

CONFIDENTIAL (FR)

CURRENT ECONOMIC COMMENT BY DISTRICT

Prepared for the
Federal Open Market Committee
by the Staff

August 14, 1974

TABLE OF CONTENTS

SUMMARY	i
First District -- Boston	1
Second District -- New York	4
Third District -- Philadelphia	7
Fourth District -- Cleveland	10
Fifth District -- Richmond	13
Sixth District -- Atlanta	17
Seventh District -- Chicago	20
Eighth District -- St. Louis	23
Ninth District -- Minneapolis	25
Tenth District -- Kansas City	28
Eleventh District -- Dallas	31
Twelfth District -- San Francisco	34

SUMMARY*

District reports present a mixed picture, with elements of weakness generally overshadowing those of strength. There are scattered indications that shortages and bottlenecks are breaking up in some sectors, although shortages of certain industrial goods remain critical. Many firms have been critically reexamining their capital spending plans, and some have scaled back such plans, not only among public utilities but in some other sectors as well. Similarly, more cautious inventory policies seem to have been adopted by some firms. Consumer spending on appliances continues sluggish, but demand for the remaining 1974 model automobiles appears to have strengthened. Residential construction continues to languish. Inflation remains a serious concern, especially in light of recent estimates of a significant drop in the expected harvest of certain key agricultural commodities.

Regional differences in the state of overall economic activity were reflected in the District reports. Economic conditions were characterized as mixed by Cleveland and Atlanta and as showing "marked contrasts" by Chicago. Activity was described as sluggish and slowing by Philadelphia and Richmond, respectively, while Minneapolis reported that prospects were not as promising as earlier in the year. On the other hand, manufacturing activity was reported strong by St. Louis and San Francisco, and Dallas reported that factory orders are generally running ahead of year-ago levels.

Capital spending plans are being subjected to increasingly critical scrutiny, and some cut-backs were reported even outside of the public utility sector, where deferrals and cancellations of capital investment projects are widespread. Among others, Philadelphia and Richmond report reluctance on the

*Prepared by the Federal Reserve Bank of New York.

part of manufacturers to increase such outlays, with some manufacturers planning some cut-backs. Cleveland reports some softening in new orders for machine tools. On the other hand, Chicago and St. Louis report continued strong demand in the capital goods industry, and San Francisco reports that business investments are heavy.

As in the case of capital spending plans, inventory policies have been under reexamination. The emergence of more cautious inventory policies on the part of businesses was reported by a number of banks, including New York, Philadelphia, Cleveland and Richmond. Some easing of shortages was reported by Chicago and Cleveland, although Cleveland also noted continued intense demand for steel and desperate attempts on the part of industrial firms and utilities to stockpile coal. Shortages were reported to be continuing to hamper output in the San Francisco District.

Several banks reported that residential construction remains in the doldrums. Other types of consumer outlays appear sluggish for the most part, although Richmond noted a rebound in retail sales and San Francisco characterized such sales as "good". A number of banks reported weakness in sales of big-ticket items such as furniture and appliances. On the other hand, several banks, including St. Louis and San Francisco, observed a strengthening of automobile sales.

Despite the apparent slowing down of business activity and the reported easing of supply conditions in a number of industries, concern over inflation continued to be expressed by many respondents. These fears have been heightened by recent reports of prospects of significantly lower harvest of certain key agricultural products, notably corn and soybeans, than expected earlier in the year--a situation described in detail by Minneapolis and Kansas City and referred to by several other banks. Agricultural conditions

were reported to be more favorable in several Districts, including Richmond, Atlanta, and San Francisco.

The demand for bank credit generally continued strong. The adoption of tighter bank lending policies, which in some instances may have helped contain the expansion, was mentioned by several banks, including Dallas, Philadelphia, Minneapolis, and New York. Thrift institutions were widely reported to still be losing deposits, and to have been especially adversely affected by the recent Treasury sale of 9 percent notes in denominations as low as \$1,000.

FIRST DISTRICT--BOSTON

Our directors' reports vary. Some indicate that business continues to be pretty good, although below peak levels, while others note concern about where the economy is heading. Unemployment rates in New England are climbing, with the seasonally adjusted rate in June reaching 7 percent in New England as a whole and 8 percent in Massachusetts. Energy-related developments continue to affect business conditions, prices, and the outlook.

