

**SUMMARY OF COMMENTARY ON CURRENT ECONOMIC CONDITIONS
BY FEDERAL RESERVE DISTRICTS**

September 1987

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SUMMARY*

Business conditions improved in recent weeks for most regions of the country although weakness persists in some areas. Chicago, New York, Philadelphia, Minneapolis, and Boston report moderate economic expansion while Atlanta and San Francisco note brisk growth. Cleveland and St. Louis, in contrast, indicate weakening business activity.

A resurgence in industrial activity has boosted many regional economies recently. Orders and production for electronic equipment, lumber, steel, and textiles are increasing. Contracting domestic auto production, however, is blunting economic expansion in some areas. Construction activity is generally mixed; residential building has slowed in most regions, but commercial construction continues to grow, especially the nonbuilding component. Consumer spending has been moderate, and retailers are cautious but positive about the outlook for fall sales. Several Districts report moderate merchandise price increases. Auto sales have been stimulated by manufacturers' incentives. Favorable crop conditions have led to greater-than-average yields in some regions, and farm credit problems are declining.

Industry

Most Districts report improvement in industrial activity and point to continued expansion, at least for the near term. Factory orders, production, and shipments are generally above June-July levels and are trending upward. Inventories are for the most part at desired levels. Although input costs are expected to rise modestly, most producers do not plan to increase prices at the present time.

Chicago notes that demand for steel is strong. Cleveland reports that firm prices have helped specialty steels, and Atlanta sees increasing activity for small steel

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producers. Boston reports increased demand for computer equipment, and San Francisco notes that orders and shipments are strong for electronic equipment producers.

Philadelphia, Richmond, and Atlanta report increasing tightness in certain labor markets. Philadelphia notes that housing construction has slowed because of a lack of skilled carpenters, while Atlanta reports that carpet shipments are being delayed because producers have not been able to hire enough workers to keep up with orders. Minneapolis bank directors are concerned that tight labor markets may deter firms from locating in parts of the region. Although total manufacturing employment continues to decline in St. Louis, textile plants are operating near capacity; apparel orders are growing, as they are in Atlanta and Dallas. Less positively, Chicago and Cleveland suggest that weak domestic auto sales could result in further production cuts and layoffs in assembly plants in their regions.

Consumer Spending

Retail activity in July and August was up moderately compared both to previous months' and year-ago levels in Boston, New York, Cleveland, Atlanta, and Kansas City; sales growth was somewhat lackluster in other Districts. Boston reported that fine summer weather boosted sales of seasonal items, and Cleveland, Atlanta, and San Francisco noted that soft goods sales were outperforming hard goods sales. A pick-up in appliance sales in Dallas, following a prolonged period of weakness, is attributed to a rise in first-time home purchases; sales of big-ticket items accelerated in mid-August in Richmond. Philadelphia and Chicago report that the late Labor Day this year is delaying back-to-school purchases, while sales of these items are strong in Atlanta, where school starts early. Hardly any Districts reported unusual imbalances in inventory levels. Retailers typically are reported to be "cautious or moderately optimistic" about the sales outlook for this fall compared to fall 1986.

Boston, Cleveland, and Richmond noted moderately rising prices or expectations of moderate price hikes ahead. In Boston, prices are expected to rise significantly more by next spring because of imports; prices of electronics and apparel items are already rising across the nation because of import quotas and the falling dollar. The tight New England labor market is making it difficult for retailers to attract and retain employees.

Manufacturers' financing and rebate incentives apparently have sparked auto sales and reduced inventory levels to more manageable levels although Chicago received reports that consumer response has been restrained. The outlook for sales apparently has generated dealer concern in much of the country.

Construction

Construction activity is mixed across the country. Residential construction is slowing in a majority of Districts although conditions vary within many areas. While single-family construction is generally increasing, Chicago, Kansas City, and San Francisco mention a continuing decline in multifamily construction. Sales of existing homes soared above last year's levels in Atlanta. Kansas City and upstate New York also report an active residential market.

Commercial construction continues to show a mixed pattern of strength and weakness, but it remains relatively strong. Nonbuilding construction is strengthening in Dallas, and Philadelphia notes that recent and prospective completions of major highway links in the suburbs will boost all types of commercial real estate in these areas.

Financial Services

Loan growth in the nation's larger commercial banks is slowing. Philadelphia, Cleveland, and Atlanta report a slackening in commercial and industrial lending, but Philadelphia expects business lending to increase moderately over the next few months. This uptick may be enhanced by improving conditions for the region's manufacturers. Passbook savings account balances are growing rapidly in several western locations.

Dallas notes a further slowing of deposit growth at both banks and thrift institutions. An increasing rate of decline in large time deposits is being offset partially by increases in small time deposits.

Agriculture, Forestry, and Mining

Livestock producers are experiencing more favorable returns with St. Louis, Minneapolis, and Dallas reporting a profitable year as the result of lower feeding costs and higher product prices. Crop conditions have been favorable in most Districts this growing season; Atlanta, St. Louis, Minneapolis, and Kansas City expect above-average yields. Excessive heat and dry weather have damaged crops in the Richmond District.

St. Louis notes that the volume of farm loans outstanding in their District is down over 15 percent from last year. Farm loan delinquencies and losses at agricultural banks have also dropped. Dallas notes that farm credit problems are diminishing in the Eleventh District as well.

More volatile crude oil prices have characterized the petroleum industry in recent weeks, but drilling rates have continued to rise. Kansas City suggests that such volatility will likely prevent a strong rebound in the energy industry in the near future.

San Francisco and Atlanta note an increase in lumber exports. In addition, imports of Canadian lumber have fallen slightly, while demand for southern pine remains strong.

FIRST DISTRICT - BOSTON

The First District economy continues to expand, according to reports from area merchants and manufacturers. Retail sales increased modestly as fine summer weather reduced the frequency of shopping trips while boosting sales of seasonal items. For manufacturing contacts, orders have been running at an improved rate for the past three to six months. A number of manufacturers expect increases in profits in the near term because of increased sales volumes, cost-cutting efforts and tax changes. While manufacturers generally do not see evidence of rising prices, retailers expect prices to rise sharply in the spring because of higher import prices.

Retail

Retail sales in the First District expanded modestly in July and the first half of August. Excellent summer weather has boosted sales of seasonal items but reduced the frequency of shopping trips. Among the merchants contacted, recent sales changes relative to a year ago ranged from minus 5 percent to plus 12 percent on a comparable stores basis. The one store with lower sales is still well ahead of last year on a year-to-date basis. A few stores reported that extensive markdowns (accompanied by a drop in margins) had contributed to their sales increases. Inventories are up somewhat in several stores. Retailers are having difficulty attracting and retaining employees because of the tight New England labor market.

