The BEIGE BOOK

July 28, 2004

Summary of Commentary on Current Economic Conditions by Federal Reserve District

Summary

Prepared at the Federal Reserve Bank of Cleveland and based on information collected before July 19, 2004. This document summarizes comments received from businesses and other contacts outside the Federal Reserve and is not a commentary on the views of Federal Reserve officials.

Federal Reserve districts reported that economic activity continued to expand in June and early July, although several districts reported that the rate of growth moderated. The Philadelphia, Atlanta, Chicago, St. Louis, Minneapolis, and Dallas Districts characterized growth rates as ranging from modest (Minneapolis) to solid (Chicago), while New York, Cleveland, Richmond, Kansas City, and San Francisco noted that growth rates slowed somewhat in their districts. Boston cited mixed reports from its business contacts. Reports of rising prices at the producer level continued to be common, though increases in retail prices were only infrequently reported. While wage gains remained generally flat, benefits costs continued to rise.

Retail sales were widely cited as having slowed; in particular, most districts reported that auto sales were flat to down. Manufacturing activity increased across the country, though there were pockets of weakness and gains were generally more measured than in the early spring. Travel and tourism were reported to be strong in many districts. Regarding construction, the pattern of past reports continued, as residential construction was still strong across most districts, while nonresidential building remained generally weak. In the banking sector, borrowing by commercial clients rose moderately in most districts. In the consumer lending category, mortgage originations were reported to be robust, but refinancings fell further. Agricultural conditions across the country were mixed, as some areas suffered from unusually wet weather. Mining and energy enterprises saw increases in activity in recent weeks.

Cost pressures were cited for a variety of production inputs in most districts. Energy, steel, and cement prices were widely cited as high and were reported to have moved higher in most districts. Some agricultural product prices, including beef, chicken, and milk, were also cited as adding to pricing pressures. The degree to which businesses have been able to pass along these prices continued to vary, but no district reported an acceleration in general retail prices. The few reports of labor shortages were narrow in scope. Wage increases were also widely reported to be moderate. However, businesses continued to cite health care costs as a factor in significantly boosting total labor costs.

Consumer Spending

Consumer spending moderated across much of the country in June and early July, following strong increases in spending in the early spring. Seven districts reported that consumer spending had softened since their last reports: New York, Philadelphia, Cleveland, Atlanta, Chicago, Dallas, and San Francisco. In the New York, Philadelphia, and Cleveland Districts, much of the moderation in spending was attributed to weather that was cooler than typical for the time of year.

Kansas City reported that spending had stayed largely flat in recent weeks, while Richmond reported that spending remained flat or was lower. Boston characterized consumer spending in its district as mixed. The districts reporting increases in spending were St. Louis and Minneapolis. St. Louis indicated that consumer spending was strong, whereas Minneapolis characterized spending as showing modest increases. A few districts noted that there were some indications of increases in spending in early July.

Auto sales were generally weak throughout the country in the late spring. Compared with sales in previous months, auto sales in June were characterized as flat or falling by the Boston, Philadelphia, Atlanta, Cleveland, Chicago, Kansas City, Dallas, and San Francisco Districts. Among the districts that commented on automobile sales, only St. Louis indicated that auto sales rose in recent months.

Home furnishings and home improvement items sold well in the Boston, Chicago, and Kansas City Districts, but New York noted that these products sold less well in its district than they had previously. Apparel sold poorly in the Philadelphia, Richmond, and Chicago Districts, but the Dallas District reported that sales of women's apparel was strong. The environment for travel and tourism was reported to be improving in the New York, Atlanta, St. Louis, Kansas City, and San Francisco Districts, but mixed in the Richmond, Chicago, and Minneapolis Districts.

Manufacturing and Other Business Activity

Manufacturing firms across the county continued to report increases in production, continuing the pattern of strong production gains seen throughout the earlier part of 2004. All districts reported increases in production in June and early July, though the Richmond, Cleveland, and San Francisco Districts reported that the pace of increases slowed somewhat. By contrast, Chicago and Kansas City reported robust activity in their districts, and steel production continued to be brisk throughout the Midwest. Philadelphia, Chicago, and Kansas City also reported that firms' expansion of their capital stock continued at a moderate pace; Boston, by contrast, reported that firms in its district do not plan to add additional capital this year beyond already-budgeted increases.

Reports of scattered shortages and longer lead times are an indication of the strength of demand for manufactured items. For instance, significantly longer lead times for many industrial inputs were reported in the Philadelphia and Richmond Districts. Contacts in the Chicago and St. Louis Districts saw shortages of cement; these shortages had been confined to the East and West Coasts in the past. The Cleveland and Chicago Districts noted that shortages of scrap steel continued to constrain production at some of their facilities.

Transportation-related issues were reported in several districts as well. St. Louis and Kansas City reported delays in coal shipments due to crowded railroad lines; contacts in the Dallas

District also expressed concerns about congested railroad lines. And Boston noted that declines in trucking capacity had resulted in rising shipping prices. Transportation and shipping services were in high demand across the country, with Philadelphia, Richmond, Cleveland, Atlanta, Dallas, and San Francisco reporting strong increases in activity in recent months for the shipping firms in their districts.

Both the Cleveland and Chicago Districts indicated that production at their auto assembly plants was below the levels of this time last year. St Louis reported that an auto manufacturer in its district will idle some of its plants in order to reduce inventories.

Construction and Real Estate

Most districts reported that new home sales stayed strong through the end of June. The Boston, Atlanta, Chicago, St. Louis, Minneapolis, Kansas City, Dallas, and San Francisco Districts all reported rising new home sales in recent weeks. Reports from New York, Cleveland, and Richmond indicated that new home sales slowed in these districts but remained at high levels. Boston reported that higher-priced homes remained on the market longer in its district than they typically have. Cleveland and Minneapolis reported that sales in the lower-price parts of their markets slowed in May and June, though Kansas City reported that this was the strongest-selling market segment in its district.

Commercial construction continued to be weak throughout the country. St. Louis, an exception, said that commercial construction showed some improvement in most of its district. Commercial building in the Kansas City and Chicago Districts was characterized as flat, while activity in Minneapolis's district appeared mixed.

Banking and Finance

Most districts reported increases in borrowing in recent months. Commercial lending improved through the end of June, with the New York, Philadelphia, Cleveland, Richmond, Atlanta, St. Louis, Kansas City, Dallas, and San Francisco Districts reporting rising commercial borrowing in recent weeks. New York, Philadelphia, and Atlanta, however, noted that the increases in their districts were modest. In the Chicago District, commercial borrowing was characterized as flat.

In general, consumer borrowing also rose recently, but seemingly more moderately than commercial borrowing. Within the consumer borrowing category, five districts reported increases in their banks' residential real estate lending: Philadelphia, Cleveland, Richmond, Chicago, and St. Louis. Several of these districts indicated that although overall residential real estate lending had risen, the volume of refinancings fell further recently. Both the New York and San Francisco Districts saw borrowing by homebuyers decline, but San Francisco noted that the levels of residential real estate lending in its district remained high.

Natural Resources and Agriculture

Assessments of the agricultural sector varied according to weather conditions, but demand kept prices high for a variety of products. Cool or wet weather hindered crop growth in the Atlanta, St. Louis, Minneapolis, and Kansas City Districts. Outcomes were reported to be mixed by the Richmond District, as thunderstorms alleviated drought conditions but also caused wind damage. Favorable conditions were noted by Dallas and San Francisco. Cleveland noted that agricultural prices (beef, chicken, and milk) continued to rise for its food processors, while San Francisco noted high prices for beef cattle and other livestock, milk, berries, grapes, and nuts.

Activity in extractive industries remains at a high level. Minneapolis, Kansas City, and Dallas reported higher levels of activity at oil and gas drilling rigs. Minneapolis and Kansas City noted that equipment shortages (and labor as well in the case of Kansas City) were holding back exploration activities. Dallas cited a lack of domestic prospects as limiting drilling activity and noted that oil-field service companies reported excess capacity. Minneapolis also reported that mining activities in its district have been very strong.

Labor Markets, Wages and Prices
Most districts reported strengthening labor market conditions. Employment agencies reported rising demand for labor in the New York, Philadelphia, Richmond, Atlanta, Chicago, and Minneapolis Districts. Reports from other employers were more varied, but still positive, in most districts. The weakest employment reports were from Boston, Cleveland, and Dallas, where reports of employment gains were either mixed (some industries up, some industries down) or relatively rare. Limited occupational shortages were reported in Boston, Cleveland, Chicago, Kansas City, and San Francisco. San Francisco reported the broadest areas of shortage: "skilled occupations in a number of industries, including construction, manufacturing, financial services, and technology services." Overall, however, districts reported only modest wage increases. Boston and San Francisco reported that rising health care costs are a continuing concern for businesses.

