

SUMMARY OF COMMENTARY ON CURRENT ECONOMIC CONDITIONS

BY FEDERAL RESERVE DISTRICTS

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SUMMARY*

The economic recovery continues to be uneven across the country. Although some Districts apparently are not sharing in recovery, others, such as Chicago and Cleveland, continue to revive largely because of the upswing in manufacturing. Industrial production has provided considerable impetus to recovery, reflecting in part export demand and a reduced pace of inventory liquidation.

As yet, there is little sign of a sizable rebound in consumer spending that will contribute to a strengthening business recovery. Retail sales in recent months show only scattered improvement, and most retailers are cautious about sales prospects. Retail inventories are indicated to be close to desired levels.

Residential investment seems to have lost some upward momentum in recent months, with fewer than half of the Districts reporting further increases in housing sales and housing starts.

Hot, dry weather in much of the country has hampered farm output, especially corn. Bumper crops of rice in some parts of the St. Louis District and record crops of cotton are anticipated in St. Louis and Dallas. Farm commodity prices and livestock prices have declined recently (San Francisco, Minneapolis, Kansas City, and Dallas).

* Prepared at the Federal Reserve Bank of Cleveland and based on information obtained before September 9, 1991. This document summarizes comments received from business and other contacts outside the Federal Reserve and is not a commentary on the views of Federal Reserve officials.

Loan activity remains soft in most Districts. Chicago, Cleveland, Philadelphia, and St. Louis report a continued reduction in business loans, while mortgage loans in general remained flat.

Manufacturing

The strongest sector of the economy is manufacturing. Most Districts note a continuing upturn in activity in recent months, but manufacturing apparently is still languishing in a few Districts (especially Boston and San Francisco).

Export growth has been a source of strength in manufacturing, and more recently, a reduced pace of inventory liquidation in some industries reportedly is adding to the recovery. Developments are not uniform through all Districts, however. Some inventory liquidation apparently continues in Chicago, Philadelphia, and Richmond, while Boston reports satisfactory inventory levels and Cleveland comments that the correction phase in inventories is nearing an end.

Both Chicago and Cleveland note strengthening among consumer durable producers, led by rising automotive and appliance output, which has supported a gradual rise in steel production. Further increases in auto output are expected for next quarter (Cleveland). Capital goods industries are beginning to show signs of recovery. Chicago points out that electronics, heavy machinery, and food processing machinery have all shown some recent turnaround in orders, and Cleveland cites an uneven revival in heavy-duty trucks and industrial equipment. Dallas also reports that sales have increased in the electronics and electrical machinery industries because of some rebuilding of depleted inventories.

Retarding a comeback in production in some Districts is the cutback in defense contracts, resulting in declining orders in Philadelphia and Atlanta and in San Francisco's aerospace industry.

Manufacturers in most Districts appear to be more optimistic about near-term prospects, and those in Philadelphia and Richmond plan to increase their capital spending over the next six months.

Consumption

There is still little indication of a stepped-up pace in consumer spending for durable and nondurable goods. Retail sales between July and early September were relatively flat or slightly higher than their levels earlier in the summer. Sales of back-to-school merchandise were described as "weak," "slower-than-expected," or "disappointing" (Boston, New York, Philadelphia, Atlanta, and Dallas). New car sales in August were off in some Districts (Chicago, Cleveland, Atlanta), although a limited inventory of 1991 model cars is partly blamed for the reduced sales pace. Cleveland, however, expects a somewhat higher level of new car sales this quarter than last. In general, retail inventories appear to be close to desired levels.

Retailers generally are cautious about near-term sales prospects, and only a few of the Districts report optimism about the outlook.

Real Estate and Construction

District reports suggest that recovery in housing sales and starts has slowed recently, although a few Districts comment that sales or starts were still rising in July and August. Both San Francisco and Chicago report that home sales softened in recent months after a spring rebound. Still, housing

apparently has become more affordable because of recent easing in mortgage rates and because of lower home prices in some areas.

Commercial construction appears to be at a virtual standstill in many Districts. High vacancy rates for commercial buildings and declines in rental prices have been blamed (New York, Chicago, Minneapolis, Dallas, and San Francisco), but tight credit standards for acquisition and development loans have also apparently restricted commercial construction (New York, Chicago, Atlanta).

Agriculture

Dry weather is expected to reduce the corn yield in Kansas City, and early reports on this crop in the St. Louis District are mixed. Richmond expects that corn and soybean yields will be normal to above normal in some areas, because of recent timely rain. A bumper rice crop is expected in Arkansas, but yields in Mississippi may not be as good (St. Louis). A record harvest for cotton is expected (St. Louis and Dallas). Crop yields in Minneapolis are predicted to be "generally good."

Adverse weather has also affected pasture conditions in Kansas City, but the livestock industry is nevertheless "mostly good" in St. Louis. Fruit growers in California report large harvests, but dry August weather reduced the harvest of apples and grapes in Washington (San Francisco).

Several Districts report declines in farm commodity prices. Potato, hay, and beef prices are off substantially from a year ago in San Francisco, and

the Minnesota index of farm products fell sharply again for a variety of crops and livestock.

Banking

Nearly all of the Districts state that loan activity is relatively flat, or has eased further in recent months. The New York District's comment that banks are willing to expand loans but are facing reduced demand, seems to capture a theme common to several Districts. Demand for business loans continues to be weak, and has softened further in some Districts (Philadelphia, Cleveland, Chicago, St. Louis). In some Districts, consumer installment loans either fell or held steady, except in Atlanta, where some pickup occurred. Most Districts report either little demand for new mortgage loans or slight declines from previous months, and even some easing in mortgage refinancing (Cleveland). Some Districts find that credit standards have not changed in recent months (New York and Chicago), but Richmond notes a tightening for commercial loans and Atlanta cites a tightening for both auto dealer and commercial development loans. In several Districts, mortgage rates have eased recently.

FIRST DISTRICT-BOSTON

Economic activity in the First District has not improved noticeably. Most retailers report fairly flat sales in July and August compared to a year ago, but some experienced greater weakness or a deteriorating trend during this period. Although a majority of First District manufacturers surveyed express disappointment that sales and orders continue below year-ago levels, one-third see a glimmer of hope in incoming business. Nevertheless, most contacts expect no significant upturn in economic activity until the first or second quarter of 1992.

Retail

The majority of retail contacts report small increases or decreases for July and August compared to a year ago. However, two respondents experienced a deterioration of results for August compared to July, another saw double-digit declines throughout the summer months, and still another went out of business. Back-to-school and cold-weather clothing sales have been weak.

Several contacts indicate a concern about future earnings, given their expectations that continuing job losses will deter consumer spending. At best, they expect modest increases in sales in 1992. Contacts generally believe that their own success in paring down inventories will reduce the pressure to lower selling prices. However, they anticipate heightened competition as a result of discounting by weaker competitors and new market entrants. They note that it will be hard to reduce expenses further because they have already cut staffing from last year's levels, and because capital budgets are already

minimal. Other expenses--such as taxes, workers' compensation, insurance, and rents--are beyond their control.