Prices are said to be rising moderately, but are expected to climb more significantly next spring because of imports. The decline of the dollar, quotas for apparel items, and political disruptions in some supplier countries have combined to raise prices and reduce the availability of foreign goods. Retailers continue to seek domestic alternatives.

Plans for new store openings next year are similar to this year. Budgets for next year, however, project smaller sales increases than have been realized to date this year.

Manufacturing

For most First District manufacturers, orders have been running at an improved rate for the last three to six months. Computer and fabricated metals firms cite the strongest gains relative to a year ago. Only a minority - in electrical equipment and machine tools - report orders below 1986 levels. Exports are said to have played little role in the improved situation; several respondents noted that foreign markets are served from overseas subsidiaries.

Inventories continue to be carefully managed and are generally satisfactory. Employment appears to be stabilizing. Where employment levels were falling through attrition, the pace has slowed, and at several firms employment has risen. Contacts granting recent wage increases report that these pay raises were at or below last year's levels.

For most respondents, capital spending is at least equal to its 1986 level, and in several cases is at its highest level in years. Much capital spending continues to be driven by technical innovation, but some firms are building new plants.

Input prices are generally steady, although one respondent mentioned that prices of imports from the Far East have been rising at an accelerating pace for the last six to nine months. Other firms noted rising energy and steel prices. Sales prices of First District respondents have been stable. While a couple of firms were able to increase prices modestly (3 percent) early in the year, others continue to sell some products below list.

A number of First District manufacturers expect improved profits in the near term. They cite increased sales volumes, productivity gains, cost-cutting programs and tax changes. None of the contacts expressed concern about inflation or the possibility of a downturn in the near future.

First District Economic Indicators Through June

The most recent economic indicators for the First District were mixed. Nonagricultural employment in the New England region, which closely overlaps the First District, declined in April, May and June. Although the most recent reports from manufacturing respondents indicate that employment levels are stabilizing, the manufacturing sector was responsible for most of the decline in nonagricultural employment. Construction employment also fell in the second quarter; however, housing permits and the value of nonresidential contract awards remained at high levels.

Despite the sluggish employment performance, the New England unemployment rate fell to 3.3 percent in June. Help-wanted advertising in June was far above the levels in June 1986 and earlier in 1987. Advertising picked up in the Providence area, in particular.

SECOND DISTRICT--NEW YORK

Economic activity in the Second District continued to vary among sectors in recent weeks. General business conditions improved somewhat further, and office leasing was fairly good. Homebuilding activity displayed a mixed pattern, however, and July spending at some retailers was below plan. On the financial side, small and mid-sized banks expect only a mild increase in inflation over the near term.

Consumer Spending

District retailers reported some slowing in sales during July. Our respondents registered over-the-year gains of 2 to 8 percent compared with increases of 3 to 13 percent in June. As a result, July sales generally were somewhat below plan. However, one chain with overall sales below target reported that results in the District were 2 percent higher than expected. Retailers were optimistic about the fall and back to school season, noting that the softening in July was the first in several months. One firm attributed its July slowdown in part to a shortage of summer merchandise that resulted from a successful promotional held at the start of the season.

Due to the somewhat disappointing sales gains in July, retailers reported inventories at higher levels than planned. An exception was the firm with a shortage of summer merchandise. None of the respondents reported inventories at uncomfortable levels, however.

Business Activity

General business conditions in the Second District improved somewhat further in recent weeks. The percentage of Buffalo purchasing agents reporting improved or stable conditions rose in July while in Rochester, for the third consecutive month, there were no reports of worsened business conditions. Inventories were down somewhat but remain at comfortable levels.

Unemployment rates moved lower in both New York and New Jersey during July to 4.4 percent and 4.0 percent, respectively. Rates in most of the District's labor market areas are below the national average and in several instances have declined sharply since last year. In Elmira, for example, where some new plants have opened, the unemployment rate dropped from 6.1 percent to 3.6 percent over the year ended in June (latest data), while in Buffalo, the rate fell from 6.9 percent to 5.0 percent over the same period as 20,000 new jobs were added. The rebuilding of the Fort Drum military post now underway in northern New York State is providing a stimulus to Syracuse and several depressed economies in the upstate area.

Construction and Real Estate

District residential construction activity presented a mixed pattern in recent weeks. In the downstate and New Jersey markets some further slowing has occurred, and homebuilders report little traffic by prospective buyers in their areas. Most pent-up demand has already been satisfied, and high land and home prices tend to be deterrents. Upstate, however, builders remain quite busy completing existing contracts, and some areas report strong interest in future contracts. Home prices in these areas have either held steady or risen only moderately. Overall, starts in the District in 1987 are now expected to be down somewhat from last year's level.

Office leasing activity has been fairly good in much of the District, and in New York City, where the vacancy rate is already relatively low, a pickup has recently occurred in commitments for space in some new buildings. However, vacancy rates remain at 20 percent or above in areas such as Westchester and Fairfield counties and northern New Jersey. While office construction has virtually halted in Westchester, new buildings continue to come on line in Fairfield and New Jersey.

Financial Developments

Senior officers at small and mid-sized banks in the Second District reported expectations of only a mild increase in inflation in the near future. Rising oil prices, due to political unrest in the Middle East, and the falling dollar were the factors most commonly cited as likely to lead to an acceleration of the inflation rate. Expectations of higher inflation were tempered, however, by a widespread belief that Chairman Greenspan would pursue a strong, anti-inflationary, monetary policy. Reflecting their anticipation of a modest increase in inflation, the officers believe that interest rates will show only a slight rise, if any, by the end of the year. Most of these bankers expressed hesitancy to raise their interest rates any higher this year unless the money center banks initiate such a move.

THIRD DISTRICT - PHILADELPHIA

The Third District economy is showing signs of moderate expansion in August. Manufacturing activity expanded and factory employment has increased for the second month in a row. While reports from retailers vary, most are satisfied with the year-over-year gains they have achieved this summer, and auto sales, although down from last year, have picked up in recent weeks. Commercial bankers indicate that business and real estate lending is growing, but consumer lending has slowed recently. Realtors say commercial markets are generally healthy but residential sales have declined as fewer houses are coming on the market. Both residential and nonresidential construction are slowing from the substantial pace set in the last few years.

The outlook in the Third District business community is for further modest growth. Manufacturers expect expanding activity, although they are not planning major increases in payrolls. Retailers are cautiously optimistic for fall. Commercial bank credit officers foresee steady growth in business lending but expect consumer loan volume to remain relatively flat. Commercial realtors believe the new office space coming on line in the next few years will be absorbed without seriously weakening the market.