A wide variety of material input costs were cited as high and steady or rising by several districts, yet retail price inflation was typically reported to be moderate. All districts reported some form of higher input costs, but the degree to which these costs could be passed on varied by industry and district. Typical reports from manufacturers suggested that they have been unable to charge higher prices to fully offset increases in their input prices. For example Chicago reported, "While more manufacturers reportedly were adding surcharges to at least partially cover these higher costs, many others still said that competition prevented them from passing any cost increases on to their customers." The Cleveland, Atlanta, and Chicago Districts all reported material cost pressures in the construction sector. Atlanta reported that strong demand conditions had made it easier to pass on these higher costs, but Cleveland and Chicago reported that contacts had less success passing on cost increases in construction.

Return to top

First District--Boston

Reports from business contacts in the First District are somewhat more mixed in early July than they were six weeks earlier. Some contacted retailers and manufacturers are less upbeat this time around, although most respondent firms continue to make gains. Many contacts mention rising prices for selected commodities, with some indicating it is becoming easier to pass these cost increases--at least partially--along to customers via slightly higher prices. Residential real estate continues to be a positive factor in the New England economy.

Retail
First District retailers cite mixed sales results in the second quarter. According to contacts, home improvement and building product sales continue to increase by double digits, while furniture sales are mostly flat compared to this period last year. Consumer spending on small-ticket items, such as art supplies and apparel, is stronger than spending on big-ticket items, such as electronic equipment and flooring. A state auto dealers' association reports weak

sales across the board in the second quarter; manufacturers' incentives continue to be popular but are not spurring sales as much as they did earlier.

Inventory levels are up slightly according to most respondents. A number of contacts report cost increases for wood, steel, fabric, and paper goods, which have resulted in slight increases in selling prices. Some respondents indicate that customers are willing to absorb these increases, particularly for paper goods. Employment levels are mostly steady, with some slight increases, although one contact is considering cutbacks. Capital spending is generally in line with plans, some of which call for minimal spending.

Most contacted retailers anticipate that sales will improve slowly in the next six months, while some expect no change or a slowdown. Respondents also express some uncertainty and caution about rising health-care costs, geopolitical instability, and rising interest rates.

Manufacturing and Related Services
Most First District contacts in manufacturing and related services report that sales and orders in the second quarter of 2004 were slightly to well above year-earlier levels. Makers of pharmaceuticals and medical equipment cite particularly large gains. With some exceptions, companies in technology and office equipment businesses did not see as much growth in Q2 as they had hoped. Manufacturers of a wide range of consumer products report new signs of weakness, especially with respect to their chain-store customers.

Manufacturers report that they have been able to pass along steel price increases but that they have been only partly successful in recouping higher costs for raw materials derived from petroleum and natural gas. Transportation costs are increasing as a result of fuel surcharges and regulation-induced declines in trucking capacity. Paper prices are up, generally slightly. Some companies are lowering their costs by sourcing more inputs from Asia, while currency movements have served to raise the cost of European inputs.

Most manufacturers are holding their U.S. headcounts flat or reducing them slightly. Some firms are adding to their sales and product design and engineering workforces. Pay increases are generally running in the 3 percent to 4 percent range, while increases in health-care costs are much higher. However, biotech employment is expanding, and industry contacts report that labor markets have tightened and salary increases are somewhat above the norm in other industries. There are also scattered reports of delays in filling accounting positions.

Capital spending plans for 2004 tend not to be ambitious. Several companies report that they plan to reduce expenditures this year or next after completing major projects. Others are choosing to continue to "hold the line."

The outlook is more mixed than in recent reports. Although many contacts continue to be optimistic about their business prospects in the coming six to twelve months, others are concerned about signs of slowdown in consumer and technology spending.

Residential Real Estate
Residential real estate markets in New England remain strong. Most contacts report high activity levels, although some have observed slightly fewer potential buyers in the last two weeks, which they attribute to vacations. In May, Massachusetts again logged record monthly sales for both single-family homes and condominiums, while the median selling price reportedly increased about 15 percent from a year earlier. Home sales in the state have exceeded the year-earlier month in almost every month during the past year.

Contacts in Vermont and New Hampshire also report double-digit price increases, but contacts in the rest of New England report either stable prices or more modest price increases. Sales remain robust throughout the region and inventory continues to be low. In particular, the lack of affordable housing persists, although higher-priced homes are staying on the market longer in most areas. Contacts do not expect any changes in the next few months.

Insurance
New England-based insurance companies report that their revenues grew moderately in the second quarter, despite a slowing pace of price increases. Sales of life insurance exhibit the strongest growth, and disability insurance providers are seeing a boost from a declining number and duration of disability claims. Sales of annuities are improving, while reports from property and casualty contacts are mixed. Demand from outside the United States, especially Asia, is said to be strong.

Employment is flat or slightly down for most companies, but spending on capital is somewhat healthier, as some companies seek to keep costs in check while attempting to boost profitability. Respondents do not expect the second half of 2004 to be significantly different from the first. Contacts are encouraged by recent economic news, including the rise in interest rates. Price pressures and the looming threat of terrorism are ongoing sources of concern.

▲ Return to top

Second District--New York

Economic growth in the Second District appears to have moderated somewhat since the last report, though most sectors remain buoyant. While input price pressures persist, prices of most consumer goods and services have advanced at a relatively modest pace. The labor market has shown further improvement, though to a lesser degree than earlier in the year. Retailers report that sales softened in June and early July, while selling prices were up slightly, due to less discounting. Business surveys conducted in June and early July suggest some renewed strength in manufacturing-sector activity, and continued upward pressure on input costs.

The housing market remains strong, though not quite as robust as the spring--the sales market has moderated a bit, while the rental market has strengthened. Residential construction remains firm, while construction costs have moderated somewhat. Office markets in the New York City area were mixed at mid-year. Tourism has been particularly robust in recent months, with brisk gains in air travel, hotel occupancy, and theater attendance. Finally, bankers report across-the-board declines in delinquency rates, slight weakening in household loan demand, but further increases in demand for business loans.

Consumer Spending
Retail sales, which had been running well ahead of plan during the Spring, slowed noticeably in June and early July: on a year-over-year basis, same-store sales gains were mostly in the range of 1 percent to 3 percent in the more recent period. Contacts attribute the slowing, in part, to unseasonably cool weather; however, most also characterize the brisk pace of sales earlier this year as unsustainable and indicate that lean inventories of clearance merchandise have hampered sales recently. In fact, most retail contacts maintain that inventories are still

on the lean side. Most contacts note that sales of home goods have softened further, though one describes this category as still strong. In general, retail contacts indicate that effective selling prices are somewhat higher than a year ago, due to fewer and smaller markdowns. Retailers report little in the way of wage pressures, and most continue to indicate that rising energy costs have little impact on total costs.

Consumer confidence was, again, little changed in June. Based on Siena College's survey of New York State residents, confidence edged down last month, led by a dip in the New York City area. At the same time, the Conference Board's survey of Middle Atlantic state (NY, NJ, PA) residents shows confidence rising modestly in June, reversing a modest dip in May.

Construction and Real Estate
Housing markets have moderated somewhat since the last report, though they are still described as strong, particularly in and around New York City. Realtors in all five boroughs report that home prices were up well over 10 percent in the second quarter, compared with a year earlier. A Manhattan industry contact notes that that market for co-ops and condos was fairly robust in June, though less "frenzied" than in April, when low inventories and strong demand sparked numerous bidding wars. Manhattan's rental market, in contrast, has continued to strengthen: one contact notes that a growing number of prospective buyers have opted to rent in recent weeks and reports that rental rates continue to rebound and are now roughly on par with a year ago. New Jersey homebuilders report that demand continues to outstrip supply, keeping prices firm; input costs remain high but are said to have abated somewhat since the last report.

Office markets in the New York City area have been mixed. Vacancy rates have edged down further in Long Island, Fairfield County (Connecticut), and both Midtown and Lower Manhattan. In contrast, northern New Jersey's vacancy rate reportedly ended the second quarter at almost 18 percent, the highest level in nearly a decade. Westchester County's rate rose moderately but was still lower than a year ago.

Other Business Activity
A major New York City employment agency reports continued improvement in the labor market in June and early July, though at a more gradual pace than in the last report. There is reported to have been some renewed softening in demand for IT workers, though this may be partly due to a seasonal slowdown.

Our latest monthly survey of New York State manufacturers indicates further strength in business conditions in early July; continued widespread increases in input costs were noted, but only about one in four firms indicate that they have raised their selling prices. Similarly, June surveys of purchasing managers in both the New York City and Buffalo areas indicate improved business conditions in June. Buffalo purchasers report increasingly widespread gains in both production and new orders, while New York purchasers indicate a resumption in manufacturing sector growth, following a May lull. Purchasers in both areas again report increasing input prices, though these were a bit less widespread than in recent months.

