthen. Mining and manufacturing activity may be gaining some momentum, as may be tourist business at heavily snow-covered ski resorts. Agricultural conditions haven't changed much from last month's report.

Employment. The most recent data indicate that employment prospects have continued to improve in much of the district. Total employment in Minnesota rose by over 12,000 workers between August and September. As a result, the state's unemployment rate dropped from 7.2 percent to 6.5 percent. In the Minneapolis-St. Paul metropolitan area, the jobless rate dropped slightly more, from 6.4 percent to 5.6 percent, and in South Dakota it also dropped a bit, from 4.4 percent to 4.2 percent. In Wisconsin, the unemployment rate was 9.2 percent in October, up only slightly from 9.0 percent in September. In Montana, it dropped to 6.6 percent in September, down from 7.8 percent in August. Regional analysts in Duluth, Minnesota--which was hit hard by the recession--expect its unemployment rate to fall below 12 percent in September from its seasonally adjusted rate of 12.1 percent in August. But unemployment remains very high in other parts of northern Minnesota and Michigan, reflecting the depressed mining industry.

Consumer Spending. Buoyed by brisk holiday sales, overall consumer spending is ending the year on an uptick.

Early reports indicate that sales of general merchandise in the holiday shopping season will be at least 20 percent higher than a year ago. One Twin Cities retail chain reports that this November is its best ever, with double-digit sales increases in its suburban locations. Electronic components and intimate apparel are moving particularly well there. Sales in Duluth, Minnesota, are surprisingly good, given the continuing weakness in this local economy. One chain in Rochester, Minnesota, recently broke its record for single-day sales, and stores have opened early to accommodate the Christmas rush. Our Bank directors report that sales are good throughout most of North and South Dakota, where snows have increased snowblower sales. General merchandise sales in Montana are spotty--stronger in the western part of the state than in the eastern part.

Auto sales are also maintaining the strength evident last month. District Bank directors report that both new and used car sales are good. Order backlogs for 1984 models have appeared in western Wisconsin. In South Dakota, large cars are selling better than small ones.

Home sales have not deterioriated much from last month's pace. Unit sales in the Twin Cities in November were 4 percent below those in October, but total unit sales in that area are 35 percent higher in 1983 than in 1982. District directors report a housing boom in both Fargo and Bismarck, North Dakota, but a softening market in Eau Claire, Wisconsin. The more expensive homes are selling best in Billings, Montana.

Mining and Manufacturing. Several encouraging signs appeared in mining and manufacturing this month, indicating that these industries may be gaining momentum. Paper production is doing "super," according to one director. According to another, demand for waferboard is sufficient to justify a few more plants in hard-pressed regions of northern Minnesota and Michigan.

Also, an iron mining operation in each of these regions is reopening. A cheese plant in Wisconsin is celebrating its best business in a long time, and a brewery is also toasting a good year. All this follows healthy third quarter earnings increases at several of the largest manufacturers in the district.

There is, however, still room for improvement in district mining and manufacturing. The industrial space vacancy rate recently increased in the Twin Cities. And, although oil and gas activity is up substantially in North Dakota, coal production is down a bit in Montana.

Tourism. District tourism was good this fall, and most of the industry looks forward to a good winter. Resorts in the Indianhead region of northern Wisconsin and the Upper Peninsula of Michigan were filled with deer hunters this fall. With the inevitable arrival of the ubiquitous district snow, ski resorts are preparing for an onslaught of business. The Big Sky ski resort near Bozeman, Montana, has added two new gondolas and forty new condominiums. But a 5 percent user fee for snowmobile trail grooming has some Michigan officials worried.

Agriculture. High corn and soybean prices and the federal Payment-In-Kind (PIK) program are still helping boost farm income. Despite Minnesota's smallest corn crop since 1976, high prices and the estimated $600 million worth of PIK corn paid to Minnesota farmers will bring that state's total corn receipts up to $1.8 billion. This exceeds receipts in the bumper crop years of 1981 and 1982. Minnesota's soybean crop this year is its fourth largest, and soybean prices are currently at about $8 a bushel. This makes the Minnesota soybean crop worth about the same as the state's corn crop this year. A similar soybean story is reported in both North and South Dakota.