MANUFACTURING

The region's industrial sector is making gains, according to the latest Business Outlook Survey. Nearly 39 percent of the local manufacturers polled in August reported that business picked up from July, only 7 percent noted a slowdown, and 55 percent said they were operating at a steady pace. Durable goods producers and nondurables goods makers reported similar business conditions.

Most measures of industrial activity were giving positive readings in August. New orders and shipments rose, and delivery times increased fractionally for the first time this year. Employment posted another gain in August, building on July's increase. Although 79 percent of the companies reported steady payrolls, 17 percent added workers, while only 4 percent made cuts. Local manufacturers' order backlogs did not share in the general improvement, however, remaining virtually unchanged from July, overall. On the price front, most of the August survey participants are holding the line for their own products; and, although 37 percent say prices for purchased goods have gone up since July, 61 percent reported no change.

Looking ahead, local manufacturers have mostly positive views. Forty-two percent of the August survey respondents predict improvement over the next six months, 39 percent expect steady conditions, and 20 percent anticipate a slowdown. On balance, area industrial companies foresee increases in orders and shipments, but they do not expect order backlogs to grow; and, despite recent gains in employment, survey respondents are not planning for further significant changes in payrolls. With regard to prices, nearly two-thirds of the respondents predict a further rise in input costs over the next six months, while only about one-third plan to raise the prices of the goods they make.

RETAIL

Sales reports from Third District retailers in late August varied from "extraordinarily good" to "below plan," although few merchants expressed disappointment with results for the summer as a whole. Most product lines are performing well, but store officials say the late date for Labor Day this year appears to be delaying back-to-school purchases. Store officials say they are guardedly optimistic for the balance of the year, and most will enter the fall

with relatively lean inventories. They expect consumers to put off Christmas shopping until late, a practice that has taken hold in recent years.

Automobile dealers say sales for the year so far are below last year's pace, with the exception of a few popular models; but increases in gross revenue (total sales less cost of cars) have helped to keep dealer net profits from slipping as much as unit sales. Sales have picked up in recent weeks in response to the latest round of manufacturers' financing incentives.

FINANCE

Loan growth at major Third District banks continues to moderate. Growth has been slowing since February, and in early August total volume outstanding was approximately 7 percent above the year-ago level. Real estate lending remains strong, but growth in commercial and industrial lending has been moderating, and consumer lending has actually declined. Personal loan volume outstanding in the first week of August was nearly 2 percent below the peak level in May. Bank lending officers say consumer installment lending, in particular, has been declining.

Commercial bank credit officers expect business lending to grow moderately over the next few months, and some believe faster growth is likely with improving conditions for the region's manufacturers. All are in agreement, however, that competition in middle market lending is strong and that net interest margins will remain under pressure as more regional banks focus on this market and reduce their participation in loans to larger borrowers in the national market. For consumer lending, there is a consensus that little growth can be expected; bankers generally believe consumers will bring their spending into line with personal income and make fewer credit purchases in the near future.

REAL ESTATE AND CONSTRUCTION

Although commercial construction in Delaware is declining sharply as the state's recent office building boom passes its peak, commercial construction and leasing is healthy in most parts of the Third District. Several new office buildings have been completed in the Philadelphia central business district this year and more are scheduled for completion over the next three years. Realtors say the new buildings are being leased relatively easily. Older buildings, however, are losing tenants at a rate that slightly more than offsets increases in occupancy of new buildings, resulting in a small increase in the total office vacancy rate. Nevertheless, most realtors believe the new space coming on the market in the next three years will be readily absorbed and that overall vacancy rates will not rise to glut proportions.

In Third District suburban areas office vacancy rates are stable or declining as leasing activity picks up and construction slows down. Following on office and residential development in the suburbs, hotel and retail space is now in demand. Realtors say recent and prospective completions of major highway links in the suburbs are boosting interest in all types of commercial real estate in these areas.

Contractors in some parts of the Third District say housing starts have fallen due to labor shortages, with the number of skilled framers, carpenters, and construction superintendents in particular falling short of demand. Residential building permits have been declining in Pennsylvania and New Jersey, but have risen substantially in Delaware. Residential realtors say sales of both new and existing homes are tapering off as fewer houses in both categories are being put on the market. They report that selling prices continue to rise.

FOURTH DISTRICT - CLEVELAND

Summary

Economic activity in the Fourth District has slowed slightly from the last report. The annual employment growth rate in Ohio has tapered off, although the unemployment rate is lower due to a reduction in the labor force estimates. The Ohio Manufacturing Index is lower in June than a year ago, reflecting primarily a decline in durable manufacturing employment. Retail sales are up as factory financing incentives have stimulated automobile sales.

Retail Sales

District retailers reported slightly stronger sales in July and August than in previous months. Sales increases occurred in a broad range of items with increases in the sale of soft goods, such as apparel, outpacing hard goods, such as appliances. However, both categories of sales are reported to be weaker than sales a year ago. Retailers expect price increases to remain modest over the near term.

The latest factory financing incentives have helped to reduce local domestic automobile inventories in order to make room for next year's models. Import dealers have also resorted to financing incentives in order to reduce inventories.

Labor Markets

Ohio's unemployment rate dropped from 7.9 percent in May to 7.2 percent in June. Much of this reduction is attributable to a 1.1 percent decrease in labor force participation during this period. Total

employment also fell slightly, with 19,000 fewer jobholders in June. Most of the job loss occurred in manufacturing, primarily durables. Employment in nonmanufacturing divisions rose slightly from May to June, with services leading the increase.

Annual employment changes continue to differ significantly among the major metropolitan areas in the Fourth District: Cincinnati, Cleveland, Columbus, and Pittsburgh. Columbus registered the largest annual percentage increase in total employment in June with a 4.2 percent increase. Pittsburgh experienced the smallest increase at 1.6 percent. Furthermore, Pittsburgh has continually lost total employment since the last business cycle peak, while Cincinnati and Columbus have increased employment by 13 percent and 18 percent, respectively. Cleveland's total employment is virtually the same as it was at the peak.

Manufacturing

The Ohio Manufacturing Index fell in June to an annual percentage decrease of 0.2 percent. Transportation equipment and primary metals registered the largest declines among the major 2-digit industries. Further declines in these sectors are expected as General Motors is scheduled to close several large assembly plants in the area. On the other hand, electrical and nonelectrical machinery posted modest gains over this same period. Nondurable manufacturing also exhibited slight increases.

The steel industry has been helped recently by firm steel prices, particularly in speciality steels. LTV has recently announced plans to increase prices for hot rolled carbon bar and wire products. However,

regional output and employment has remained steady over the last few months.