Tourism-related industries continue to turn in very strong results. Airport passenger traffic, year-to-date, is up 15 percent from 2003 levels at New York City area airports and up 10 percent at both Buffalo-Niagara and Greater Rochester airports. Manhattan hotels report that revenue was up more than 20 percent from a year earlier in June, reflecting a 7 percent increase in occupancies and a 14 percent rise in average room rates. Broadway theaters report a further acceleration in business in June and early July, as total revenues were up roughly 12 percent from a year earlier; virtually all of the increase reflects higher attendance, while the average ticket price was little changed.

Financial Developments
Small to medium-sized banks in the district report mixed demand for loans in the latest survey. Loan demand rose slightly in the commercial segments but declined slightly in the consumer category. There was a continued widespread decline in demand for home mortgages: nearly two-thirds of bankers report lower demand, while only 16 percent report higher demand. Refinancing activity decreased, according to 52 percent of bankers, with 21 percent reporting an increase.

Loan rates increased across all categories, with the commercial and industrial segment loan rates registering the most widespread increase. Average deposit rates are reported to be steady to higher. Credit standards remained unchanged according to virtually all respondents. Finally, bankers report lower delinquency rates across all loan categories.

Return to top

Third District--Philadelphia

Economic activity in the Third District was rising moderately in July. Manufacturers reported increases in orders and shipments compared with June. Retailers indicated that sales of general merchandise were strengthening in early July after a slight dip in June. Auto and light truck sales slowed in June and were about steady in early July. Banks reported that overall lending continued on an upward trend, with increases in most credit categories. Service sector firms have seen increased demand and employment agencies reported stepped-up hiring.

The outlook in the Third District business community is generally positive. Manufacturers expect increases in shipments and orders during the next six months. Retailers expect a good pickup in sales for the back-to-school shopping period. However, auto dealers forecast a fairly steady sales rate in the second half of the year, somewhat below the pace of the first half. Bankers expect moderate growth in lending to continue in the months ahead. Service sector companies are optimistic that business will continue to expand.

Manufacturing
Manufacturing activity in the Third District continued on an upward trend in July, and the number of firms reporting gains increased slightly compared with June. About half of the companies surveyed in July posted higher shipments and orders than in the previous month, and around one in ten reported decreases. Overall, there were increases in order backlogs and delivery times at area plants. Increases in new orders were especially strong for firms producing industrial materials and equipment, building materials, and a variety of paper products. Order backlogs have risen markedly among makers of petroleum, metal, and lumber products.

Around half of the manufacturing firms polled in July indicated that the prices of the goods they purchase rose during the month, although some noted that prices for steel and lumber appeared to be leveling off. Many firms continued to express concern about continuing high prices for natural gas. Around one-third of the firms surveyed for this report implemented price increases in the past month for the products they make. About one-third of the firms indicated that they have raised wages recently; most of these reported that the increases were between 2 and 4 percent.

The region's manufacturers expect further expansion in business activity. Half of the firms surveyed in July expect increases in shipments and orders, and less than one in five expects decreases during the next six months. Area manufacturing firms are scheduling increases in capital spending and are planning to add employees in the next six months.

Retail

Third District retailers generally reported a slowing in sales from May to June but some strengthening in early July. Most of the store executives contacted for this report attributed the slower sales in June to unseasonably mild weather, which restrained sales of fans, air conditioners, warm weather apparel, and other seasonal merchandise. Merchants also said store traffic was off as outdoor activities took precedence over shopping for many consumers.

Retailers said the slackening in sales in June left some stores with higher than planned inventories, and these stores were implementing price discounting to move summer merchandise. However, most stores have been keeping inventories relatively light, so extensive discounting is not anticipated. Several stores have already begun back-to-school promotions, and most retailers expect a healthy pickup in sales as the back-to-school shopping period gets under way.

Auto dealers reported a slowing in sales in June compared with May, and roughly steady sales in early July. Inventories have increased well above desired levels at many dealers. On balance, dealers in the region expect total vehicle sales to be steady during the rest of the year, but at a lower level than during the first half of the year. They anticipate declining demand for light trucks to be offset somewhat by higher demand for cars.

Finance

Outstanding loan volume at Third District banks rose slightly in June, according to banks contacted for this report, and the trend has continued in July. Commercial and industrial loans were growing moderately, with much of the gain coming from rising credit needs of service companies and continuing growth in lending to residential construction firms. Residential mortgage lending has also continued on an upward trend. Consumer credit was rising, with moderate increases in credit card lending and somewhat stronger growth in other types of personal loans. Contacts at the region's banks and financial services companies continue to remark that strong competition among bank and nonbank lenders is limiting increases in loan interest rates.

Bankers in the District generally expect overall lending to rise during the rest of the year. They anticipate further moderate gains in business and personal lending. Many expect lending for residential construction and sales to peak soon, but they note that activity in this sector has yet to show signs of easing.

Services

Most of the Third District service firms contacted for this report indicated some recent improvement in business conditions. There has been increased activity in accounting and engineering services and some strengthening in demand for information technology services. General business services activity has also picked up somewhat. Trucking firms reported growing demand for their services throughout the region. Most service sector contacts express cautious optimism that business conditions will continue to improve.

Temporary and permanent employment agencies in the region reported increasing demand for workers. Firms in a broad range of industries are seeking sales and marketing professionals, and there has been growing demand for information technology workers, especially programmers. While staffing companies indicated that firms are stepping up employee searches and hiring, they noted that most companies are adding workers only as their business picks up and staffing needs become pressing.

Return to top

Fourth District--Cleveland

Following significant increases in activity in recent months, the pace of economic activity appeared to slow in the Fourth District through the eight weeks ending June. The pace of production increases slowed for most District manufacturers, though production typically remained above year-ago levels. In the retail sector, several firms reported that sales gains slowed in the late spring. Residential builders reported that sales continued to slow as well, especially in the lower-price part of the market, while business conditions for commercial builders remained weak. By contrast, District banks continued to report rising commercial loan demand. Trucking and shipping firms continued to see strong activity.

Input price pressures remained a persistent feature of the economic environment, with a wide array of metals, energy, and food prices rising in recent weeks. Few firms reported any significant hiring plans for the remainder of 2004.

Manufacturing
The increases in production that were typical throughout the District in the early part of 2004 appeared to taper off in the eight weeks ending June. Nevertheless, production for most manufacturers remained above year-ago levels. These trends were largely the same for both nondurable and durable goods producers. Among durable goods producers, domestic steel manufacturers continued to report strong shipment volumes at a time when they would typically expect demand to decline due to seasonal patterns. In fact, many mills continued to limit the amount of steel they provide to their contract customers. District auto plants appeared to see an increase in production levels in the late spring, but these levels remain below those of a year ago.

Manufacturers typically reported that they were running their plants at or above normal utilization levels. While capacity utilization rates remained particularly strong among steel producers, some noted that they continued to be constrained by shortages of some raw materials. Several durable goods manufacturers reported that their inventories had risen above acceptable levels. Nondurable goods manufacturers, by contrast, continued to report that their inventories were at acceptable levels. Regarding hiring, most firms reported that they had not added additional staff recently, and several durable goods firms foresaw staff reductions in the months ahead. Wage rates reportedly remained stable in recent weeks.

In general, input costs continued to increase for manufacturers in May and June. Prices for various metals, including aluminum and steel, rose further recently; these prices reportedly remained significantly above their levels of a year ago. And several food processing firms reported that prices for some foods increased sharply in recent weeks, including milk, chicken, and beef. Finally, prices for petroleum-based products also continued to rise. Several producers reported that they could partially pass these input cost increases through to their customers.

Retail Sales

Several District retailers reported that sales gains slowed in the late spring. This follows the robust increases in spending that occurred earlier in 2004. Many contacts attributed the recent sluggishness in sales to unseasonably cool temperatures throughout the District in the eight weeks ending June. Some also noted that fewer markdowns might have held consumers back. On a year-over-year basis, discount stores saw sales gains, while sales at department stores were typically weaker. Several contacts also indicated that the Midwest has tended to see slower sales growth recently than other parts of the country.

Retailers reported holding less inventory than at this time last year. While wage rates remained steady, increases in input costs were more widely reported than in the recent past. Increases in food prices were especially pronounced recently, affecting restaurateurs and grocers. Nevertheless, the prices of many other categories of goods continued to fall, for example, electronics and apparel.

In general, new car sales were sluggish throughout most of the District in May and June, though sales in northeastern Ohio were reportedly robust during this period. In addition, several dealers reported that sales of larger vehicles remained strong despite high gasoline prices.