Auto Sales

Automobile sales improved in August over previous months, but New England dealers attribute much of the improvement to seasonal factors. Sales are still below levels of a year ago. Although contacted dealers see a slight pickup in consumer confidence, stricter credit standards at banks have reportedly made financing car purchases more difficult. Lower interest rates have not sparked a substantial rise in consumer spending, according to the dealers.

Manufacturing

Reports from First District manufacturers are less uniformly gloomy than in the previous survey. At one-third of the respondents, shipments and orders are flat or up, by as much as 10 to 15 percent, from year-ago levels. Areas of relative strength include electronics, gas turbines, and consumer appliances. For the majority, however, sales and orders continue below late summer 1990 levels, with declines ranging to 20 percent. One-third of the contacts indicate that new business was practically nonexistent in August, that existing orders were cancelled or delayed, and that backlogs are dwindling. By contrast, another third saw a glimmer of hope in recent orders, possibly attributable to transitory causes, such the weather or customer inventory adjustments. Nevertheless, most contacts express disappointment that business does not match their expectations or the improvement reported by the media. Foreign sales are also reported mixed and somewhat disappointing. Inventory levels are generally described as satisfactory.

At most manufacturers contacted, the workforce is below year-ago levels, by 2 to 15 percent. Some firms have also reduced hours worked.

One-third plan further cuts in employment, generally through attrition.

Over half of the respondents have reduced 1991 capital spending below 1990 levels and below plan. Several report that spending is now less than depreciation. Only two firms are expanding capacity for specific products.

Input prices are generally described as stable, rather than declining as they were previously. All of the manufacturers surveyed report that their own sales prices are flat or falling. Several firms complain of a squeeze on their profit margins.

Although a few contacts report tentative upticks, most see no clear indication that the recession has ended. Indeed, a majority expect the "tough sledding" to continue through the first or second quarter of 1992. Because they cannot see a potential source of significant growth, they expect the recovery to be very slow.

Residential Real Estate

New England realtors contacted in early September blame questionable job security for sluggish residential real estate sales. Only in eastern Massachusetts have realtors seen an increase in sales volume relative to last year. Housing markets in New Hampshire and Vermont remain in the doldrums, according to respondents, because the Boston and New York economies, critical for both vacation home sales and tourism, have not yet recovered.

The consensus among real estate contacts is that competition among banks for residential mortgages has made rates very attractive. By contrast, sharp declines in residential rents have made credit for investments in condominiums and other multifamily residential property difficult to obtain.

SECOND DISTRICT--NEW YORK

Reports on District developments remained mixed in recent weeks. Relatively little new construction together with improved leasing activity resulted in a decline in office vacancy rates, and several areas reported a pickup in home sales, particularly to first time homebuyers. The August survey of Buffalo purchasing managers showed more firms reporting higher output and a substantial drop in those reporting lower output. District department store sales results for July and August were mixed, however. Moreover, unemployment rates in New York and New Jersey rose in August after declining in July. Senior loan officers at small and midsized banks reported reduced loan demand.

Consumer Spending

Sales results varied among District department stores during July and August though all respondents reported an improvement from June. Over-the-year changes in July ranged from -5.0 percent to +9.6 percent with several stores posting better-than-targeted sales. Over-the-year changes in August ranged from -3.0 percent to 6.0 percent as most contacts met their modest sales plans. The strongest selling items in July and August were women's apparel and accessories followed by men's and children's wear. However, most contacts reported that back-to-school sales were slower than anticipated. Some pickup in home furnishings occurred but respondents noted continued consumer reluctance to purchasing big ticket items.

Due to tight monitoring and, in some cases, to better-than-expected sales, inventories are generally at quite satisfactory levels though one chain reported them above plan. Contacts remain cautious about the

outlook for consumer spending, especially those who experienced disappointing back-to-school results.

Residential Construction and Real Estate

Several areas in the District report a pickup in home sales in recent weeks, particularly to first-time homebuyers who have watched prices decline over the past two or three years and are now finding homes at affordable levels. Lower mortgage rates have also contributed to the recent improvement. In addition, brokers in Manhattan report increased investment demand for condominium apartments from foreigners whose currency has appreciated relative to the dollar. Much of the recent buying has been in the existing home market, however, and thus far, homebuilders have not experienced much impetus for new construction. As a result, they anticipate that sales of new homes this year will be little changed from last year's low levels. A shortage of credit for acquisition and construction loans continues in much of the District.

Relatively little new construction of office buildings and a continuing improvement in office leasing activity have caused vacancy rates to decline in several parts of the District. The declines have been modest, however, and rates remain high in many areas. Leasing in midtown Manhattan during July was the strongest this year and the primary vacancy rate edged down for the second consecutive month. In downtown Manhattan the July decline in the primary vacancy rate was the third in the last four months. The planned merger between Chemical Bank and Manufacturers Hanover is expected to result in a sizable addition of excess space in both downtown and midtown Manhattan.

Other Business Activity

Continuing the volatile pattern of the last several months, unemployment rates in New York and New Jersey rose 0.4 percentage point in August after declines of 0.6 and 0.3 percentage point, respectively,

in July. New York's unemployment rate in August was 7.5 percent and New Jersey's was 6.7 percent. Both states have been reporting nonfarm employment at below year-earlier levels for a number of months, a pattern which continued in July. With the impact of recently announced mergers and cutbacks yet to be felt, few observers anticipate a near-term improvement in the District's employment picture.

The August survey of Buffalo purchasing managers showed an increase in firms with greater output and a substantial drop--from 41 percent in July to 18 percent in August--in those with smaller output. The percentage with the same or increased new orders also rose slightly. The July survey of purchasing managers in Rochester showed a sizable rise in the percentage anticipating improved business conditions over the next three months.

Financial Developments

Most senior loan officers surveyed at small and midsized banks in the Second District reported that while their willingness to extend loans remains unchanged from three months ago, they are facing reduced loan demand. In particular, consumer demand for installment credit and automobile loans has slowed, while demand for home equity loans has not shown a trend in either direction. The majority of senior officers also indicated lower delinquency rates on all consumer loans compared with three months earlier.

Most loan officers reported that their interest rates have remained stable and their credit standards unchanged over the last three months. However, a few respondents are conducting more rigorous background and employment verifications of potential borrowers. The credit quality of borrowers at the majority of surveyed banks has not changed in recent months.

THIRD DISTRICT - PHILADELPHIA

Economic conditions in the Third District appeared mixed in early September. Manufacturers reported continuing improvement, with increases in orders and shipments. Retailers indicated that sales have been running only even with a year ago. Bankers said commercial lending continued to slip while consumer and real estate loan volume was just steady.