Housing

Contracting for new construction rose slightly in July. Increases were reported in single-family homes and commercial and industrial building in many areas across the district. Although mortgage rates have inched up in recent months, they remain among the lowest in the nation. For example, in the Cleveland area, average rates for 30-year fixed-rate mortgages stand at 10.09 percent.

Banking

District loan demand continues to be soft. Total loans outstanding at large banks fell at an annual rate of 7 percent from the beginning of July to mid-August. Commercial and industrial loans, which declined at an annual pace of over 20 percent, accounted for nearly all of the loan reduction. Real estate lending has been flat as mortgage rates have generally drifted upwards. In contrast, home equity lending continued to increase at a rapid pace and traditional consumer installment lending has picked up somewhat, after being essentially flat during June.

FIFTH DISTRICT - RICHMOND

Overview

The District economy continued to expand in August, although agriculture suffered from the weather and growth was sluggish in some service-related sectors. Employment rose and labor markets remained tight in much of the region. Manufacturing activity accelerated in August, but retail sales and port activity were generally unchanged. Bankers report that the demand for nonresidential construction loans declined over the summer. Respondents to our regular surveys of business and financial conditions remain optimistic that the economy will improve in the months ahead.

Consumer Spending

Retail activity in August was generally flat according to our most recent mail survey. Retailers report little change in their total sales, but an increase in sales of big ticket items in mid-August as compared with late July.

Retailers continue to expect higher sales in the next six months, but the proportion of those expecting rising sales declined since our previous survey. Forty-two percent of the respondents predict increased sales in the next six months, while the remainder are evenly divided between those predicting lower sales and no change in sales. By comparison, 60 percent of the July respondents had expected increases in sales. Thirty-five percent of the respondents described their inventory levels as "too high" and 48 percent said they were "just right." Nearly

60 percent of the respondents believe that prices for the items they buy will rise in the next six months.

Manufacturing

The pace of manufacturing activity increased in August according to our survey. Half of the respondents reported increased shipments in August, as compared with 37 percent who cited upturns in July. Stronger growth was also indicated by reports of increases in new orders, backlogs of orders, and the workweek. Manufacturers continue to indicate increases in the prices of both raw materials and finished products. Inventories of materials rose slightly, while finished goods inventories were generally unchanged. About two-fifths of the respondents described their inventory levels as "too high," while another two-fifths considered theirs to be "just right."

The proportion of manufacturing respondents expecting growth in activity increased since our July survey. Fifty-seven percent of the August respondents expect shipments to rise in the next six months, compared with 46 percent of the July respondents. Also, 38 percent of the August respondents predict increases in their capital expenditures in coming months, as compared with 31 percent of the July respondents.

Labor Markets

Manufacturers and retailers responding to our surveys report tightness in their labor markets. Employment rose in both manufacturing and retailing in August, but thirty-nine percent of the manufacturing respondents and 52 percent of the retail respondents say they have job openings that remain unfilled.

Port Activity

Import and export volumes at the major ports in the District were generally unchanged in August from July. However, port representatives expect shipping activity to increase in the next six months.

Agriculture

The summer's hot, dry weather caused substantial damage to some District crops. Corn yields were hardest hit, tobacco and peanut yields were marginally affected, and the soybean crop remains at risk. There have also been several reports of heat stress on poultry flocks and dairy herds. Recent scattered rainfall and cooler temperatures should limit further losses.

Two District states have asked the federal government to designate some of their drought-stricken counties as disaster areas, and other states are in the process of doing so. Such designations would allow some farmers to be eligible for federal disaster relief payments.

Financial

A survey of large banks across the District indicates that the demand for nonresidential construction loans has slackened compared with demand earlier in the summer. Some respondents attribute the downturn to seasonal factors, and they are optimistic that activity will increase after Labor Day.

Large banks in the District expect interest rates to be stable on intermediate-term loans through the next 90 days, but they predict higher rates for loans of longer duration, such as mortgages.

SIXTH DISTRICT - ATLANTA

The pace of southeastern economic activity remains brisk in most sectors at the end of the summer. Employment in key regional industries continues to expand; residential construction activity has picked up, and office vacancy rates are expected to drop in some major regional markets. Although retailers' sales have slowed recently, recent dealer incentives have boosted auto sales. Port activity is benefiting from the weak dollar, and tourism has been strong throughout the region. Crop yields and profits are expected to outpace last year's drought-reduced levels.

Employment and Industry. The service sector continues to add employment in the Sixth District. Health services and business services such as equipment renting, management consulting, and computer services have shown strong growth lately. Contacts indicate that factory employment growth is likely to continue to increase. Textile employment has grown briskly, and demand remains strong for the region's textile products. Shipments of carpet from some mills are being delayed because producers have not been able to hire enough workers to keep up with the large number of orders.

Concentration on narrow, localized market niches has reduced import vulnerability of regional steel producers. Small mills have been adding to capacity and boosting productivity with improved technology. Lumber industry spokesmen are concerned about the multifamily building slowdown and the rise in mortgage interest rates; however, the tariff on Canadian lumber has helped to curb the tide of imports. Also, the surge in lumber use for home remodeling is helping to support the market.

Consumer Spending. August's retail sales showed only slight gains from a year ago in spite of good performance a month earlier. Retailers are heavily promoting back-to-school items. They say that apparel sales continue strong; however, there is little growth in other items. For the most part, inventories remain at comfortable levels although there are scattered reports that the stock of summer apparel remains heavy for

late August. Retailers project sales for the coming months to be at or only slightly above last year's level.

Early August car sales in the District were boosted by new factory incentives featuring finance rates as low as 1.9 percent and generous cash rebates on 1987 models. Industry contacts reported a strong market response, particularly for some GM cars and trucks for which sales had been especially weak. Despite the sluggish sales of domestic autos, the District's new vehicle registrations in the first half of 1987 were off only 0.7 percent from last year, much less than the 7.9 percent drop nationally.

Construction. Although the spring uptick in interest rates caused a dip in existing home sales in June, sales for the second quarter finished well ahead of last year's pace. All the District states except Alabama bettered the national average of 5.7 percent growth. District realtors say pockets of activity in the region, like the Florida Gulf Coast, Jackson, Mississippi, and middle Tennessee, are fueling the growth.

The Sixth District is attracting an increasing portion of foreign investment in U.S. commercial real estate. In both Atlanta and Miami, 18 percent of downtown commercial properties are owned by foreign investors, and this rate is expected to increase. Although no upward pressure in prices has yet occurred, the slowdown in construction in these overbuilt markets, coupled with the rising demand of foreign investors, is expected to increase prices, say contacts in these cities. Contacts in almost all District metropolitan areas expect increased foreign investment in the near future.