Construction

Reports from residential builders pointed to a further slowing in sales in the last several weeks. The decline in demand seemed particularly evident in the lower-price part of the market, which builders view as being more sensitive to increases in interest rates. Indeed, many builders attributed the recent slowing in sales to rising mortgage rates and are altering their financing products accordingly in an attempt to make them more attractive. In contrast to previous reports, many homebuilders now expect that sales in 2004 will not surpass those seen in 2003. While input costs are still said to be higher than in the winter and at this time last year, they have reportedly remained steady in the last several weeks.

After some signs of improvement in previous months, business conditions for commercial builders reportedly remained weak through the eight weeks ending June. One exception was school construction, which continued to be a bright spot in an otherwise weak environment. It is reported that input costs continued to rise for commercial builders, especially for items such as steel, lumber, concrete, and petroleum products. Only a few contacts reported that they could fully pass input cost increases on to their end consumers.

Banking

Loan demand from commercial clients reportedly remained strong in the eight weeks ending June and has also increased from this time a year ago. District banks have reported stronger commercial borrowing consistently since the beginning of this year. By contrast, consumer loan demand was mixed in May and June. Some institutions continued to report strong residential real estate lending, though the rate of refinancing activity has continued to slow. Delinquency rates reportedly remained largely unchanged in recent weeks, and applicant credit quality was characterized as stable or slightly improving. Contacts reported that their core deposits had grown both in recent weeks and relative to this time a year ago. With respect to hiring, some institutions indicated some difficulty finding qualified entry-level employees, despite an abundance of applicants.

Trucking and Shipping
Contacts from the trucking and shipping industry continued to report robust conditions in May and June, with shipment volumes rising in recent weeks and advancing ahead of those from this time a year ago. As has been the case for some time, demand came from an array of industries. It was reported that requests to ship steel were especially strong, and foreign shipments of steel were said to be the strongest in approximately three years. All trucking companies reported running their fleets near capacity. Several noted that they plan to purchase trucks to expand their fleets soon, though truck orders can take up to six months to fill. Input costs continued to be high, with fuel prices fluctuating in recent weeks but reportedly staying stable on average. Finally, firms reported that drivers were demanding higher wages recently.

Return to top

Fifth District--Richmond

Overview
The Fifth District economy expanded at a more moderate pace in June and early July, restrained by softer retail sales and slower growth in manufacturing output. Retailers reported fewer customers in District stores and said that their sales slumped in recent weeks. Manufacturing shipments expanded more slowly in June, and new orders and employment were flat. Services businesses, in contrast, generally reported strong revenue and employment growth, although summer vacation schedules apparently slowed real estate activity in some areas. In finance, commercial lending picked up, but residential mortgage lending was sluggish as refinancing activity dwindled. While a number of contacts reported markedly higher prices for fuel and building materials, prices in the manufacturing and services sectors were said to be rising at an average annual rate of less than 2 percent. In agriculture, summer thunderstorms brought relief to dry fields in Maryland and South Carolina but caused wind damage to crops in some areas of the Carolinas.

Retail
District retailers generally reported flat to lower sales in the weeks since our last report. A contact at a large discount chain said that while sales remained relatively solid, higher gasoline prices had trimmed his sales somewhat; in his words, "when gasoline prices go up, there's less money to spend." A contact at a normally busy Washington, D.C., beltway anchor store told us mall traffic was down, and the manager of a clothing store in central West Virginia said apparel sales were "in the doldrums." Retail employment was generally flat in June and July. A department store manager in Gastonia, N.C., for example, said his store increased hours for part-time workers rather than hire additional full-time employees because sales were flat.

Services
Contacts at services firms told us that demand had picked up in recent weeks. A manager at a Tidewater Virginia rental outlet that specializes in tools said his revenues were well above a year ago, and a national trucking firm with offices in North Carolina reported stronger demand for freight transportation services. There were scattered reports of adverse impacts from higher prices in the services sector. The owner of an architectural firm in the Baltimore, Md., area, for example, expressed concern that higher prices of construction materials might

limit the number of new construction projects--potentially reducing his business. In addition, a trucking firm in North Carolina reported that a run-up in fuel prices had not been fully passed through to customers, squeezing its profit margins.

Manufacturing
District manufacturing activity generally advanced at a somewhat slower pace in June. For the most part, shipments grew more modestly than in May, while gauges of new orders and employment were essentially flat. However, manufacturers in the chemicals, fabricated metal, plastics, and lumber industries reported that shipments and new orders picked up. A plastics manufacturer in North Carolina noted that his firm was seeing signs of an expanding economy, citing "longer lead time on raw materials, raw material price increases, decent new order activity, and slight increases in wages." In contrast, several District furniture manufacturers reported continued declines in demand. A furniture manufacturer in Maryland told us that retail furniture sales were slow. He also noted that the price of cherry wood had risen sharply in recent months. Overall, however, our contacts indicated that manufacturing price increases remained generally modest, as prices rose at an average annual rate of about 2 percent.

Finance
District bankers reported a pickup in the demand for commercial loans in recent weeks but said that demand for home mortgage loans was constrained by sluggish refinancing activity. Contacts cited modestly higher demand for commercial loans, supported by increased merger and acquisition activity. Several bankers, however, commented that commercial borrowing activity continued to be hampered by businesses' hesitancy to make capital expenditures. A lender in Richmond, Va., noted that there was "no sense of urgency [on the part of businesses] to borrow for capital expansion." Residential mortgage lenders said that while new home originations remained healthy, mortgage refinancing activity had dried up.

Real Estate
Although realtors reported that interest in home buying had backed off as the summer vacation season arrived, the pace of home sales in the District remained fundamentally strong. Contacts in the Washington, D.C., and Fairfax, Va., areas reported brisk home sales, though they noted some growth in inventory. A contact in Washington, D.C., told us the market for condominiums and co-ops, however, remained "plain crazy." Reinforcing the strong tone, a contact in Fredericksburg, Va., said home sales in her area continued to be robust and a Greensville, S.C., realtor said sales there were "unbelievable." A realtor in Northern Virginia said home prices were still going up but "not stopping a thing." A homebuilder with operations in both Virginia and the Carolinas, however, said he had noticed that customer traffic in new homes had diminished somewhat. On the price front, homebuilders continued to report higher prices for lumber, concrete, sheet metal, and steel.

Fifth District realtors reported that commercial leasing activity slowed considerably during recent weeks, partly because of the normal seasonal lull. "It's the annual summer routine, everyone is on vacation, it's hard to schedule meetings, and the deals just don't get done," noted one realtor in Washington, D.C. Despite the seasonal slowdown in most of the District, a contact in Columbia, S.C., reported that the local market had strengthened during the last month as "office space is hot and retail space is on fire." Rents across all sectors were generally flat since our last report and new construction activity remained spotty.

Tourism

Tourist activity was mixed since our last report. Hoteliers at Virginia Beach, Va., and Myrtle Beach, S.C., reported stronger bookings for the Fourth of July holiday weekend compared to a year ago. Furthermore, they noted that because the holiday fell on a Sunday, bookings rose substantially during the weeks before and after the holiday as vacationers stretched out the weekend. In addition, a manager at a mountain resort said that time-share sales were doing extremely well with many buyers paying in full at closing. In contrast, a contact on the Outer Banks of North Carolina indicated somewhat weaker bookings compared to a year ago, which she attributed in part to bargain-hunting vacationers waiting until the last minute to book rooms.

Temporary Employment
Contacts at District temporary employment agencies reported that stronger economic conditions led to increased demand for workers in recent weeks. A contact in Northern Virginia noticed more interest in administrative assistants from nonprofit agencies and general corporations, and in Raleigh, N.C., workers with engineering, sales, and customer service skills were more widely sought.

Agriculture
Somewhat warmer-than-normal temperatures coupled with scattered thunderstorms were a mixed blessing for District farmers in recent weeks. Thunderstorms caused some wind damage to crops in the Carolinas and moisture damage to the hay crop in West Virginia. But the recent rainfall was welcomed in areas of Maryland and South Carolina where high temperatures and sporadic precipitation had stressed corn crops. On a brighter note, the cotton and soybean crops were in excellent condition in Virginia, and the peach crops in Maryland and South Carolina remained in good to excellent condition.

Return to top

Sixth District--Atlanta

Summary
According to business contacts, economic activity in the Sixth District remained positive in June and early July. Several retailers, however, noted that sales have been slower than in previous months. Auto dealers, in particular, reported disappointing June sales. Residential housing construction and sales remained vigorous, while commercial real estate markets posted modest improvements. Industrial contacts reported improving manufacturing activity, and demand for transportation services was strong. Tourism activity remained solid, while business travel improved and responses from the financial sector were upbeat. The demand for labor continued to improve in some sectors, although only marginal wage increases were reported. Several contacts noted price increases for selected goods.