The stories for wheat and other district crops don't detract from this. Wheat yields are generally good in North Dakota and Montana. While the sunflower crop in North Dakota is down about 40 percent, higher sunflower prices will probably keep receipts from falling much.

However, the district's livestock operations are still being hurt by high feed costs and low cattle prices. Those prices are down as much as 17 percent from a year ago. The continued cost-price squeeze has caused a culling of herds which will further depress prices, an effect which could be exacerbated by the new dairy diversion program. Prices are expected to pick up later next year when the reduced herds are brought to market, though.

TENTH DISTRICT--KANSAS CITY

Overview. Reports from the Tenth District indicate a continuation of favorable economic conditions. Retail sales have moderated somewhat, but remain strong, with little upward movement in prices. Prices of industrial inputs also are little changed. Inventories of retail goods and of industrial inputs are regarded as satisfactory. Housing starts have leveled off while home sales have slowed. Savings inflows at savings and loan associations have increased, but mortgage demand has declined. Tenth District banks report a slight rise in deposits and generally stable loan demand. Marketing of fall harvested crops is slow, with many farmers apparently holding their crops in anticipation of higher prices.

Retail Trade. Retailers surveyed report that year-to-date total sales are up 5 to 20 percent over 1982 levels. Growth in sales, however, has slowed slightly in the past three months. Virtually all of the retailers contacted are satisfied with present inventory levels and none intend to start clearance sales earlier than in the past. A large number of respondents indicated that they raised prices slightly on some items during the past three months, but most of these increases were seasonal in nature. Almost all are optimistic about the sales outlook for the upcoming Christmas season.

Purchasing Agents. Most purchasing agents contacted report input price increases of between 2 and 6 percent over last November, although some report no change or even moderate declines. Few report significant price changes over the past three months. None of the agents contacted expects significant price increases before yearend; however, a few anticipate price increases very early in 1984. With one exception, purchasing agents report no availability problems, but several report some lengthening in lead times. Most firms are satisfied with current inventory levels and do not plan any changes in the next few months.

Housing Activity and Finance. Home builders report that housing starts continue to outpace 1982 levels. Starts appear to be leveling off, however. Recent inventory increases in the multifamily and $100,000+ single family categories, along with the onset of inclement weather, are in part responsible. Sales also are slowing. Reduced foot traffic by potential buyers and recent price increases are cited as contributing factors. The leveling off of starts and slowdown in sales have improved the outlook for materials. Builders foresee no shortages or price increases for materials through the first quarter of 1984. Most savings and loan associations report continued improvement in savings inflows. Some attribute this to more aggressive, competitive bidding for funds. Demand for mortgage funds and commitments has fallen from its peak in mid-summer, largely for seasonal reasons. Most savings and loans expect a slowdown until next spring, when anticipated lower mortgage rates and pent up demand should bring new homeowners into the market. Mortgage rates have been fairly steady and are expected to remain so for the rest of 1983.

Agriculture. The harvesting of row crops is virtually complete throughout the Tenth District. Winter wheat conditions across the District range from good to excellent. Planting from fencerow to fencerow is reported in some areas, indicating low participation by farmers in the 1984 Payment-In-Kind (PIK) program for wheat. Winter wheat pasture is in excellent condition, but some District bankers report a shortage of cattle to place on the pasture. Marketing of fall harvested row crops is reported to be slow, with many farmers holding their crops in storage in anticipation of higher prices. The selling of feeder cattle throughout the District is reported to be at normal levels. An average number of cattle have been sold while a larger proportion of calves than usual are expected to be held through the winter by ranchers. Some liquidation of gilts and sows is reported to be occurring in isolated areas of the Tenth District, but hog producers generally appear to be retaining breeding herds in anticipation of improved prices. Some paydowns by farmers are being made on their agricultural production loans, but the major part of the activity is expected to occur in December and in early 1984. Thus, it is too early to assess the impact of PIK payments on loan paydowns.