Office leasing in Miami is strong although vacancy rates are still high. Contacts there say they expect a 30 percent increase in leasing this year over last. Sales and leasing of industrial property in Atlanta remain very active, and the vacancy rate in the second quarter was again below the national average.

Financial Services. Loan growth at the larger commercial banks in the Sixth District continued to decline in July. Business, real estate, and consumer loans are all

expanding at a reduced pace. Many banks, searching for lending alternatives, have begun to reemphasize home lending.

Tourism. Tourism continues its strong summer performance throughout the District. Florida campgrounds are reporting another good year. Hotel occupancy along the Mississippi Gulf Coast has been increasing, a sign that tourism is reviving in that area.

Port Activity. The share of exports in the trade mix of southeastern ports is gradually rising in response to the lower dollar. The value of exports was up 3.3 percent during the year ending in June, slightly surpassing the rate of increase for imports. All District ports except New Orleans posted trade gains during the period. In Savannah, port officials expect that demand for Georgia products such as kaolin, fertilizers, and pulp and paper will continue to grow in the year ahead. In Miami, where higher shipments to Latin America have revived exports, the outlook also is bright. In Mobile, increased forest products exports have helped to offset lower coal shipments.

Mining. In August the number of operating oil rigs declined modestly but still remained one-third higher than a year ago. However, production of crude oil remained at about 5 percent less than in August 1986. District refineries report falling profit margins in recent weeks as crude oil prices rose faster than product prices.

Agriculture and Forestry. Southern pine lumber, which accounts for 10 percent of the nation's total lumber exports, experienced a favorable spring with exports over 10 percent higher than last year. Demand for southern pine remains strong at relatively high prices.

Yields of major crops in the region are expected to be much higher than last year's drought-reduced harvests. Production will be up despite reduced acreages this year. With prices and costs near those of a year ago, profit per acre should also improve moderately.

SEVENTH DISTRICT--CHICAGO

Summary. Business activity continues to rise in the Seventh District, and further expansion is expected. Total employment growth in the five District states, seasonally adjusted, about matched that in the U.S. during this year's first half. Chicago area help-wanted ads in the first half were well ahead of a year earlier. Reports from this bank's directors in August, overall, were the most optimistic since at least the early 1980s. District purchasing managers see continued strong expansion. In contrast, auto sales have remained persistently below last year, and resulting production cuts and layoffs are particularly affecting industrial activity in southeast Michigan. Purchases of machinery have been mixed. Steel demand remains vigorous. Nonresidential construction activity, overall, appears about even with last year in the District, but has slowed in some areas. Residential construction and resales have slowed. Large District retail chain stores indicate only small gains in July sales compared with last year.

Purchasing Managers. Reports from Chicago and Milwaukee purchasing managers for July show strong gains in production, orders, and backlogs, lengthening lead times, and rising prices. Suppliers are increasingly able to make announced price increases "stick." Reports from Chicago purchasers in the first half of August indicate another strong month, with orders up sharply.

Motor Vehicles. Temporary and indefinite auto production cutbacks and layoffs, in response to continued slower sales, are having wider effects in parts of the District where the industry is heavily concentrated, particularly southeast Michigan. This slowdown is partly offset by increased demand for trucks, including both light models bought partly by consumers and larger trucks. Although Michigan manufacturing employment in June was 3 percent below a year earlier, the only District state to show a decline over this

period, nonmanufacturing employment there was 4 percent higher, a larger gain than for the U.S. or the District as a whole. Lower Michigan factory employment in the latest year mainly reflects auto industry and related cuts. Sharply lower auto production in July reduced high inventory levels closer to normal levels. Model year-end cut-rate financing and rebates are expected to cut stocks further, though reports indicate that consumer response has been restrained. A major uncertainty overhanging District auto makers is the outcome of labor negotiations currently underway at GM and Ford.

Machinery. Markets are mixed for types of machinery with substantial production in the District. Demand for diesel engines for use in trucks is strong. Shipments of truck trailers have increased. Orders have risen for diesels used in some other industrial applications. Orders for railroad engines, however, are almost nil. Buying of railcars is up, but still low. A steel producer reports higher demand from makers of construction equipment and pressure vessels used in chemical process industries. Machine tool buying is weak, but an industry source views an upturn as imminent. Production of parts, shifted abroad when the dollar strengthened in the first half of the 1980s, is being brought back to the U.S.

Farm Equipment. Unit sales of farm equipment remain sluggish, although concessional terms to cut inventories strengthened tractor sales this summer. Unit sales of farm tractors were 32 percent above the very low year-earlier level in July, mostly reflecting inventory paring efforts by a major District manufacturer. August sales are also expected to show a large gain as another manufacturer introducing a new line is offering discounts of up to 50 percent on a large inventory of old models.

Steel. District sheet steel production continues strong. A contact expressed concern about possible future shortages of some types of sheet steel. Demand for structurals and bars remains at a high level. Plate is on allocation, reflecting improved demand as well as capacity shut down when the

market was soft. In response, a large Chicago-area plate mill is being restarted. Inventory rebuilding has been an important element in the strength of steel markets this year, following the six-month work stoppage at USX. However, analysts disagree on the relative importance of restocking versus improved final sales in the upturn in steel. Demand has improved from various steel users. The fall in the dollar has made domestic steel competitive with Japanese and European steel not only in U.S. markets but also abroad, though American exports of steel are restrained by trade barriers.

Nonresidential Construction. Work on new office buildings remains vigorous in downtown Chicago, and more announcements of new buildings are expected. Several hotels are underway or planned. Commercial building activity in suburban areas has slowed considerably over the past year. Heavy August rains and flooding delayed projects. A \$225 million steel mill will be built in Indiana, the state's second major new mill announced in the past year.

Residential Sales and Construction. Markets for new homes and resales in the District slowed in response to the jump in mortgage interest rates in the second quarter. Most reports indicate that activity continues slower. Construction of houses is expected to be at a good level for the year, but below 1986. Multifamily construction has fallen sharply due to adverse effects of last year's tax law changes. The inventory of houses for sale is low, suggesting that resales will continue below strong 1986. Chicago area housing prices are estimated to be 10-12 percent higher than a year ago.

Consumer Spending. Large District retailers report small increases in the dollar volume of sales in July, compared with a year earlier. Weakness continued in early August. A survey of Illinois department and specialty stores showed moderately higher July sales than a year earlier, but smaller gains than earlier this year. The late Labor Day is expected to shift sales from August to September.

EIGHTH DISTRICT - ST. LOUIS

Summary

The District's economy weakened in recent months as employment and construction growth slowed. Agricultural conditions, however, have been positive as good weather has resulted in large yields of major crops. Livestock producers have enjoyed a profitable year with low feed costs and favorable prices.