Consumer Spending
Reports from District retail contacts indicated sales during June and early July had slowed from previous months. Overall, most contacts said that sales during June and early July were flat to slightly higher compared with a year ago. Retailers in Georgia and Florida were said to be hopeful that a tax-free week at the end of July would boost sales. New vehicle sales in June were lackluster, although new cash incentives reportedly boosted traffic and sales in early July. District contacts reported that weak June sales performance extended to some previously strong selling segments. Used car dealers noted a continued pick-up in demand, with some reporting improving prices on some classes of vehicle.

Real Estate
District single-family housing markets remained robust in June and early July. Reports were strongest among Florida contacts, and especially within the condominium segment. Home sales and construction were similar to strong year-ago levels in most other parts of the District. Home prices continued to increase in many areas, and contacts continued to note higher building material costs. There was concern expressed by some Realtors that home sales may moderate through year-end, but most contacts anticipated District housing markets will remain at high levels.

Optimism continued to grow among commercial real estate contacts as modest improvements in leasing activity were noted and the amount of sublease space declined. Construction remained at low levels but reports of plans for new development increased. The majority of commercial construction underway was in the retail sector.

Manufacturing and Transportation
Manufacturing activity continued to improve in several industries. For instance, contacts reported increased demand for drilling equipment, manufactured homes, heavy trucks and trailers, and processed building materials. These producers were boosting inventories of finished products in response to the growing demand. However, one contact suggested that inventories for linerboard for shipping containers was low because strong demand had outstripped capacity. Producers of chemical products reported improving pricing, and some had increased inventory levels to take advantage of bulk purchasing discounts. Contacts reported new projects and jobs created in the defense and aerospace sector in Alabama. Some tractor and trailer manufacturers were running at full capacity and several noted difficulty meeting delivery dates for orders. The transportation equipment industry was reportedly expanding production in the region, and demand for transportation services by manufacturers remained strong. More layoffs were recently announced in the District's apparel industry.

Tourism and Business Travel
Reports from the District's tourism and hospitality industry were positive in June and early July. In south Florida, activity was very strong, bolstered by international visitors. Hotels reported strong occupancy numbers and some restaurants posted record sales. A few reports indicated that business travel was increasing and that bookings for conventions and business meetings for upcoming months were strengthening.

Financial
Responses from the region's financial sector were mostly upbeat. Loan quality was good, and past dues remained low. Higher rates on term loans had not dampened loan demand, according to some. Indeed, several contacts noted continued strong activity in the real estate sector, especially in Florida. Demand for industrial and commercial loans was reported to have improved only modestly. The pace of merger and buyout activity in the banking industry picked up, and several reports noted that layoffs are likely when branch offices are consolidated.

Employment and Prices
Demand for workers remained strong in several sectors, such as healthcare, construction, hospitality, and security. Staffing service contacts reported that the demand from the manufacturing sector was also picking up. Employment advertisements in several major newspapers increased significantly from a year earlier. Only modest wage increases were

noted in general. One report suggested that manufacturing wage increases were lagging other sectors, because of the large pool of available workers from past layoffs.

Several reports cited instances of rising prices for building materials and food products, and that these were mostly being passed on to final users. Contacts noted that some food prices had increased notably over the past few months. High prices for lumber, metals, and cement remained a challenge to builders, although strong demand has made it easier to pass on these higher costs in new building projects.

Agriculture
Above normal precipitation slowed farming activity across the District. Excess soil moisture conditions were reported in areas of Alabama, Louisiana, and Mississippi. Recent USDA estimates placed cotton acreage higher than expected and contacts expect some further downward pressure on prices. Poultry exports from the District continued to improve.

Return to top

Seventh District--Chicago

Summary
The Seventh District economy continued to expand solidly in June and early July, despite a slight softening in consumer outlays. Business spending continued to rise, and hiring remained stronger than earlier in the year. Overall construction and real estate activity moved slightly higher, with strong gains on the residential side. In general, manufacturing remained strong. Lending volumes were again relatively flat. Producers' input costs remained elevated, though there were fewer reports of further increases. Retail price increases and upward wage pressures were largely subdued. Crop conditions improved in the southern portions of the District, but continued to lag and even deteriorate in the northern parts.

Consumer spending
Consumer spending softened slightly since our previous Beige Book report. Most retailers said that total sales came in below plan during June. However, a contact with one national chain said that the firm's results improved early in July and were above trend. Merchants reported that home furnishings, electronics, and lawn and garden goods were selling well, while apparel continued to lag. One retailer indicated that inventories for some product lines were too lean, resulting in lost sales. District auto dealers said that showroom traffic and light vehicle sales were slow in June. Most said that business had not improved noticeably by mid-July, but pointed out that the bulk of light vehicle sales have been taking place in the latter half of each month. A few auto dealers noted that parts and service sales had increased recently. Some contacts said that cool, rainy weather was hampering tourism activity, particularly in Wisconsin and Michigan. However, a tourism contact in Chicago said business was up from last year, and a major airline noted that bookings had risen recently in response to fall travel deals. A large regional theater chain reported that ticket and concession sales were strong in June.

Business spending
Reports generally indicated a further pickup in business spending, though many firms remained cautious. The number of firms that were increasing capital outlays continued to rise moderately. In addition, one information technology executive said there was a solid, across-the-board pickup in business technology spending. More firms reported adding to their

advertising spending. Business travel was said to be rising as well. With regard to hiring, staffing firms reported that demand for temporary workers remained very strong, though year-over-year increases in new orders seemed to plateau in June. An executive with one temp help firm was confident enough in the firm's growth outlook to "fire" some of its higher-volume, but lower-paying customers. Another noted that orders for permanent hires were "pouring in the door," particularly for IT, professional, sales, and skilled-trades workers. Outside of reports from temporary help agencies, firms generally were more bullish on their hiring plans than during the previous Beige Book period. We continued to hear isolated reports of labor shortages. A dearth of truck drivers in the District seemed to intensify recently, forcing one major freight carrier to turn away new business. In addition, railroads were scrambling to hire new workers to meet rising shipping demand and ease delays.

Construction/real estate

Housing and construction activity increased again in June and early July. Contacts reported that sales of both new and existing homes were very robust in June, with several expressing surprise at the resiliency in demand. Many Realtors and builders suggested that the latest surge in home purchases was spurred by buyers' expectations for higher interest rates. Nonetheless, some homebuilders were confident enough in the strength of underlying demand to take on new spec projects. Overall nonresidential activity changed little since our previous report, and remained somewhat soft. Contacts in the Chicago market reported that an influx of new and sublease space was pushing up vacancies, and that landlords were boosting concessions. Office markets elsewhere in the District appeared more stable, and there were even reports of an uptick in small lease deals in some markets. While conditions in light industrial real estate were largely unchanged, one major development company suggested it was becoming more aggressive in developing spec space in the region, particularly in the Chicago and Indianapolis areas.

Manufacturing

Manufacturing activity remained strong in June and early July, and despite some stock building, inventories still were lean through much of the supply chain. Some materials producers (steel, gypsum wallboard, and cement) said that there was no letup in demand in recent months. Steel inventories were said to be up at service centers, but down at factories. Contacts in gypsum wallboard and cement said that both industries continued to run near capacity. Cement shortages, which had been limited to areas on the East and West Coasts, were spreading to other regions, including the Midwest. Producers of heavy equipment indicated that new orders continued to run well above year-earlier levels and that inventories were at all-time lows. A large producer of home appliances announced that it was recalling some furloughed workers to meet rising demand. Moreover, another large appliance maker said that strong demand was leading some retailers to increase inventories. By contrast, automakers reported that inventories jumped unexpectedly in June as light vehicle sales slumped nationwide. One producer said that its assembly plans for the third quarter were below year-earlier levels.

Banking/finance

There was very little change in the pace of financial activity in June and early July. On the household side, new mortgage originations were still strong while refinancing activity was relatively soft. Lenders reported that household credit quality continued to improve and there were no changes in loan standards and terms. Business loan volumes remained fairly flat, well below many bankers' expectations. Lenders suggested that businesses were still relying on their flush cash positions to meet liquidity needs rather than borrowing. While overall business loan quality continued to improve, there were more reports of banks compromising on covenants to attract business.

Prices/costs
Prices for some inputs, such as steel and energy, generally have leveled off, but remain elevated. While more manufacturers reportedly were adding surcharges to at least partially cover these higher costs, many others still said that competition prevented them from passing any cost increases on to their customers. One builders' association said that higher materials prices had pushed the cost of building a home up roughly 10 percent, and that builders had been able to pass along only a small portion of that increase to home buyers. At the retail level, price increases remained largely subdued due to intense competition. Regarding wages, contacts reported little change from the previous reporting period, with increases mostly contained.

Agriculture
Corn and soybean crop conditions improved in the highest producing parts of the District (Iowa, Illinois, and Indiana) as warmer weather helped make up for earlier setbacks. In Michigan and Wisconsin, however, fewer acres were classified in good or excellent condition compared to the previous Beige Book reporting period. With higher milk prices this year, more dairy producers have been able to meet loan payments and update equipment. Farmland values increased once again, with substantial demand coming from nonagricultural investors, including those seeking land for recreational uses.