In their forecasts, most Third District business contacts generally see current trends in their industries continuing. Manufacturers predict further improvement over the next two quarters. Retailers expect sales to run at just a steady pace well into the fall. Bankers expect total loan volume to remain nearly flat. While some believe the decline in commercial lending may bottom out soon, they say convincing evidence of a turnaround is not yet in sight.

MANUFACTURING

On balance, Third District manufacturers contacted in late August and early September reported continuing improvement in business conditions. Half said orders and shipments had been steady in recent weeks while nearly a third said orders and shipments have been increasing. However, some weakness was reported by firms producing transportation equipment and defense goods; these companies indicated that orders were slipping toward very low levels. Overall, while almost half of the firms polled reported steady inventories, more than a third indicated that stocks were declining. Employment appeared to be stable, on balance, with more than three-fourths of local firms maintaining steady payrolls and working hours.

Looking ahead, Third District manufacturers are generally optimistic. Most of those contacted for this report expect orders and shipments to rise over the next two quarters, and many anticipate an increase in order backlogs. On balance, area manufacturers plan to hold

inventories at current levels over the period. While most firms are planning to maintain steady employment through the winter, approximately one-fourth intend to hire more workers. Overall, capital spending plans at area plants call for only a slight increase in outlays over the next six months.

RETAIL

Most Third District retailers surveyed in early September reported that sales for August were approximately even with August a year ago, in current dollars. Most also said that the year-over-year comparison for early September appeared to be flat as well. Similar reports were given by virtually all types of stores and for all lines of merchandise. Merchants also said that back-to-school shopping was not strong. Several retail executives said they believe recently enacted income and sales tax increases in Pennsylvania and New Jersey were a restraining influence on consumer spending.

Third District retailers generally share a very cautious outlook. Most do not look for significant growth in sales this fall. Some noted that competitive pressures appear to be building as expectations for an early recovery fade; they point to deep markdowns and extended sales at some stores. In general, merchants do not expect solid improvement until Christmas shopping begins, and they hope to better the weak performance of last year. Nonetheless, some store officials indicated that they have not ordered aggressively for the holiday sales period.

FINANCE

Total loan volume outstanding at major Third District banks continued to edge down in late August and early September, according to local bankers. The decline is concentrated in commercial and industrial lending. Bankers generally indicated that there is little loan demand from potential business borrowers that meet their credit standards. Most of the bankers interviewed for this report indicated that consumer loan demand was soft although outstandings continued to be nearly stable. Real estate loan volume was also described as steady. Although reports varied among banks, it appeared that, overall, real estate loan volume was being held up by new lending for light industrial buildings and extensions of loans to

existing commercial borrowers who have been unable to obtain permanent financing; most bankers said they were seeing little demand for new residential mortgages and they were making few new loans for office or commercial space. Home equity loan volume has been steady at most large banks in the district.

Most of the bankers interviewed in early September expect loan volume outstanding to remain steady in the short-term. Some indicated that seasonal slowness may be obscuring signs of a pickup in commercial lending; nevertheless, most believe that a rebound in financing activity, for both businesses and consumers, will not occur until potential borrowers become confident that economic conditions will improve soon.

FOURTH DISTRICT - CLEVELAND

Summary. Recovery underway in both the nation and the District appears to be at a slower pace than in even the mildest of the postwar recoveries, according to most District respondents. Real consumer spending is still sluggish, with second-half growth predicted between 1% and 3% this half. Continued recovery in Fourth District industrial production, which began last spring, is expected to be supported by a slowing of inventory liquidation and by revival in most capital goods industries. The real estate market has weakened. Lenders report continued softness in bank loans, and recent declines for mortgage refinancing.

The Economy. Respondents uniformly agree that recoveries in both the nation and the District are off to a slow start, and most also expect that output growth, at least for the first year of the upturn, will fall short of the mildest of the past business recoveries. Most predict that real GNP will expand this quarter in a 2% to 3% range, but a few still expect a fourth-quarter real GNP growth rate of about 3% to 4%.

In Ohio, manufacturing output, which often lags the national recovery, rebounded last quarter, and respondents anticipate continued growth based on the strength of exports coupled with an ending to inventory liquidation.

Consumption. Retail sales in the late summer months have been relatively flat, and early September sales were up only a few percentage

points from a year ago, according to a retailer. Still, another retailer managed to liquidate the bulk of its excess stocks. Retailers are reported to be very cautious in planning inventories for the Christmas season in order to avoid large inventory overruns and subsequent discounting.

Economists associated with consumer goods are uncertain about the short-term outlook for real consumer spending. Some expect about a 3% growth rate this half, but several others anticipate only 1% to 2% growth.

Auto industry sources estimate that domestic new car sales will average about a 6.5-million-unit-annual rate this quarter and next, up a few percent from last quarter. New car dealers believe that a shortage of many 1991 models may account for some of the sales declines in August. They uniformly believe that further price incentives will not be necessary to clear the remaining car inventory.

Manufacturing. The District's recovery in manufacturing output, which began last spring, has continued into the summer, led especially by higher auto output. Several producers and suppliers expect that auto output will continue to edge to upward. Domestic car production this quarter is estimated at about a 5.8-million-unit annual rate; slightly more than a 6 million-unit rate is expected next quarter. Some concern was expressed that the slowly rising trend in production might be interrupted by consumer resistance to higher prices for 1992 models, which would leave the industry with larger-than-desired inventories.

Steel producers in the District have been operating at about 70% of capacity for most of the year, but they expect a gradual strengthening over

the balance of the year. Steel inventory liquidation appears to have run its course sooner than expected because of a recent spurt in orders from the auto and appliance industries, according to steel sources. Recent steel price increases appear to be sticking, an indication of stronger demand, and some workers who were laid off are currently being recalled.

The machinery and industrial equipment industries are probably close to a trough, and prospects for a turnaround have improved since operating rates in manufacturing have begun climbing, according to a capital goods producer. A producer of industrial controls equipment expects that the contraction in industrial equipment will end this quarter. Domestic shipments of commercial aircraft are expected to rebound this quarter from last, and the gradual recovery in heavy-duty truck orders and production should gain strength by year-end in response to rising operating rates in manufacturing. Another capital goods producer reported a sizable pickup in sales and profits for its third quarter, attributable to both domestic and international sales. Finally, a supplier to capital equipment producers reports that its orders from general machinery producers and the steel industry are showing signs of recovery, and that its delivery schedules have begun to lengthen.

The massive reduction of business inventories during the latest recession will be largely completed this quarter, according to an industry economist. The source noted that July's inventory-to-sales ratio for nonauto durable goods was back to its 1987-89 average.