Outlook

The outlook of small District businesses has improved. Only 7 percent of 211 businesses surveyed in July expected a worsening of national economic conditions in the following 6 months. This represents a substantial drop from the 17 percent anticipating deteriorating conditions in an April survey.

Employment

District nonfarm employment declined at a 1.0 percent rate in the second quarter compared with a 2.3 percent national rate of increase. The second quarter slowdown of District nonfarm employment was due to declines in the mining, manufacturing and construction sectors and sluggish growth of the service-producing sectors.

Manufacturing

Manufacturing employment dropped 3.5 percent in the second quarter, returning to the level of a year earlier. Employment in most major industries has continued to decline, with only producers of

electrical equipment, food products and textiles and apparel posting job increases compared with a year earlier. Regional textile plants, particularly those producing cotton products, are running at near full capacity and have a substantial backlog of orders. Textile prices reportedly have increased this year due to high consumer demand for apparel and to rising costs of inputs, particularly petroleum products and cotton. Plants making footwear in the region are operating near capacity. The permanent closure of an aging truck plant in St. Louis recently eliminated over 2,000 jobs. Due to poor car sales, 2,700 workers will be laid-off in October from an auto assembly plant in the St. Louis area.

Construction and Real Estate

Regional construction activity slowed recently as the nonresidential sector weakened. The seasonally-adjusted value of District nonresidential building contracts grew by 3.5 percent in the three months through July, following a 15.3 percent gain in the previous three months. Much of the slowdown was in Arkansas. Despite the recent deceleration, District nonresidential contracts were 35.8 percent above a year earlier.

Regional residential building continued to decline. The value of District residential contracts fell by 8.4 percent in the three months through July. Losses were concentrated in Missouri and Tennessee. Although weak recently, District residential contracts were up 7.1 percent in the May-July period compared with the same period a year earlier due to strong single-family building. A slight decline in residential building was posted nationally during the same period.

The office vacancy rate in the St. Louis metropolitan area increased to 16.4 percent in June from 13.6 percent a year before, but remained about 4 percentage points below the national metropolitan average. Area vacancy rates are expected to rise by the end of 1987 as a large volume of office space is completed. St. Louis' industrial vacancy rate of 5.4 percent was slightly below the 6.1 percent national average in June and down from 6.7 percent in June 1986.

Agriculture

The crop year has been extremely favorable for most District farmers. Harvests of major crops have begun amid predictions of record corn and soybean yields. The cotton harvest began a month earlier than normal due to early planting. The only potential hazard remaining is overly wet harvest conditions. The combination of low-priced feed and favorable prices for hogs and cattle also has allowed livestock producers to enjoy a profitable year.

Due to reduced acreage, large government payments to farmers, and lenders' restraint, the volume of farm loans outstanding at District commercial banks in June fell by over 15 percent from last year. The largest decline occurred in Kentucky where farm loans were off by 30 percent. Farm loan delinquencies and farm loan losses at agricultural banks improved in District states with the exception of Mississippi.

NINTH DISTRICT - MINNEAPOLIS

Economic growth in the Ninth District continues apace. Labor market indicators point to favorable employment conditions. While consumer spending didn't strengthen generally, tourist spending did. Mining activity has picked up, and improved agricultural conditions are likely to lead to higher farm income.

Employment

Ninth District labor markets have continued to create good employment opportunities. In Minnesota, the district's most populous state, employment grew strongly in July, with all sectors posting growth, including manufacturing. The employment growth drove down the state's unemployment rate two-tenths of a percent, to five percent in July--its first decline since April. Employment conditions were particularly favorable in the Minneapolis-St. Paul metro area, where the help-wanted advertising index rose about 31 percent higher this June than last. In Montana the unemployment rate has been projected to hold steady at 6 percent in July, although the drop in seasonal employment may be sharper than usual. In North Dakota, construction jobs were the biggest contributor to higher employment, according to recent data. A Bank director reports that labor markets in eastern South Dakota are so tight that the shortage of workers may deter some firms from locating there. And another director notes that the construction and operation of two new state prisons are projected to markedly increase employment in the Upper Peninsula of Michigan.

Consumer Spending

Reports on retail spending for general merchandise have been mixed. One retail chain complained of high markdowns to sell off summer

merchandise; as a result, its July sales were lower than planned. But another chain reports that its July sales were stronger than a year earlier, particularly in the Minneapolis-St.Paul area. Elsewhere in the district, a discount chain is opening a few stores. A Bank director notes that the sales volume of retailers in a large mall in La Crosse, Wisconsin, were over 7 percent higher this year than last.

Sales incentives have increased purchases of motor vehicles recently. One domestic manufacturer reports that its district sales have been strong, with both car and truck sales up over 15 percent in August and its inventories down. Another domestic manufacturer reports that consumer response to its incentives has been brisk, and that increased farm income should help rural sales this fall. A director notes that in western Wisconsin some car dealers, who had been doing poorly, have recently been doing better.

Scattered reports indicate that district housing activity has been mixed. Home sales in Minneapolis were 4.7 percent lower in July than a year earlier, and single-family housing permits in Minneapolis-St.Paul were off a bit in June. But in other parts of the district, housing activity may be picking up. In North Dakota a newspaper editor reports that new home construction is booming in Fargo, while a business representative in Williston, notes that a glutted housing market has recently improved there. A director reports that orders for telephones were up lately, indicative of new home construction.

Tourism

The district's large tourism industry has continued to enjoy excellent summer business. An industry spokesman in Minnesota reports that business this year is far beyond projections. Inquiries at Minnesota's State Tourism Office are up 36 percent over last year. Industry representatives for

the Black Hills of South Dakota note that this year was very good, and new tourist projects there are now underway. Tourist trade has also been flourishing in western North Dakota. In the Indianhead region of northwestern Wisconsin, campgrounds and resorts have been full. And the best tourism conditions in six years have been reported from Michigan's Upper Peninsula. Most areas are projecting good fall business as well.

Resource-Related Industries

Some good news is evident in the district's resource-related industries. Signs of increased interest in oil exploration were mentioned by observers in western North Dakota and in Montana. Gold mining has been active in South Dakota and Montana. The country's first platinum/palladium mine, employing over 200 workers, was recently dedicated in rural Montana. The port of Duluth reports a big increase in the amount of coal and iron ore shipped through to U.S. and Canadian destinations this year.

Agriculture

Agricultural conditions have continued to improve. Higher livestock prices and profits are causing euphoria among raisers, according to a Bank director from South Dakota. A director from Montana notes that calf prices are also high and that Montana wheat producers are benefiting from a big crop and price supports. Record soybean yields are expected in Minnesota. Plans for an egg-laying facility holding one million hens were just announced in South Dakota. Wet weather is a concern to farmers in some parts of North Dakota, though.