Return to top

Eighth District--St. Louis

Summary
Business activity in the Eighth District continued to improve since our last report. Despite growth in many areas, however, some contacts in manufacturing and services reported plant closings and layoffs. Retail and auto sales increased in June over year-earlier levels. Residential real estate markets continued to do well in the District, and commercial markets appear to be stabilizing. Total loans at a sample of small and mid-sized District banks increased between mid-March and June.

Manufacturing and Other Business Activity
Manufacturing activity in the District increased in many industries. Firms in the garden tools, plastics manufacturing, packaging, and automotive parts industries reported plant expansions, openings, and employment increases. A contact in the aerospace industry reported plans to train displaced automotive industry workers to manufacture aerospace parts. Despite the improvement in some areas, there have been reports of plant closings, company reorganizations, and layoffs. Affected industries include printing, electronics, automotive tire, home appliance, and industrial parts. A District automotive manufacturer will idle some of its plants this summer in an effort to reduce inventories of sport-utility vehicles. Several District coal producers reported shipment delays due to congested and overloaded freight rail lines. Contacts in the construction industry reported cement shortages and increasing prices. Contacts attribute the shortage of cement to the rise in steel demand abroad, arguing that many of the ocean vessels that would be used to import cement are tied up shipping steel.

In the services sector, firms in the tourism industry have reported facility openings and increases in hiring, while firms in the health services, correctional, and telecommunication industries reported workforce reductions. Business activity in the retail services sector was strong. Contacts reporting store openings included boutique grocery, furniture, outdoor equipment, clothing, electronics, office supply, and building materials retailers. Discount retailers reported sales growth in June compared with May. Retailers also noted stronger sales growth in June compared with the same month a year ago. Most District auto dealers reported increased sales in June compared with May. In addition, contacts reported higher sales in June compared with year-earlier levels.

Real Estate and Construction

The housing market continues to do well in the Eighth District. May year-to-date home sales in the Memphis area were up 13 percent compared with the same period in 2003, and in the greater St. Louis area the growth was 5.8 percent. Residential construction is still strong in most of the District's metropolitan areas. Year-to-date permits increased throughout the District in May 2004 compared with May 2003. There was a 10 percent growth in year-to-date permits in the St. Louis County area. Construction has picked up in northeast Arkansas, where builders are optimistic about the second half of the year, and has remained steady in rural west Tennessee.

The District's commercial real estate market may be stabilizing. Office vacancy rates for downtown St. Louis increased only slightly to 22.8 percent in the first quarter of 2004 from 22.5 percent in the last quarter of 2003. The downtown Louisville vacancy rate fell to 20.4 percent from 21.0 percent, while in downtown Memphis the rate increased slightly from 23.4 percent to 24.5 percent. The industrial vacancy rate for the Louisville metropolitan area increased to 18.3 percent in the first quarter of 2004 from 16.7 percent in the last quarter of 2003. Commercial construction has shown some improvement in most of the Eighth District. Overall commercial construction in the St. Louis area increased by more than 6 percent during the first 5 months of 2004 compared with the same period in 2003. Contacts reported that construction in north central Arkansas was up significantly compared with the previous year and that the market continued to improve in Memphis and rural west Tennessee.

Banking and Finance

Total loans outstanding at a sample of small and mid-sized District banks were up 4.2 percent from mid-March to late June. This increase stems from a 3.0 percent rise in commercial and industrial loans along with a 4.8 percent increase in real estate loans. Loans to individuals and loans to commercial banks showed declines of 3.1 percent and 22.9 percent, respectively. During the same period, total deposits at these banks decreased 4.6 percent.

Agriculture and Natural Resources

While the rains have subsided for some District states, others are still plagued by wet weather and flooding damage in certain areas. Most ratings of soil moisture levels continue to be adequate or surplus. In every District state, at least 50 percent of each crop, including over 75 percent of the corn crop, has been rated in good or excellent condition. Livestock and pastures are mostly in good condition.

Every District state has completed more than 90 percent of its winter wheat harvest. The growth of corn, soybeans, and sorghum is ahead of normal in the District, while cotton growth is keeping pace with its five-year average.

▲ Return to top

Ninth District--Minneapolis

From early June through mid-July the economy in the Ninth District grew modestly. Growth was noted in residential real estate, construction, manufacturing, mining, energy and consumer spending. Conditions were mixed in commercial real estate, tourism and agriculture. District employment relative to last year picked up considerably, while wage increases were moderate. Significant price increases were noted for building materials, food products and freight.

Construction and Real Estate

Commercial construction and real estate activity was mixed. A development official reported Sioux Falls, S.D., is in the midst of a construction and renovation boom, with what may be the busiest year on record. Fargo, N.D., continued its stable growth path, including the construction of a 50,000-square-foot corporate headquarters and two big box sports retailers.

However, in Minneapolis-St. Paul, activity was more stagnant. The vacancy rate for industrial space remained significant, as industrial absorption was slow. Representatives from a large real estate firm noted that inquiries increased, but manufacturers await another positive quarter to purchase more space. The office market remained mostly unchanged with plenty of unused space, but the practice of offering more concessions to prospective tenants has leveled.

Residential real estate activity grew. Housing units authorized in district states grew 5 percent for the three-month period ending in May compared with a year ago. About 20 percent more home sales closed in June compared with a year ago in the Minneapolis-St. Paul area. However, one realtor noted that sales among lower-priced homes were slower. A bank director described the housing market in Billings, Mont., as tight, with prices and buying activity up.

Consumer Spending and Tourism

Overall consumer spending increased modestly. A major Minneapolis-based retailer reported same-store sales during June were 2 percent higher than a year ago. A manager at a Minneapolis area mall reported June traffic increased moderately, while another Minneapolis area mall manager noted that June traffic was up 12 percent compared with a year ago. Traffic and sales at a Minnesota mall outside the Minneapolis-St. Paul area were up about 1 percent to 2 percent in June compared with last year. In Montana, a mall manager noted that sales were up 7 percent in May from a year ago, and that June traffic was solid. However, preliminary results of a survey of retailers in Minnesota, Montana and North Dakota conducted by the Minneapolis Fed and state retail associations showed that overall sales were flat during the three-month period ending in June. A Montana bank director said that recent auto sales were generally about the same as a year ago.

Tourism was mixed, but the outlook is strong. Tourism was down substantially in June due to cool, wet weather in the Upper Peninsula of Michigan, according to a tourism official; however, hotels reported that bookings recently picked up for the remainder of the season. June tourism activity was about the same as a year ago in South Dakota, with strong bookings noted for July and August in the Black Hills. Recent tourism activity and advanced reservations were strong in Montana, according to a tourism official.

Manufacturing

Manufacturing activity increased. A June survey of purchasing managers by Creighton University (Omaha, Neb.) indicated strong growth in manufacturing activity in the Dakotas and Minnesota. A chemical company announced plans to double manufacturing capacity at a Minnesota facility, and a watercraft maker plans to expand production. A bathtub maker in the Upper Peninsula reported strong sales and is operating three shifts a day, six days a week. A machine manufacturer in western Wisconsin noted slightly stronger sales than a year ago and is somewhat optimistic about the near future as customers add shifts and run their machines at capacity.

Energy and Mining

Activity in the energy and mining sectors remained strong. Early July district oil and natural gas exploration increased slightly from early June levels. A bank director from Montana noted that the demand for exploration and drilling equipment has exceeded the available supply. In North Dakota, a plant that makes natural gas from coal shut down for unscheduled repairs. Meanwhile, prices for most major district mining commodities remained strong. District iron ore mines continued to produce at capacity; however, labor contracts for many mine workers will expire at the end of July. The operating mines in Montana produced at near capacity. "Prices have been steady at the higher levels," reported a Montana mining official.

Agriculture

Agricultural conditions were mixed. Cool weather hindered crop growth. Crop progress fell behind the pace of last year and the five-year average for most district crops. The U.S. Department of Agriculture forecasts that 2004 production of winter and spring wheat in the district will fall 16 percent and 10 percent, respectively, from 2003. The USDA, responding to drought conditions, allowed expanded grazing on restricted lands. However, increased rainfall somewhat relieved drought conditions in the western part of the district. As a result, a Montana bank director noted that yields for hay and grain in central Montana could be near record levels.

Increased crude oil prices drove up the input costs for many agricultural producers. The USDA forecasts that wheat, corn and milk prices will soften somewhat from the recent strong levels, and prices for livestock, hogs and broilers will increase slightly.