Banking. Tenth District banks report little growth in loan demand since the last Beigebook survey. Real estate, agricultural, commercial, and industrial lending are generally unchanged from last month. Only consumer lending increased Districtwide. Most bankers do not expect loan demand to rebound in the near future on grounds that the Tenth District, which entered the recession late, has entered the recovery late. The prime lending rate at Tenth District banks is 11 to 11 1/2 percent, unchanged from last month. Deposits at Tenth District banks grew slightly last month. Money market deposit accounts are responsible for nearly all of the growth. Demand deposits, NOW accounts, Super NOW's, passbook savings accounts, and large CD's remained constant. Responding banks report that the deregulation of time deposits on October 1 is having little impact on small-denomination time deposits, which grew only slightly last month. In regard to the imminent switch to contemporaneous reserve accounting, most Tenth District bankers anticipate little difficulty in complying with the new procedures.

ECONOMIC COMMENTARY

ELEVENTH DISTRICT—DALLAS

Economic recovery in the Eleventh District is continuing and some sectors are showing strong year-end gains. Total manufacturing production is rising with particularly strong increases in manufacturing equipment. A seasonal slowdown in commercial construction has occurred but residential construction was unseasonally strong. Loan growth picked up at all member banks in the District, but business loan demand remains sluggish at large banks. Auto and retail sales continue at a brisk pace. Farm income will be higher this year than last.

Growth in manufacturing production in the District continued at a moderate pace. Gains in demand for nonelectrical machinery led to increases in total employment and in the number of hours worked. Production of capital equipment is particularly strong with orders for material-handling equipment leading the way. Orders for lumber and wood products, which usually decline at year-end, have remained steady. Capacity utilization at lumber mills is high, except in Houston where it has been significantly below other areas. Strong demand has kept capacity utilization and employment high at District aluminum plants. Inventories of aluminum products are still below desired levels, and the high order rate is impeding accumulation. Strong auto sales and increased capital spending have also buoyed steel orders. Steel fabricating firms now want to build inventories and add employees. Demand for fabricated copper from District producers remains sluggish because of strong competition from

Third World producers. Orders at the October market for spring apparel products were the largest on record.

The number of active drilling rigs in Texas rose to 932 in mid-November. This was the highest level since early January and 39 percent above the mid-July trough of 669. Huge inventories are still plaguing the oil-field supply industry. Analysts expect more bankruptcies in that sector.

Department store sales in all major District cities were well above year-earlier levels. Even El Paso is reporting higher sales compared to last year although sales are still below pre-devaluation levels. Home furnishings are the strongest component, but clothing sales are picking up rapidly. Intense competition is expected to keep future price gains moderate.

District auto sales remain strong. October sales were above year-earlier levels throughout the District, but in Houston sales are down on a year-to-date basis. Dealers' profit margins have increased because a larger share of financing revenues is being retained and inventory carrying costs are lower. Tight inventories are still hampering sales somewhat.

Residential construction is likely to continue to slow next year. An unseasonally large increase in both single-family and multi-family permits was reported for October. Nearly 70 percent of these permits were for apartments and condominiums with the bulk of activity concentrated in Dallas. Concerns about overbuilding in the multifamily sector continue, and serious questions are now being raised about the means used to attract investors to some of these projects. Land prices appear to have been inflated by "land flips," a process by which a tract of land is sold several times in a short period to boost its value. The increase in single-family permits may be the result of builders accumulating inventories. Builders expect lower mortgage rates to stimulate sales.

Commercial construction remains strong despite a seasonal decline in October from September. On a year-to-date basis the value of commercial construction is up in virtually all non-energy dependent areas. Retail construction is continuing at high levels. For 1983, the value of permits for office space in Dallas will probably end up on par with the near record 1982 level.

Loans at member banks were up in October bringing the year-over-year increase to more than 16 percent. Business loans at large weekly reporters, however, declined in October after showing earlier gains. Real estate lending continues to be the strongest loan category. Total deposits at the large banks are below year-earlier levels with the largest declines in small and large time deposits.