TENTH DISTRICT - KANSAS CITY

Overview. Some modest improvement is apparent in Tenth District economic activity. Overall retail sales are growing slightly and new car sales are somewhat stronger. Manufacturers' purchasing agents report further price increases for inputs but materials generally remain readily available. Some limited improvement has occurred in oil exploration and development activity. Little strength is present in the housing sector. Loan demand at district banks has weakened recently. Fall crop yields are expected to be generally above average. Little expansion is evident in the livestock sector.

Retail Sales. A majority of respondents report sales above year-ago levels. Most also report growing sales over the past three months, though a few report constant or declining activity. Prices have been generally stable over the past three months. About half of the retailers surveyed report increasing inventories, while the rest report stable stocks. Expectations of future inventory change are also mixed. Most respondents expect stronger sales ahead.

Automobile Sales. Automobile dealers generally report that sales are steady to slightly stronger in August. Inventories are trim as dealers await 1988 models. Adequate financing is available for both dealer inventories and customer purchases. Dealers are hopeful that sales will be stable to up slightly during the remainder of 1987.

Purchasing Agents. Purchasing agents report that prices have generally increased over a year ago, with the greatest increases occurring in oil derivatives such as plastics and in textile inputs such as cotton cloth. Most respondents expect increases to level off in the next quarter. Materials are generally readily available and few problems are expected for the remainder of the year. Inventory levels are generally satisfactory with some trimming and

seasonal adjustments being made. Many agents report that plants are running near capacity.

Energy. After tensions in the Persian Gulf pushed domestic spot prices into the \$20-\$22 range, reports that OPEC has been producing in excess of its quota have sent domestic prices back down to the \$18-\$20 range. This volatility will likely prevent a strong rebound in the district's energy industry in the near future. But some limited improvement in exploration and development activity has been observed. The average weekly number of operating drilling rigs in the Tenth District increased from 232 in June to 273 in July, 45 percent above the year-ago level. Nevertheless, the rig count in the district remains less than one-fifth of its 1982 peak.

Housing Activity and Finance. District homebuilders report that housing starts remain at or above last year's levels, but generally down from a month ago. Single-family home construction remains stronger than multi-family construction. Looking ahead, homebuilders expect housing starts to stabilize. Most homebuilders report that new home sales are up and inventories are down, with house prices rising at about the rate of inflation. Builders have had no problems with materials availability and they expect none in the foreseeable future.

Deposit growth at Tenth District savings institutions is reported down from a year ago. However, there has been a recent slight improvement in savings inflows. Demand for mortgage funds has been slow and is expected to remain steady or improve somewhat during the remainder of 1987. Mortgage rates, which have been steady to firming recently, are generally expected to remain steady or increase slightly during the rest of 1987.

Banking. Respondents report that total loan demand fell slightly at Tenth District banks during the past month. Demand weakened slightly for

commercial and industrial, consumer, and residential real estate loans. Demand fell off more sharply for commercial real estate loans, while demand for agricultural loans held steady. Respondents report no change in their prime rates, and virtually none expect any change in the near term. No changes in consumer loan rates were reported, and, again, no changes are expected. Balances in all types of deposit accounts generally remained constant, though there are scattered reports of changes, both up and down.

Agriculture. Fall crops are doing well across most of the Tenth District as the harvest approaches. Good moisture and warm weather combined for an excellent growing season, and corn, milo and soybean yields are expected to be above average in many parts of the district. In parts of mid-Missouri where the corn harvest has already begun, yields up to 30 percent above normal have been reported. The expectation of exceptional yields has created some concern about storage capacity around the district. Although most areas report adequate storage, some limited storage expansion is underway. In other areas, harvested crops may have to be put on the market as storage facilities are filled.

There are a few signs of limited expansion in hog inventories in Kansas and Nebraska. However, most operators in the district are not expanding, afraid that currently high hog prices will not hold. Similarly, there has been little or no expansion in district cattle herds, though cattle prices remain relatively strong. Many district feedlots are currently running well below capacity, in anticipation of a large seasonal influx of feeder cattle this fall.

ELEVENTH DISTRICT—DALLAS

The District economy is growing very slowly. Manufacturing activity is stable or increasing in most industries. Drilling continues to turn up. Construction values have been showing gains. Retail sales remain fairly flat, but some respondents note increases. There has been essentially no deposit growth at the commercial banks in the Eleventh District during the last three quarters. Farm prices are up from a year earlier and agricultural credit conditions are improving.

District manufacturers indicate that, overall, business conditions have improved very modestly in recent months. Orders to apparel producers have increased significantly, as retailers have begun to shift from foreign to domestic suppliers. Refiners note that their output remains strong, but that profit margins are slim. Chemical manufacturers say that orders to them are strong, considering normal seasonal weakness, and express a favorable outlook for the coming months. Sales by electrical and electronic equipment manufacturers have been fairly stable in recent months and remain above a year earlier. Defense contractors say output and prospects for new orders remain strong. Sales by producers of energy-related durable goods have lately remained unchanged, despite continued increases in drilling activity. Some manufacturers of durable goods tied to the construction industry report that orders are stabilizing at very low levels, while others report additional declines.

The District drilling rig count continues to climb. The rig count rose in July and held steady in the first half of August. Well permit applications, a leading indicator of drilling activity, also increased in July. Energy industry observers say that recent increases in drilling were not based on this summer's runup in oil prices and that the price declines in August are unlikely to induce drilling declines.

Indicators of District construction activity have lately shown gains. For the three months ended in July, the value of construction contracts was up 10.0 percent from the

first quarter. This expansion represents an increase from low levels, however, and contracts have grown only slightly over the depressed levels of a year earlier. These increases have occurred despite continued reductions in nonresidential building. The strength in contracts has been focused in non-building construction, a category that includes sewer and water lines and streets and roads. Residential contracts have also shown some growth over the last few months but remain below a year earlier. Nevertheless, both single-family and multifamily building permits have been declining lately. Construction employment is continuing to drop in response to past reductions in contracting.

District retailers report flat to slightly increased sales. Sales of home furnishings and of some appliances have picked up, after a protracted period of weakness. This increase is ascribed to growth in the proportion of homebuyers who are purchasing a residence for the first time. Sales of consumer electronics continue to fall, however, in response to rising prices tied to the declining value of the dollar. Most retailers expressed optimism about third quarter sales.

District auto sales are up in response to interest rate incentives offered by domestic manufacturers. Dealers say that domestic auto sales are also up because prices of domestic models have remained unchanged, while prices of foreign cars continue to climb. Concerns are widespread that sales may slow substantially after the financing incentives lapse at the end of September.