Employment, Wages, and Prices

Employment increased since the last report. In Minnesota, a distributor of electronic components could hire at least 300 new employees by the end of 2004, and a recreational vehicle company recently announced plans to add 150 new jobs. A South Dakota company that sells auto insurance over the Internet plans to add 240 new positions over the next three years. Applications for unemployment insurance were down about 18 percent in Minnesota during June compared with a year ago. A temporary staffing agency survey showed that 29 percent of employers in Minneapolis-St. Paul expect to hire more workers during the third quarter of 2004, and 4 percent expect to reduce payrolls. Last year 21 percent expected to increase payrolls, and 11 percent planned reductions. A trucking association representative noted difficulty finding quality truck drivers.

In contrast, a call center in North Dakota will close at least temporarily in August, resulting in about 260 layoffs. A computer company in South Dakota laid off 300 employees after closing a plant in June. Restructuring at the U.S. Forest Service could result in 15 layoffs at one Montana office, according to the supervisor.

Wage increases remained moderate. Nurses at a hospital in the Upper Peninsula recently signed a contract that includes an annual 4 percent wage increase, but also agreed to pay more for health insurance. A Minnesota bank director noted that recent increases in wages and benefits for building trade unions have ranged from 3 percent to 6 percent.

Significant price increases were noted for building materials, food products and freight. Steel prices were up at least 25 percent and seem to increase every three to four months, according to a bank director. A major food product producer and distributor based in Minneapolis recently announced plans to raise prices on several food products, including soups, frozen breakfast food and yogurt. Merchants in northern Montana reported higher freight costs, as much as 30 percent. Gasoline prices in Minnesota were down 29 cents in the beginning of July compared with prices in May, but were 27 cents higher than a year ago.

Return to top

Tenth District--Kansas City

The Tenth District economy continued to expand in June and early July, albeit at a slightly slower pace than in the previous survey. The manufacturing, housing, energy, and travel sectors all posted strong gains, and labor markets continued to improve. On the other hand, retail and auto sales were generally unchanged, and commercial real estate remained weak. Wage and retail price pressures were still muted, and manufacturing price increases eased slightly.

Consumer Spending
Consumer spending in the district generally held steady in June and early July. Most retailers reported flat sales compared with the previous survey, although sales were still above year-ago levels at most stores. Among product categories, sales of home items were generally characterized as strong, while no category was consistently reported as weak. Most store managers were satisfied with inventories, and virtually all managers anticipate solid increases in sales through the fall. Motor vehicle sales in the district were also generally unchanged compared with previous months and were flat to slightly lower compared with a year ago. Dealers appeared relatively satisfied with inventory levels, although some planned to trim stocks modestly heading forward. Most dealers anticipate steady sales through the fall, as manufacturer incentives are generally expected to remain in place. Travel and tourism activity continued to improve solidly in June and early July. Airport traffic set new records in several district cities and was above year-ago levels throughout the district. In addition, contacts reported that there were still few signs of a negative impact of high gasoline prices on tourism.

Manufacturing
District manufacturing activity continued to grow strongly in June and early July. Most manufacturers were operating at high levels of capacity utilization, and new orders generally remained strong. Many firms reported they were adding employees and extending hours, in some cases by adding an entire shift. With the strong recent activity, supplier delivery times were up considerably from a year ago, and a number of plant managers continued to report difficulties obtaining steel and some other raw materials. Coal was also in short supply in some areas due to rail transportation bottlenecks, and some coal-using plants were considering temporary production cutbacks as a result. Firms generally reported steady

increases in capital expenditures, and nearly all plant managers expect growth in factory output to remain very strong for the rest of the year.

Real Estate and Construction

Residential real estate activity continued to grow solidly in June and early July, while commercial real estate remained generally weak. Single-family housing starts rose further in most cities and were above year-ago levels across much of the district. As in the previous survey, most builders said demand was strongest for entry-level houses. Shortages of some materials--particularly steel products and cement--were reported in several areas, and some builders were worried that cement could become even more difficult to obtain in the months ahead. Builders generally expect solid construction activity to continue for the rest of the year, with little, if any, impact from rising interest rates. Residential realtors reported further increases in home sales--particularly for low- and mid-priced homes--as well as moderate rises in home prices since the previous survey. Heading forward, realtors generally expect sales to continue at a high level and home prices to increase modestly. Mortgage lenders reported that demand for home purchase loans was up moderately in most areas, more than offsetting a general easing in refinancing activity. Lenders expect refinancings to continue to taper off in the months ahead, but for overall mortgage demand to remain solid. Commercial real estate activity remained generally weak. Vacancy rates were up slightly in some areas, and commercial construction was generally flat. On the positive side, realtors in Denver reported that demand from new tenants resulted in some decline in "shadow" space--space that was previously leased but unoccupied and not on the market. Commercial realtors also expect some improvement in office markets by the end of the year.

Banking

Bankers report that loans increased and deposits held steady since the last survey, boosting loan-deposit ratios. Demand rose for commercial and industrial loans, residential construction loans, and commercial real estate loans. Demand for other loan categories was little changed from the previous survey. On the deposit side, all types of accounts held steady. All respondent banks left their prime lending rates unchanged, and all banks either raised their consumer lending rates or planned to do so in the near term. Lending standards were unchanged.

Energy

District energy activity expanded solidly in June and early July. The count of active oil and gas drilling rigs in the region was up moderately from the previous survey and up strongly from a year ago. In addition, some producers said they would have expanded even further were it not for continuing regulatory constraints and labor and equipment shortages. Although problems finding workers and adding equipment are expected to intensify in the months ahead, most contacts anticipate further slight increases in drilling, as energy prices are generally expected to remain elevated.

Agriculture

Agricultural conditions remained solid in June and early July. Rain and cool weather significantly improved pasture conditions, although not enough to spark herd expansion. The rain arrived too late for the winter wheat crop, however, causing intermittent sprouting that decreased quality in some regions. Spring-planted crops were generally in good condition, although the persistence of cool weather far into the season slowed maturations, particularly for corn. Overall, bankers and producers were optimistic about farm incomes this year, expecting them to be close to last year's strong levels.

Wages and Prices
Wage and retail price pressures generally remained muted in June and early July, and growth in manufacturing prices eased slightly. Labor markets continued to show solid improvement, with hiring announcements exceeding layoff announcements by a wide margin. Moreover, district layoffs since the last survey were largely concentrated in the telecommunications industry, while hiring announcements were distributed across a broad spectrum of industries. Most firms did not have to raise wages more than normal to attract workers, though some worker shortages and wage pressures continued to be reported in the energy, manufacturing, transportation, and health care industries. As in previous surveys, retailers reported flat selling prices for most items and expect most prices to remain stable heading forward. Prices for some furniture and flooring items, however, did continue to rise slightly, and some managers expect rising delivery fees to boost retail prices modestly in the months ahead. Builders reported further price increases for most construction materials and generally expect these increases to continue. Manufacturers also continued to report rising materials and output prices, though these increases were somewhat smaller than in previous months. Factories expect further increases in raw materials and finished goods prices in the months ahead. District steel producers, for example, said they planned to raise output prices in the second half of the year due to strong demand and rising costs of steel scrap. These plans represent a change from the previous survey, when the same firms said they planned to lower output prices in response to an easing in steel scrap prices in the spring.

Return to top

Eleventh District--Dallas

Eleventh District economic activity continued to expand from late June to mid-July. Manufacturing activity increased and activity strengthened in the service sector. Retailers reported some softening of sales growth over the past few weeks. Construction and real estate activity continued to improve. The financial services industry said lending was up slightly, but deposit growth has softened because money is returning to financial markets. Energy activity was mostly unchanged. Agricultural conditions remain favorable.

Prices
Price pressures are mixed. A number of manufacturing industries continued to report higher selling prices but the rate of growth in price increases slowed for some products and retailers reported some softening of pricing power. Transportation and energy costs remain a concern for many industries.

Crude oil prices remained volatile, peaking at an all-time high on June 1, drifting down in mid-June, and then surging back up again. Domestic consumption of crude oil has softened in recent weeks, falling back to levels near a year ago. Inventories are back up to the five-year average. Natural gas prices have stayed relatively high, between $6 and $6.50 per thousand cubic feet.

Producers of fabricated metals report that shortages for some inputs are driving up prices and causing some construction projects to be delayed or cancelled. Primary metals producers say rising input costs are being passed along to customers, although margins are less than a year ago. Shortages of scrap remain a concern. Contacts say that China was driving up the prices of scrap a few months ago, but now it's the domestic steel mills driving up prices.

Producers of clay, cement, brick, tile and glass continue to report cost pressures from higher input and transportation costs. These producers say they are able to pass some of these cost increases on to customers. Prices are up for paper, recycled materials and pulp. Strong demand combined with capacity limits pushed up prices for chemicals, such as chlorine, benzene, styrene and polyvinyl chloride, although price increases slowed for other chemicals. Apparel manufacturers say that prices continue to decline.