Real Estate. Lenders and realtors generally report that demand for housing has slowed in recent months, although some lenders experienced a

pickup in new loans in August. Listings are fewer-than-usual for the summer. Some attribute the less-than-seasonal strength in housing starts and sales this summer to a lack of consumer confidence. They claim that mortgage funds are readily available to creditworthy buyers, and report that mortgage rates eased recently to an 8-3/4% to 9-1/4% range for a 30-year conventional loan mortgage.

Financial Developments. Most lenders report little change in total loan activity in recent months, except for declines in mortgage loan refinancing following a surge in the spring and early summer months. Some sources believe that continued softness in business loans may reflect low working capital needs because of the large liquidation of inventories, and that future growth of business loans may be constrained by increasing business bankruptcies. Some easing in mortgage loans for new and existing homes is also noted, but a few banks report some pickup in auto installment loans in August, and continued growth in home equity loans. Several depositors acknowledge that they have not been aggressively seeking loans because of capital constraints or soft demand for credit. They also report further reductions in interest rates on deposits in recent weeks.

FIFTH DISTRICT-RICHMOND

Overview

District economic activity continued mixed in August, but respondents remained optimistic about business prospects for the next six months. Manufacturing activity rose somewhat but retail sales and exports declined. Employment was steady in manufacturing but lower in retail businesses. Loan demand remained weak except in home refinancing. Conditions in agriculture improved as timely rains helped crops.

Consumer Spending

Our regular survey of retailers indicated that, on balance, retail activity weakened in August. Total sales apparently fell somewhat along with sales of big ticket items. Shopper traffic was lighter than in July. Inventories were drawn down and employment declined. Wages rose as did wholesale and retail prices.

Looking forward, retailers were optimistic about the business outlook for the next six months. They anticipated increases in shopper traffic and sales. Most expected little change in employment and inventories but looked for wages, retail prices, and wholesale prices to rise further.

Manufacturing

Our regular mail survey of manufacturers indicated that District factory activity improved in August. Increases were reported in shipments, new orders, and the length of the workweek. Inventories apparently shrank while employment, prices, and other business indicators remained steady. Manufacturers identified poor sales, government red tape, competition, and excess capacity as their biggest problems.

Manufacturers remained optimistic about general business conditions and

their own prospects for the next six months. They foresaw increases in virtually all categories of activity including capital expenditures and exports.

Port Activity

Representatives at District ports--Baltimore, Charleston, and Hampton Roads (Norfolk)--reported that exports were generally lower and imports higher in August than in July. Compared to a year ago, exports were up and imports were down. Contacts at District ports expected export growth to outpace import growth throughout the fall and winter.

Tourism

A telephone survey of hotels, motels, and resorts in the District suggested that tourist activity through the Labor Day weekend was unchanged both from July and a year ago. Over half of the respondents reported that fall bookings were about even with last year's, and almost all expected tourist activity to remain about even with a year ago in the months ahead.

Finance

District financial institutions contacted by telephone indicated that credit availability was generally steady over the last six weeks. Several banks, however, said they had tightened standards for commercial loans. Commercial loan demand was reported soft, but the demand for residential mortgages firmed as refinancing activity increased. Most banks expressed a continued willingness to make new consumer loans.

Banks indicated that they had lowered their rates on some types of loans following recent declines in money market rates. Almost half reported that they had reduced their rates on consumer and mortgage loans. None, however, said that they had lowered commercial loan rates.

Housing

Residential real estate activity remained sluggish in most of the District according to a telephone survey of housing analysts and real estate lenders. Most respondents reported little change in prices, sales, or construction starts, though lower interest rates were said to have slightly boosted sales in some localities. Respondents in the Washington, D.C., area noted a glut of homes for sale and for rent. Most respondents reported little speculative residential construction. One exception to the generally sluggish housing market in the District was Greenville, SC, where activity was reported to be strong.

Agriculture

Recent rainfall generally improved the condition of District crops according to farm analysts. Corn and soybean yields were expected to be normal in Virginia, West Virginia and Maryland and somewhat above normal in the Carolinas. Dry conditions were noted in some areas of Maryland, however, and poor pasture conditions were reported in some regions. In the Carolinas, recent rains have damaged crops somewhat and kept farmers in some localities from spraying their fields for insects.

SIXTH DISTRICT - ATLANTA

Overview: Economic recovery in the Southeast continued during August, but at an unsteady pace. Manufacturers' reports are mixed with nondurable goods orders expanding more rapidly than durables. Realtors suggest modest recovery in residential sales, reducing existing inventories. However, builders are unwilling, or unable, to renew significant development. Retailers were disappointed with August sales after two months of higher activity. No improvement in commercial construction is expected this year. Regional convention bookings and tourism are up modestly from year-ago levels. Bankers report some improvement in loan demand from earlier in the year, but borrowers continue to feel constrained by strict credit guidelines. Aggressive competition, soft commodity prices, and ample pools of job candidates are yielding product price stability and restraining wages pressures.

Consumer Spending: August retail sales were generally below expectations and year-ago levels. Confirming lackluster consumption and lean retail profit margins, advertising expenditures across all media remained at reduced levels recorded early this year.

Durable goods have shown little improvement, with home furnishings especially weak. General department store traffic declined modestly from this spring and early summer. Upscale department stores report lower back-to-school sales from one year ago. However, sales at stores emphasizing discount pricing expanded, as consumers continued to substitute away from more expensive selections. Retailers are expecting little, if any, increase in holiday sales from last year.

New car sales weakened in August after moderate improvements over the summer. However, used car sales continued to strengthen; contacts attributed this to consumer cost-consciousness and credit constraints. Dealers have been conservative in ordering 1992 models.

To counter announced price increases and expected consumer reluctance, rebate programs are reportedly under development.

Tourism in the region improved moderately during August compared with year-ago levels. Modest increases in convention bookings and visitors were reported in Atlanta, New Orleans, and Orlando. Based on advance bookings, convention attendance should continue to improve through the fall.

Manufacturing: Manufacturing activity remains mixed, with little change from the last reporting period. Textile contacts expect increasing shipments of denims and fleecewear through the end of the year, while producers of household textiles, such as draperies and linens, expect sluggish demand through the fall. Increasing paper mill shipments reflect continued strength in paper-related production.

Other manufacturers expect little improvement until next year. Automobile and building materials shipments continue to slump. Weak commercial construction continues to adversely impact the region's structural metal production. Sluggish construction and auto activity is expected to restrain demand for related chemical production through early next year. New layoffs continue to be reported at electronic equipment producers affected by declining defense contracts.

Financial Services: Most banking contacts reported improved demand for consumer and mortgage loans in August from June and July. However, loan demand for capital expenditures is unchanged from earlier this summer, and below year-ago levels. Some auto dealers and developers maintain that credit terms have continued to tighten.