Conditions at the District's financial institutions continue to be sluggish. The deposit growth rate at thrift institutions continued to slow in July but remained positive. Regulatory capital at Texas thrifts decline from a positive \$3.4 billion in May 1986 to a negative \$2.1 billion in May 1987. There has been virtually no deposit expansion at District commercial banks during the last three quarters. In July, deposits were 1.7 percent lower than a year earlier. Large time deposits at District commercial

banks are declining at an increasing rate, but these reductions are being partially offset by increases in small time deposits. The legalization of limited branch banking in Texas in 1986 has led to reductions in the number of banks. The decline primarily represents mergers of subsidiary banks of multibank holding companies into a single bank with a branch network.

In District agriculture, product prices are substantially above a year earlier and farm credit problems are diminishing. Profit margins in livestock operations are wide, as a result of low feed prices and increased livestock prices. Reduced output by foreign producers, together with renewed consumer demand for cotton products, has put upward pressure on cotton prices. A warm September will be needed to protect the West Texas cotton crop, much of which was replanted in June after heavy rains and hail destroyed previous seedings. In July 1987, prices of all major District crops were above a year earlier, with the exception of potato prices. For the same period, prices for all components of the Texas Livestock and Livestock Products Index were above a year earlier, with the exceptions of broilers and eggs.

TWELFTH DISTRICT -- SAN FRANCISCO

Summary

Overall, economic activity in the Twelfth District continues at a healthy pace, although Alaska, Idaho, and Utah do not share in the current prosperity, and the pace of construction activity continues to weaken in many parts of the District. Consumer spending is steady, and high-technology manufacturing activity appears to be picking up. Lumber producers continue to enjoy strong prices and demand, while oil-producing regions are benefiting from recent price hikes. Construction activity continues mixed, among regions as well as among building types. Many financial institutions are experiencing substantial changes in their portfolio mixes, away from consumer credit and toward home equity loans.

Consumer Spending

Consumer spending patterns have not changed appreciably in most parts of the District during recent months, with most respondents describing overall sales as "flat" or "unchanged." Strength in car sales varies geographically, and within market areas sales generally are stronger among used cars and smaller cars, including Korean imports. In most areas, apparel, housewares, and small appliances are selling well. Shopping malls and department stores in southern California, Oregon, and Seattle report sales growth and express optimism regarding fall sales.

An Arizona survey suggests a broad-based decline in purchases and planned purchases of consumer durables in that state, consistent with the slowing pace of activity there. Consumer purchases since the last survey declined in most spending categories, but the proportion purchasing home appliances increased from 24 percent to 31 percent. The proportion planning to purchase automobiles during the next six months dropped from 42 percent of the respondents in July 1986 to 28 percent in July 1987, while the fraction planning to buy electronic products and tools dropped

from 43 percent to 33 percent. Declines of 10 to 15 percentage points also were reported for household furnishings and home improvements, with home appliances experiencing a smaller decline.

Manufacturing

The long-anticipated turnaround in the semiconductor and electronic equipment industries appears to be materializing at last but, in the words of one respondent, it is "a slow creep-out rather than a rapid turnaround." Orders and shipments are stronger overall, but increased demand currently is concentrated in computers and office equipment, communications, and instruments. One Portland-area firm has announced plans to double capacity at one of its plants, and another is re-examining old plans to build a new \$130 million silicon-wafer plant. Moreover, 17 percent of respondents to an Arizona survey planned increased capital spending, an improvement from recent quarters when virtually none planned spending increases. The same survey revealed that 57 percent of respondents expected to increase employment during the coming months, and the remaining 43 percent plan no changes. However, many firms are increasing production by utilizing existing plant capacity and labor resources, which has limited plant expansion and additional hiring. In addition, continued offshore migration of production, particularly of standard memory devices, is limiting U.S. gains.

Several respondents note that exports to both Europe and Japan have strengthened. A Washington banker argues that the improvement also is due to new product designs and redesigns of existing products reaching the production stage, and that continued improvement in this area depends critically on activity at large regional electronic and electrical equipment firms.

Agriculture and Resource Related Industries

Most Idaho lumber mills reported that they were operating at capacity, with 6 percent fewer employees than a year ago. Softwood lumber exports to Europe and

Japan for the first five months of 1987 were up 16 and 12 percent respectively from the same period in 1986, while log exports rose 11 percent. Exchange rate considerations, a surge in housing starts in Japan, and increases in log demand from China and Korea account for much of the improvement. Canadian lumber imports for the first five months of 1987 were 2.8 percent lower than they were in 1986.

Some oil equipment firms finally are operating "in the black," as the number of drilling rigs has been increasing for the last eight to nine weeks. In Kern County, the number of drilling rigs has increased during each of the last four months, and 51.5 percent of the rigs are working, compared with only 27.5 percent of rigs a year ago.

Construction and Real Estate

Construction activity in the Twelfth District continues to be mixed, with particularly weak activity in economically struggling areas, and multifamily construction weakening throughout the District. In California, the number of residential construction permits year-to-date through July stands 11.5 percent below last year's level, while the value of nonresidential construction awards for the first seven months of the year remains 14 percent above the year-earlier level despite deterioration during June and July. The number of housing permits and mortgages in the Seattle area has declined in recent months, and sales of both new and existing homes have fallen in eastern Washington. In Utah, total construction value for the first six months of the year was down 15.7 percent from last year's level, after June declines of 25 percent in the number of new single-family construction permits and 45 percent in nonresidential valuation.

Financial Sector

Declines in consumer loan volume and in credit card usage compared with last year were reported in most parts of the District, but were not universal. At a Washington bank, consumer loans outstanding advanced at over a 10 percent annual rate between April and July, following net paydowns in the first part of the year.

Moreover, an Arizona banker reports that credit card usage through the first seven months of the year rose 21 percent from the comparable period last year, and installment credit rose by 6.6 percent over the same period.

Many respondents attributed the general decline in consumer credit volumes to the new tax law, which eliminated consumer interest deductions, causing increased use of home equity loans and home equity lines of credit. An Oregon bank reports that credit card debt has grown only minimally, and auto loans have been flat, while the use of home equity credit lines has increased by 17 percent in the last year. There is little evidence that consumers are drawing down savings accounts to purchase durable goods. One large California bank reports that its passbook savings volume has advanced significantly since December. A community bank in the San Joaquin Valley also reports increases in savings account balances, while one Arizona bank reports that its savings account balances are up 15 percent. However, contradictory evidence comes from a southern California Savings and Loan, where savings inflows have been weak for the last seven months.