Price reports from retailers were mixed. Some retailers say customers are less resistant to price increases and selling prices are up, particularly for women's apparel. Other retailers say price competition remains stiff and, after experiencing some pricing ability earlier this year, discount stores advanced their clearance sales by three weeks.

Labor Market
There are scattered reports of a strengthening labor market, with an increase in the number of firms hiring or considering hiring. There were also more reports of wage increases. Contacts continue to be concerned about the high cost of workers compensation, health care and insurance, but several noted that the rate of growth in these costs has slowed.

Manufacturing
Manufacturing activity continues to increase. Demand was seasonally strong for clay, cement, brick, tile and glass, despite heavy rains in June slowing construction-related activity. Producers reported an increase in demand for lumber, paper, apparel, food products, and primary metals. Demand for fabricated metals is up, partly because of a pick up in demand from the commercial construction industry. Contacts expect the industry to increase hiring in the future but say they are becoming less labor intensive and more capital intensive with the addition/refurbishing to more modern/efficient equipment.

High-tech manufacturers reported mixed results. Some contacts said sales were slower in the second half of June and others reported some recent pickup due to low inventory levels. One respondent noted that sales contracts are being written for much shorter periods than they were three or four years ago and that this likely reflects the continued uncertainty about the outlook. Telecommunication manufacturers report slight gains in hiring and wages, but contacts remain cautious.

Gasoline demand dipped slightly in recent weeks, falling back to the levels of a year ago. Refineries along the Gulf Coast operated at capacity utilization rates of 97-98 percent through June, according to producers, who said that gasoline inventories are still near the bottom of the five-year average. Refined product imports were at high levels, but did little to help gasoline inventories, especially for reformulated gasoline. Chemical producers report strong demand.

Services
Service sector activity strengthened. Temporary staffing firms report a pickup in demand--primarily from employers adding to their payrolls in the light industrial, manufacturing, customer services and leisure and hospitality sectors. Demand for legal services is up slightly. Firms say they have increased hiring of lawyers and paralegals both as a reaction to and anticipation of higher demand.

Summer airline traffic has been solid, but airlines report that increased industry capacity and higher fuel costs have impaired profits. Trucking activity remains strong, and firms report a shortage of qualified truckers. Demand for rail shipments also continues to be very strong. Some manufactures expressed concern that railroad congestion was making it difficult to get raw materials from vendors and finished products out to the market.

For the first time in several years, telecommunications service firms say demand is picking up from both residential and business customers. The industry remains competitive, and prices continue to fall. There are also reports of some limited hiring.

Retail Sales
Retailers report some softening of sales growth over the past few weeks, leading most contacts to be slightly more cautious about the outlook for sales over the next few months. Sales are stronger at high end stores than at department stores, according to contacts. Sales of women's apparel were notably stronger. Automobile sales in the District remain weak.

Construction and Real Estate
Demand for residential real estate remains strong, and existing home sales in many markets are on pace to beat last year's record. An increase in the supply of homes available for sale has restrained selling prices according to contacts. Homebuilders continued to report cost increases. Apartment demand improved in the second quarter but not at the pace that most contacts had expected. Construction of new units has not eased, and rents remain on a downward trend.

Demand for industrial space rose steadily over the past six weeks according to contacts. Office demand picked up among larger tenants recently, according to contacts, and concessions continued to decline. Sill, rents remain depressed.

Financial Services
Deposit growth is unchanged or down slightly. Contacts say customers are moving money into financial markets even though deposit rates are up slightly. There has been no change in the rate of loan growth. Commercial and industrial lending has increased, but competition remains stiff. Consumer lending is growing modestly. Mortgage activity was reported as unchanged.

Energy
Domestic and international drilling activity is quite strong. The U.S. rig count strengthened by 40 rigs in recent weeks, finally moving above 1200 working rigs, but drilling in Texas has remained flat at about 495 working rigs. The rig count in the Gulf of Mexico remains stuck at around 90 rigs, well below the 165 rigs at the last peak in activity in 2001 and the 110 rigs working at the last drilling trough. Many parts of the oil field service industry report excess capacity.

Producers say balance sheets are quite strong, but there is no where to invest all the money because domestic drilling is constrained by a lack prospects and international drilling is limited because oil prospects are concentrated in high risk, politically volatile countries. Most producers are using cash flow to repurchase their own stock.

Agriculture
Crop conditions have been mostly favorable. Producers say that cotton plantings and conditions are improved over a year ago. Demand for cattle remains solid.

Return to top

Twelfth District--San Francisco

Summary

Reports from contacts indicate that the District economy continued to expand at a solid pace from early June through mid-July, although growth appeared to have slowed slightly compared with the previous survey period. Compensation and final prices rose modestly in general; however, there were scattered reports of increased wage pressures for selected types of workers. Consumer demand for retail items moderated compared to the previous survey period, while demand for most services remained strong. Manufacturing output continued to expand, but the pace slowed compared with earlier this year. Sales were brisk for most agricultural products. Demand for residential real estate remained robust, and demand for commercial real estate was stable or up a bit. District banks reported solid demand for all loan categories and good credit quality.

Prices and Wages

District contacts reported modest price inflation during the survey period. Fuel and energy prices fell back somewhat, but rising prices for steel, cement, and some raw materials boosted production costs in some industries. Some contacts noted increased pricing power relative to earlier in the year, but in general vigorous competition still limited firms' ability to pass cost increases on to final prices.

Wage and salary pressures were modest overall. However, shortages of qualified job applicants and increased outside competition for existing employees generated notable wage and salary increases for skilled occupations in a number of industries, including construction, manufacturing, financial services, and technology services. Contacts noted that where wages have been rising, productivity gains generally have been adequate to hold constant or reduce labor costs per unit of output. There were a few exceptions, notably for some firms in the banking, health-care, and construction industries, where productivity growth did not keep pace with wage gains and rising labor costs were absorbed into profit margins or passed on to final prices. Some contacts noted recent or anticipated slowing in the pace of productivity gains in their industries. Respondents in all sectors reported that rising health insurance costs made a significant contribution to increases in overall compensation costs.

Retail Trade and Services

Contacts reported slight moderation in retail sales compared with the previous survey period. Automobile sales fell in June. The decline was centered on domestic makes, for which inventories reached very high levels. However, overall sales recovered somewhat in early July. In retail, a contact from a major department store chain noted that "sales have softened" compared with earlier in the year, although other retail contacts reported further sales increases.

Service providers saw strong demand throughout the District. Robust sales were reported for providers of advertising, communications, entertainment, and health-care services. Shipping traffic through District ports expanded, spurred by vigorous international trade flows. District travel and tourism activity strengthened further. Hawaii's tourist traffic has been growing at a double-digit pace compared with a year earlier, and hotel occupancy rates there recently regained their highs from the year 2000. Hotel occupancy rates also rose in San Francisco.

Manufacturing

District manufacturers reported generally solid demand for their products, although growth slowed in some sectors. Semiconductor sales grew at a slower pace and manufacturers' inventories rose slightly, but capacity utilization in the industry remained high. Demand was strong for some categories of communications equipment, including items used for high-speed Internet access and office computer networks. Metal fabricators, transportation equipment makers, and manufacturers of wood products operated at high levels, although new orders slowed slightly. Demand remained strong for apparel and textile products.

Agriculture and Resource-related Industries

Contacts reported brisk sales for District agricultural products. Demand for beef cattle and other livestock has been especially strong, reportedly pushing prices to unusually high levels. Berry crop yields were very high in the Pacific Northwest, but solid demand kept prices firm. Similar strength was evident for the California nut and grape crops, although sales reportedly were weak for some other fruit crops in that state. Demand for dairy products remained strong, and one contact noted that milk prices were at five-year highs.

Real Estate and Construction

Demand for residential real estate remained vigorous, and reports indicated modest further improvement on the nonresidential side. Sales of new and existing homes were rapid in most areas, especially in Southern California and Hawaii, where demand growth noticeably outstripped supply growth and rapid price appreciation continued. However, reports indicated that the pace of home sales and construction starts has leveled off in some parts of the District, including Utah and the Seattle area. Demand for residential rental properties weakened slightly in the Los Angeles area. On the commercial side, demand for office space improved a bit further in some areas, although prices and rental rates remained largely flat. In the population centers east of Los Angeles, demand for commercial real estate was very strong, with prices on industrial space reportedly up 40 percent from a year earlier.

Financial Institutions

District banking contacts reported strong loan demand and good credit quality on existing loans. Business loan demand increased further in most areas, although contacts in a few areas noted a recent drop due to reduced business optimism about the likely payoff to capital improvements. Lending for new residential mortgages fell somewhat but remains quite high. Several contacts noted significant increases in venture capital funding and planned initial public offerings.

Return to top

Last update: July 28, 2004