Construction: Southeastern housing markets continued a moderate recovery in July and August. Except for Florida, single family permits in July pulled ahead of year-ago levels; multifamily permits remained weak. Most realtors reported modestly improved homes sales in

August from June and July. However, the Atlanta market appears to have faltered. Regionally, home sales in the mid-price range (trade-ups) are strong. Despite lower interest rates, first-time buyers of lower-priced properties are being constrained by higher FHA down payment requirements. Sales in the luxury market are stagnant.

New home inventories are declining, but builders report that modest demand and tight credit standards continue to limit speculative development. Contacts expect no improvement in nonresidential construction during the remainder of this year.

Wages and Prices: Most contacts report stable product prices and no acceleration of wage pressures. Stabilizing fuel prices and vigorous competition have pushed shipping rates below year-ago levels. Natural gas prices firmed in the last month but remain below levels required to induce new drilling. A producer of air conditioning equipment reports that materials and parts prices are holding steady in a very competitive market. Regional housing prices have yet to rebound in response to moderately increased demand. Building supply companies remain under downward price pressure. Prices of the region's lumber products, however, have risen in response to firming domestic and export demand, as well as supply constraints on Northwest lumber.

Generally, labor availability is not a problem. Our contacts anticipate no acceleration of wage pressures over the next several months. Budgeted wage gains are equal to or slightly below those seen last year at this time. The major exception continues to be health services. According to one contact, new medical technology requires more highly skilled labor and a relative scarcity of skilled technicians continues to exert pressure on wages in that sector. Escalation of benefits costs continues to trouble employers, who are implementing increasingly aggressive policies to curtail these costs.

SEVENTH DISTRICT--CHICAGO

Summary. The Seventh District economy expanded modestly in July and August, according to most contacts, despite sluggish consumer spending growth. The overall manufacturing sector strengthened further, with continued gains in consumer durable goods production joined by hints of recovery in several capital goods industries. Residential real estate transaction activity softened somewhat, but remained sufficiently brisk to support gains in household goods production. The outlook for commercial construction and supplier industries was little changed. Bank asset and retail deposit growth in the District was restrained by both supply and demand factors.

Consumer Spending. Contacts generally indicated that growth in District consumer spending remained sluggish. One large general merchandise chain reported relatively flat sales in August (in nominal dollars, year-over-year) in the District, in line with the national average, and stated that regional differences in sales results have narrowed markedly over the year. A large discount chain reported that its sales in larger markets in the District declined in August (compared to last year), in part due to competitive pressures, while sales rose nationally. A retailers' association in Michigan reported that members continued to experience depressed traffic and sales levels, but conditions have stabilized in recent months. A liquidation trustee reported that retail contacts have experienced some upturn in sales in the past month. A large automaker reported that car sales declined in recent weeks, but still remained stronger than earlier in the year. However, anticipated strengthening in sales to fleets over the next two months is expected to boost total sales.

Manufacturing. The recovery in the District's manufacturing sector continued in recent weeks. Gains in consumer durable goods production were joined by signs that some capital goods production began to turn upward, although weak spots still exist. Purchasing managers' surveys in Detroit, Indianapolis, Western Michigan and Chicago showed increasingly widespread expansion. Detroit reported some softening in responses from nonautomotive businesses, but widespread gains were again recorded in the automotive sector. The results from Indianapolis registered a significant turnaround in the second quarter, with an important contribution from the automotive sector. Western Michigan showed continued solid expansion in July and August, with new signs of improvement from several capital goods respondents. Chicago's index moved strongly into expansionary territory in August, after gradually rising from low levels early in the year. Each of the monthly surveys recorded consistent inventory liquidation thus far in 1991, both during the contractions recorded early in the year and during the recoveries seen in more recent months.

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Most anecdotal reports also suggested strengthening among consumer durable goods producers and their suppliers. A large steel producer reported that shipments in the summer months were better than expected, with important contributions from shipments to auto and appliance manufacturers, although most customers still show little inventory rebuilding. A large electronics firm reported that semiconductor order growth continued to trend upward, with orders from automakers making an important contribution. Semiconductor orders from the previously weak capital goods sector were expected to turn up in the fourth quarter. An electric utility in Michigan reported its first monthly year-over-year gain in power sales to industrial customers in August. Several small suppliers to the auto industry reported new hiring activity, although a large automaker plans to use overtime rather than new hiring to meet labor requirements for the balance of the year. A producer of paper containers reported that demand from appliance producers has been stronger than expected, and a large appliance manufacturer stated that the industry trough had passed. Reports from the capital goods sector were mixed, but generally better than earlier in the year. A July survey of metalworking firms reflected improved expectations for business conditions, although appraisals of current conditions remained weak. After recording flat sales in the first half of 1991, a heavy machinery producer reported solid order gains in recent months. A large manufacturer of heavy-duty trucks reported renewed softness in industry orders. A producer of a wide range of specialized machinery reported that order gains remained relatively soft, however, with improved orders for food processing equipment offsetting continued weakness elsewhere. A large manufacturer of construction equipment experienced a renewed slump in orders in August, and stated that dealers continued to cut inventory amid low sales expectations.

Real Estate/Construction. Several contacts reported that the sharp pickup in the District's residential real estate sector earlier in the year may have softened somewhat recently, but activity is still running at respectable levels. A large District realtor reported that residential sales gains have been running in line with seasonal expectations in recent months. After home sales rose sharply in the second quarter, housing permits in Indianapolis rose fairly sharply in July. A realtors association reported that home sales in Wisconsin remained brisk in the summer, and 1991 sales are running at a record pace. A producer of gypsum wallboard reported that industry shipments into the Midwest strengthened in July. An appliance distributor reported that orders from home builders in the Midwest had improved over the past several months, with continued gains expected in the second half of the year. Year-to-date industry appliance shipments to dealers in the Midwest were essentially flat, according to one large manufacturer, which is relatively strong performance compared to much of the rest of the country.

Commercial real estate activity generally remained subdued in August, although the pickup in District manufacturing activity may be beginning to boost the demand for industrial space. A brokerage

firm reported that rental rates for downtown Chicago office space continued to decline in the second quarter, with rising vacancy rates joined by negative net absorption. A large District cement producer tied to commercial construction reported continued year-over-year shipments declines, with little near-term improvement expected for shipments in the Chicago metropolitan area. A group of small commercial lighting companies anticipate a 3 to 5 year depression in sales for nonresidential building in the Chicago market. The office market in metropolitan Detroit remained soft in recent months, according to a brokerage firm, with vacancy rates continuing to rise.

Few District banks reported new tightening in standards for new commercial real estate loans in recent months, but financing generally remained difficult to obtain, with strict preleasing and borrower equity requirements in place. Lending terms have become increasingly costly, particularly for loan extensions. One District retail store chain recently completed a large equity offering designed to allow the retailer to internally finance its store expansion program. Previously, expansion had been constrained by the inability of real estate developers to obtain construction financing from banks.