Farm income in Texas will be higher this year than last because of increased livestock sales, higher crop prices, and the Payment-in-Kind program. Cattle and hog producers, however, continue to lose money on production, and bad weather has reduced cotton income.

TWELFTH DISTRICT -- SAN FRANCISCO

In the Twelfth District the economic expansion is continuing, although growth in some areas such as the Northwest, especially Oregon, is lagging. Retail sales remain strong and orders are picking up in a number of capital goods industries. Many firms are rebuilding inventories that have been depleted by continued strong sales. However, businesses remain cautious about adding to inventories. Nonresidential construction is showing strength in some regions of the district. Commercial and industrial loans at large commercial banks expanded in early November after being noticeably weak since mid-year.

Consumer Spending

Consumer spending still is strong throughout most of the district. The strength is apparent in retail sales and in new and used automobile sales. Attempting to keep inventories lean, many retailers and suppliers had run short of items as consumer spending remained stronger than expected. The combination of depleted inventories and anticipated strong Christmas sales has encouraged many businesses to expand their inventories. Nevertheless, the prevailing attitude toward building up inventories still has to be described as cautious. Respondents indicated that the performance of sales over the remainder of this year will be an important factor in molding plans for inventory accumlation in 1984.

Manufacturing and Mining

A number of capital goods industries are experiencing a pickup in orders. The most obvious strength is among firms involved in manufacturing high-technology equipment and electronics. Orders for airplanes are up, primarily due to purchases by foreign airlines. Aluminum production is increasing. The lumber industry also is showing some improvement, but this is mostly related to stronger demand for paper and packaging materials. Mining in Utah, however, is experiencing little if any improvement.

Some manufacturers reportedly are somewhat more hesitant than retailers to add to inventories. The reasons for this apparently are uncertainty about consumer spending in the future and high interest rates. Once again, firms are looking to continued strong sales through the rest of this year to confirm the durability of the economic expansion.

Respondents throughout the district suggest that at this point businesses are not planning <u>sharp</u> increases in real capital outlays. Businesses still are uncertain as to the sustainability of the recovery and are reluctant to make major commitments for plant expansion. The bulk of the capital spending that is planned appears to be targeted for new equipment and modernization rather than expansion.

<u>Construction and Real Estate</u>

Following the national pattern, residential construction generally has slowed somewhat in the West. Nonresidential building activity varies considerably from area to area. Reports indicate that such construction is relatively strong in southern California as well as the Central Valley of California. In Southern California, much of the nonresidential construction is for companies in the electronics, aerospace, telecommunication, and computer industries. The state of Washington is seeing some rise in nonresidential construction, while Oregon and Idaho are experiencing either flat or declining activity in nonresidential construction.

<u>Agriculture</u>

There still is concern that the strength of the dollar is hampering the agricultural sector. For example, the strong dollar is thought to be preventing Asian parties from buying high-quality California cotton. With regard to another development, the closing of the Willamette Production Credit Association in Oregon reportedly has adversely affected farmers in their efforts to obtain financing for 1984. One respondent thought that this could lead to "forced" sales of some farmland in the area.

Financial Institutions

Business loans (NSA) at large commercial banks in the Twelfth District expanded in early November. Prior to the recent growth, business loans at large banks generally had contracted since about mid-year, while at small banks these types of loans had expanded relatively rapidly. Many of the respondents thought that the difference in the behavior of business loans at large and small banks observed until recently reflected the fact that the large corporate customers, which tend to deal with the bigger banks, have access to primary markets for funding. Some respondents indicated that larger corporations had been using funds acquired earlier in the year when bond and equity financing was more attractive. The combination of direct access to primary markets, improved profits, and lower inventories reduced the need for large corporations to rely on bank loans. The recent growth in business loans at large banks could be related to a buildup of inventories.

Depository institutions in California continue to actively advertise the deregulated deposit accounts. In general, interest rates offered on deregulated accounts do not appear to be inconsistent with other market rates, although rates on longer-term time deposit account tend to be higher in California than in the rest of the nation. In the Twelfth District, small-time deposits still are expanding, but have not shown signs of accelerating in early November.