Banking. Reports from several large banks in the District reinforced earlier indications that both demand and supply factors worked to suppress bank credit and retail deposit growth in June and July. Several large banks reported that demand for retail deposits was dampened by increasingly competitive returns on nondeposit instruments and sluggish economic conditions in deposit market areas. At the same time, banks themselves reported somewhat less aggressiveness in promoting retail deposits. Generally, slower asset growth led to some softening in the desired growth for wholesale liabilities, but neither increased deposit insurance premiums nor slower asset growth affected the desired growth for retail deposits. *Still, several respondents indicated that they were likely to be less aggressive in attracting retail deposits over the balance of the year.*

Most banks contacted reported weak asset growth since the end of May. Each bank that reported weak asset growth cited softer loan demand, although other factors (including planned reduction in lending and securitization) were also cited. At the same time, most banks reported little change in standards for commercial and industrial lending in recent months, after more frequent indications of tighter standards being adopted earlier in the year. Weaker loan demand was generally concentrated among larger corporate customers, with banks noting several reasons, including lower financing requirements for inventory and capital investment, as well as alternative nonbank and/or capital market financing sources. Some reports of increased loan demand from medium-sized and smaller firms arose, with one bank reporting increased capital spending by smaller businesses.

EIGHTH DISTRICT - ST. LOUIS

Summary

The economy in the Eighth District is showing signs of growth, but contacts stress that any expansion is weak. Although manufacturing activity overall is stagnant, the stabilization of auto-related manufacturing and rising exports are encouraging signs. Residential construction activity has picked up slightly. Loan growth remains weak. Tourism has been marginally higher this summer than last in most parts of the District. Most crops are in fair condition as the fall harvest approaches.

Manufacturing

Most manufacturers surveyed expect to increase production in the next few months, but do not plan to increase the size of their workforce or invest in new plant or equipment. Most also report that inventories are at satisfactory levels, although an increasing minority indicate that inventory levels are higher than desired. Auto-related manufacturing has stabilized for the most part, with employees at some vehicle assembly plants working overtime. Nonetheless, a drop in orders has reportedly caused substantial layoffs at one steel factory that makes parts for railroad cars carrying new motor vehicles. A shoe manufacturer will close several factories and warehouses in Missouri permanently this fall, eliminating 1,400 jobs. According to a company spokesman, the national recession and strong import competition were the primary reasons for the closings.

Contacts generally report an increase in exports, though some mentioned that the rate of growth had slowed. Strong export growth was reported by producers of furniture and paper products in some rural parts of the District. As District exports to Mexico rise, a number of companies have begun to investigate similar export opportunities. Political instability has made exporters more cautious in pursuing sales to the Middle East and the Soviet Union, according to some contacts. Most respondents believed that the upward movement in the exchange value of the dollar since February has had little effect on exports.

Construction and Real Estate

Residential construction activity has picked up modestly in some parts of the District. Strong economic growth in northwest Arkansas has created construction jobs for workers from other parts of the state, where activity remains stagnant. Contacts describe western Kentucky homebuilders as "holding their own," largely because of lower interest rates and the ability of some builders to get construction loans now that they could not get several months ago. Despite increases in lumber prices, new home prices have remained relatively constant. Contacts do not anticipate a general recovery in the residential construction industry in 1991 and are split as to whether the recovery will occur in 1992 or 1993.

Tourism

Despite the recession, tourism in Missouri, Arkansas and western Kentucky has been somewhat stronger this summer than last. Contacts in Missouri and Arkansas attribute the increased activity to the desire for short, economical vacations close to home. Arkansas tourism also has been stimulated by an expanded advertising campaign. The recent level of

tourism in Tennessee, however, is reportedly the same as last year. Some Missouri contacts fear the state has lost some tourism business because of the legalization of riverboat gambling in Iowa, and will incur further losses when riverboat gambling begins in Illinois in the near future.

Banking and Finance

Total loans outstanding at District banks remain substantially below year-ago levels as most loan categories show a decrease during recent months. For example, both business and consumer loans declined from mid-June through mid-August relative to the prior two months.

Agriculture and Natural Resources

Although soil moisture ratings in the District remain below optimal levels, most crops in the District are generally in fair condition. The lack of adequate moisture, however, has hampered development of the soybean crop and accelerated the maturation process of the corn crop. As a result, harvesting of the corn crop is well under way in the southern regions of the District and just beginning everywhere else. Early reports suggest that corn yields are mixed. The rice harvest is under way in Arkansas and Mississippi; rice growers expect to harvest a bumper crop in Arkansas, but poor weather conditions this past spring have diminished rice prospects in Mississippi. District cotton producers report that expectations of a record harvest have depressed prices. Livestock are mostly in good condition, but the dry weather has hurt pastures. Southern pine lumber producers report that production has picked up, though it still lags behind a year ago. Exports of Southern pine lumber, on the other hand, are running ahead of last year.

NINTH DISTRICT—MINNEAPOLIS

The Ninth District continues to feel the effects of the national recession. Labor market conditions have improved slightly, though employment growth has been weak. Retail sales have showed only moderate growth, and automotive sales continue to be slow. Conditions in the manufacturing and resource-related industries were mixed. Tourism was the major bright spot.

Employment, Wages, and Prices

Labor market conditions improved in most of the District. Minnesota's July unemployment rate fell to 4.4 percent from 4.8 the previous month, and below the year-ago rate of 4.9 percent. Unemployment rates fell in July, relative to their June levels, in Montana (6.1 percent from 6.4), North Dakota (3.9 percent from 4.2) and the Upper Peninsula of Michigan (8.6 percent from 9.2), but in all three cases remain above their year-ago levels (5.0, 4.0, and 7.7 percent, respectively). In South Dakota, the unemployment level in July rose 0.1 percentage point from June to 3.2, but remains substantially below its year-ago level of 3.6 percent. On a cautionary note, the preliminary level of Minnesota's initial unemployment claims was 20 percent higher in August than its year-ago level. Changes in the July unemployment rates from year-ago levels were mixed in western Wisconsin. The growth in nonagricultural employment in July from year-ago levels was an anemic 0.52 percent in Minnesota and 0.83 percent in Montana, but a robust 1.41 percent in North Dakota and a whopping 2.74 percent in South Dakota. In a number of sectors of the Minnesota economy July employment levels fell, relative to their year-ago levels: manufacturing down 1.24 percent, construction down 6.14 percent, transportation down 0.44 percent. Only in the FIRE (finance, insurance, real estate), services, and government sectors did Minnesota's employment rise substantially in July, relative to its year-ago levels: 1.69,

3.28, and 0.54 percent respectively. In Montana, the weak employment growth was due in large part to a sharp fall in mining employment, down 6.06 percent in July from its year-ago level.

Consumer Spending

Retail sales in the District were mixed. Sales tax receipts in Minnesota were down 6.25 percent in July relative to year-ago levels. Major retailers in the District report August sales increases of comparable stores, relative to year-ago levels, ranging from 1 to 13 percent with discount stores generally reporting the largest increases. Retail sales have been strong in Montana, North and South Dakota, and the Upper Peninsula of Michigan, which continue to reap the benefits of the influx of Canadian shoppers.

District new car sales continue to be weak, with one major domestic auto company reporting car sales declines of 15 percent in August and 22 percent for the year to date, relative to a year ago. Used car prices remain high.

Housing sales remain somewhat weak in the District. In the Minneapolis-St. Paul area existing home sales were up 4.1 percent in July relative to a year ago, after falling in June. The June drop was attributed to a change in the terms of FHA-insured loans. The price increase of the median-priced home in the Twin Cities area rose 2.1 percent in the second quarter over a year ago, continuing the trend of the 1980's in which existing home prices in Minnesota have failed to keep pace with inflation.

Tourism activity has been excellent in all parts of the District. The number of crossings over the Mackinac Bridge onto the Upper Peninsula was up 3.3 percent for the first eight months of this year and 6.9 percent in August, relative to a year ago. Crossings over the International Bridge between the Upper Peninsula and Canada were also up 3.8 percent in August relative to their

year-ago level. There has been a substantial increase in tourism at Mount Rushmore due in part to its recent fiftieth anniversary celebration.

Construction and Manufacturing

Conditions in the District's construction industry have been mixed, with the overhang of office space in the Minneapolis-St. Paul area expected to continue to depress commercial activity in the area. The value of future construction contracts in the Twin Cities area remains above year-ago levels. However, the July level of new housing permits was down 15 percent.

The Minnesota index of economic activity rose to an all-time high in June, up 1.2 percent from May and 1.5 percent from its year-ago level. However, new business incorporations were down sharply in August, only slightly higher than their year-ago level, while average weekly hours in July were slightly below their year-ago level, and manufacturing employment was down 1.3 percent over the same period.

Resource-Related Industries

Crop yields in the District are expected to be generally good. However, prices are sharply down. The mid-July level of the Minnesota index of all farm products fell 13 percent relative to its year-ago level, with crop and dairy prices falling by 18 percent, and livestock prices falling by 6 percent. The only bright spot was poultry and egg prices which rose 6 percent over this period. Milk prices are reported to be below the break-even point.

TENTH DISTRICT - KANSAS CITY

Overview. Economic conditions in the Tenth District continue to improve modestly. New home sales have increased, auto sales have picked up, and other retail sales remain steady. Most firms are maintaining or trimming inventories, and prices generally are changing little. Agriculture and energy may be contributing less to district growth than in the past few months, however. Drilling for oil and gas is off slightly, cattle prices have dropped, and hot, dry weather has reduced expected crop yields.

Retail sales. Most retailers report sales unchanged from last month and down from a year ago. Retailers generally expect sales to stay flat the rest of the year. Selling prices have changed little in the last month and are expected to remain flat. Most retailers are satisfied with their current inventory levels.

Auto sales have picked up recently in district states. Potential buyers are able to get loans in most instances. As the new model year begins, dealers are trying to trim inventories of 1991 cars. Dealers in all district states anticipate stronger sales of 1992 models.

Manufacturing. Purchasing agents report steady to slightly higher input prices over the past month. Respondents expect prices to stabilize over the coming months. Materials are readily available, with no problems expected for the rest of the year. Most firms expect to maintain or trim inventories in the months ahead. While some plants are working close to capacity, none are facing bottlenecks or skilled labor shortages.

Energy. Weak natural gas prices and only slightly stronger crude oil prices have dampened energy activity in the district. The average number of operating drilling rigs in district states dipped from 244 in July to 237 in

the first three weeks in August. The August rig count fell to 16 percent below its year-ago level.

Housing Activity and Finance. Housing starts across the district are up from a year ago and mixed compared with a month ago. Builders report mixed expectations for starts the rest of the year. New home sales are up, helping to reduce inventories of unsold homes. Prices for new homes are up in some parts of the district and down in others. While construction materials are readily available, builders continue to report increases in lumber prices.

Most savings and loan respondents report net deposit outflows greater than both last month and a year ago. Most respondents expect outflows to continue in the coming months. Demand for mortgage funds has increased slightly in most areas of the district, but further increases in demand are not expected by most respondents. Mortgage rates are down slightly, and most respondents expect slight downward pressure on rates through the end of the year.

Banking. Changes in loan demand were mixed at district commercial banks last month. Respondents reporting decreases, increases, and no change in overall loan demand were about equal in number. Demand for commercial real estate loans was generally lower, while demand for agricultural loans was slightly higher. Other loan categories showed no definite trend. Most banks report either steady or declining loan-deposit ratios. Total deposits were generally unchanged or somewhat higher at responding banks last month, but large CDs and small time and savings deposits declined at some banks.

Most banks report no change in either their prime rate or their consumer lending rates. One or two banks report decreases in these rates, and a few

respondents expect to lower these rates in the near term. No banks report changes in other lending terms.

Agriculture. Dry weather has reduced expected yields from the district's row crops. Dryland crop yields in much of the district may fall to as much as 50 percent below average. Irrigated crop yields are expected to drop slightly below normal. Due to the reduced yields, some district corn fields will be cut for silage instead of being harvested for grain. While more rain will be of little help to this year's row crops, additional moisture would improve growing conditions for the district's winter wheat crop.

Pasture conditions have also suffered from the hot, dry weather. Many ranchers are providing supplemental feed for cattle grazing dry pastures, and a few have reduced cattle herd sizes due to the shortage of adequate pasture.

Falling fat cattle prices drastically reduced revenues of district feedlot operators in August. Operators who paid high prices for animals placed in feedlots saw narrow profit margins turn into substantial losses as finished cattle prices fell. Despite the losses, most operators have continued to feed a normal number of cattle, expecting an upturn in fat cattle prices.

ELEVENTH DISTRICT--DALLAS

Output growth in the 11th District economy has increased slightly since the last survey. The improvement has been centered in the residential construction and manufacturing sectors. Growth has continued weak in the service-producing sectors. Energy extraction has declined in response to persistently low natural gas prices. Consumer spending remains sluggish. Most retailers report disappointing back-to-school sales and auto sales remain at low levels. While the financial conditions of banks continue to improve, loan demand is flat. Agricultural conditions have weakened.

Orders to District manufacturers are rising, and most respondents say that their inventories are at desired levels. Growth in demand has been particularly noticeable in construction-related manufacturing. Producers of lumber and wood, and stone, clay and glass say that upturns in national and regional residential building have boosted their orders. Apparel, electronics, and electrical machinery firms note that their sales have risen because customers are replenishing depleted inventories. Demand for refined petroleum products remains flat, but petrochemical producers cite some recent gains in orders. Although declines in domestic drilling have reduced domestic orders for oil field equipment, overall District sales remain unchanged because of rising export demand. Indicative of the general expansion in manufacturing, makers of packing board and corrugated liners say that demand for their products has steadily increased over the past three months.

Growth in the District service sector is weak. Respondents in consulting and accounting services say that demand has been flat. Lodging industry respondents note softness in demand from business customers. Legal

services, advertising agencies and temporary employment firms cite mild expansions in activity. Although most respondents express a good deal of uncertainty about their sales outlooks for the rest of the year, they generally expect mild growth.

Retail sales have picked up slightly but are below year-ago levels. Respondents report very competitive markets and disappointing back-to-school sales. Retailers are optimistic that sales will improve, although they expect the upturn to be slow in real terms. Most firms say that their inventories are at desired levels and that prices are stable. Dallas area sales show more weakness than elsewhere in the District. Auto sales are below year-ago levels.

Output in the District energy sector continues to decline. While natural gas prices have increased slightly, they remain near their lowest levels in 20 years. Drilling activity has declined, particularly in the Gulf of Mexico. Respondents note that if this winter is normal, natural gas prices should average a little higher than last year and oil prices should experience their normal seasonal rise. Oil prices should decline slightly next year due to increased sales from Iraq and Kuwait.

Construction activity has increased due to a moderate rebound in residential building. During the Middle East War, residential construction in the District temporarily deviated from its moderate growth trend. Since the end of the war, residential construction has gradually returned to its former growth rate. Commercial construction remains sluggish. Commercial vacancy rates in the major metropolitan areas remain high although they continue to fall. Builders show little hope for any significant expansion in commercial

construction at least through the end of this year. Respondents note a recent decline in the demand for industrial office space. Industrial rents and vacancy rates are said to be flat overall.

District commercial banks report soft loan demand. While the financial condition of banks continues to improve, business loan demand remains weak. Respondents say that the reduced loan demand stems from sluggish economic activity, regulatory changes, and an availability of capital from other sources. Bankers do not expect loan demand to increase significantly over the next few months.

Agricultural conditions have worsened. Cotton prices, which were high during the first half of this year, have dropped due to higher yields. Although cotton farmers in the District are expected to harvest record volumes this year, shrinking government subsidies and recent price declines are said likely to reduce net cash income. The dairy industry remains depressed due to low milk prices. Livestock prices fell sharply in the first part of August and recovered somewhat in the following weeks. Livestock prices are not expected to fully recover until after September.

TWELFTH DISTRICT -- SAN FRANCISCO

Summary

Economic conditions remain weak in much of the Twelfth District, with areas that have felt the impact of the recession reporting few signs of recovery. In intermountain areas where the recession has had only modest effects, economic conditions continue to be much better than in the District as a whole. Wage and price increases throughout the District are modest, and consumer spending continues to be sluggish. Slow retail sales have hurt sales tax revenues in many jurisdictions, further squeezing already-tight state and local government budgets. Manufacturing activity remains mixed, with the aluminum industry reporting worsening conditions. Some District farmers report disappointing fruit harvests, due either to poorer than expected quality or disappointing volumes. Construction and real estate activity remain slow, especially in California. Loan demand continues to be sluggish in California, while Utah financial institutions report relatively good conditions.

Business Sentiment

Economic expectations of Twelfth District business leaders improved slightly in September. While a majority of respondents still foresee GNP growth of less than 2.5 percent during the next four quarters, only 5 percent now expect the next four quarters to be characterized by recession. More than half of respondents project improvement during the next four quarters in business investment, housing starts, and consumer spending. Expectations about inflation also seem to be improving, with 61 percent of respondents now projecting some reduction in inflation during the next four quarters compared with 50 percent six weeks ago.

Wages and Prices

Overall wages and prices are increasing modestly in the Twelfth District. Retail prices are reported to be relatively stable, while prices have fallen during the past year for many food products. Prices also are reported down significantly for some office electronic products. Increases in health care costs still outpace the general inflation rate by a wide margin. Wage increases continue to cluster in the 3.5 to 5 percent range throughout the District. In California, however, tight state government fiscal conditions have forced many middle and upper level state employees to take 5 percent salary cuts.

Retail Trade and Services

Consumer spending remains weak in most parts of the Twelfth District. A soft goods retailer reports that sales still are very sluggish in California, Oregon, and Alaska. For his chain, sales are slightly stronger in Washington and very good in Utah. In California, higher sales tax rates are blamed for some of the slowdown in retail sales. Auto sales remain weak in much of the District, although some improvement was noted in Arizona and among higher-end cars in Idaho. Year-over-year declines in newspaper advertising volume have moderated somewhat in recent months, but July volume was still 18 percent below its year-earlier level.

Manufacturing

Manufacturing activity in the West is mixed. Metals industries continue to report weak conditions. Layoffs are mounting in the aluminum industry, with one firm in the Pacific Northwest reportedly cutting employment by more than 50 percent. Aluminum and zinc prices are down, while copper prices have stabilized recently. Employment in the aerospace industry continues to suffer from defense cuts. Helicopter manufacturing employment in the U.S. is expected to fall 2 percent in 1991, despite improving exports. Boeing continues to receive orders for commercial aircraft, although the pace of new orders has slowed in recent months. In Utah,

some non-durable manufacturing industries report growth in orders of 8 to 10 percent from last year. A chemical products manufacturer reports that orders have picked up in recent months, but remain 7 percent below a year earlier.

Agriculture and Resource-Related Industries

Agricultural conditions in the Twelfth District have weakened somewhat. Fruit growers in California report that harvests were large, but some growers had trouble meeting size and quality standards. Hot August weather in Washington reduced the volumes of the apple and grape crops. Many commodity prices are reported down from a year ago. Potato prices are off 50 percent, while hay prices are reported down 15 percent. Beef prices also are lower as a result of increasing inventories and low demand. In California, agricultural exports continue to expand despite a curtailment of the state's export promotion program as a result of budget cuts.

The forest products industry remains in poor shape, although one report from the Pacific Northwest suggests that some lumber mills have begun to rehire workers. Lumber prices have fallen back after a sharp run-up in the second quarter. Forest products industry employment in Oregon and Washington remains well below its level a year ago.

Construction and Real Estate

Construction and real estate activity remain sluggish in many parts of the Twelfth District. In California, home sales are reported to have slowed following the rebound seen this spring, while median home prices seem to have stabilized. Commercial markets in southern California continue to languish, with vacancy rates in downtown Los Angeles expected to rise as new space comes on line. Residential prices also are reported soft in Washington, and residential construction activity there has fallen sharply since last year. Conditions in Utah and Idaho are much better, with relatively strong prices and sales activity. The median home price is reported up in Arizona.

Financial Institutions

Conditions at Twelfth District financial institutions remain mixed. In California, loan demand continues weak for most categories of loans, while credit quality is deteriorating and write-offs are increasing. Loan demand also is reported soft in Arizona, although auto and residential real estate loan volumes have improved. Banking conditions in Utah remain solid.