Tourism, affected by fears of gasoline shortages, picked up in July after a very slow June. The number of tourists appears to be about the same as last year, but they are not buying as much. Dollar sales seem to equal year-ago levels but, due to higher prices, real sales are down 10 percent, according to industry spokesmen.

A director from a large conglomerate reports that carbon black sales continue doing pretty well, but that much of their profits are inventory profits. There is expected weakness in the carbon black markets because of sluggish auto sales. Despite a slowdown in sales, this manufacturer plans to raise prices again to reflect rising costs. Carbon black is made from petroleum feedstocks whose prices have tripled since last fall.

Natural gas is expected to be in very short supply again this year. Companies with southern pipelines supplying the Northeast have informed New York and New Jersey utilities that they will not be able to meet their contracts. According to our director who is involved in bringing liquid natural gas (LNG) from Algeria, deliveries are still being held up by Federal regulatory agencies and by plant problems in Algeria. This LNG is under contract to New York and Boston utilities.

A booming area is specialty metals and alloys. Demand has increased in part because of conversion needs caused by the energy shortage. In addition,

our directors report continued stockpiling of strategic metals and minerals like copper and zinc.

High interest rates have dampened loan demand and deposit growth. Our directors from small and moderate-size banks from Massachusetts and New Hampshire report demand deposits lower than a year ago. They suspect that there has been some loss to new accounts and to Treasury bills. Business loans are also lower, due to higher interest rates. Even the home improvement loan business is being affected.

A business director reports that tight money is having a general impact and that there is a widespread feeling that there is a big tail-off in expenditures on all kinds of things. He notes that intermediate-size firms are being locked out of credit markets. As a result, they are deferring expansion plans. He feels that uncertainty about when interest rates will come down is making firms delay borrowing because they are afraid of being locked into high rates if they are about to drop soon.

Professors Eckstein and Samuelson and Dr. Shapiro were reached for comment this month. All agree that the economic outlook has deteriorated significantly recently. On the basis of the data revisions, Shapiro forecasts an inventory recession. The inventory figures along with foreign borrowing explain the strength in business loan demand in the first quarter. Despite his forecast that the recession will bring unemployment to between 6 and 6.7 percent by mid-1975, Shapiro recommends a money growth target of 4 to 5 percent, "although the Fed may be in some trouble if it pursues 4 percent too rigorously".

Eckstein's forecast is for 2.5 percent real growth over the next year, but he grants that this is at the optimistic end of the range. With tighter money, short-term interest rates would stay high, the housing recovery

of 1975 would be totally aborted, consumer durables would weaken in late 1975 and 1976, and capital spending would be hurt in 1976. The benefits in terms of inflation would come after 1976. To preclude this outcome, Eckstein argues that the Federal funds rate should be brought down to 10 percent by the year-end. In the meantime, the Fed must monitor the disintermediation situation carefully and be prepared to let rates fall more rapidly. If the Fed continues its tough policy, Eckstein feels that it must become more sympathetic to the selective credit controls approach.

The Federal Reserve is creating a shortage of liquidity, according to Samuelson, and it needs to get ready to bail out the thrift institutions. In light of the universally bleak outlook, he urges those who favor continued monetary restraint to do a careful cost-benefit analysis of the scenarios under different regimes of money growth. Attempts to analyze the output costs and inflation benefits of stagnant growth, such as those by Tobin, Gordon, and Hall, all indicate very little inflation abatement from even very lengthy periods of stagnation. Advocates of "old time religion" must be aware of what they are paying and how much they are buying. "They're buying little because there is nothing in the store!" The appropriate, near-term goal for monetary policy, according to Samuelson, is to burn a low two-digit inflation down to a high one-digit inflation, while praying for good weather and weakness in the Arabian cartel. Under these circumstances, "tight money begins at less than 8 percent".

SECOND DISTRICT--NEW YORK

In the views of the Second District directors and other business leaders who were contacted recently, while many firms are critically reexamining their capital spending plans, few are cutting back such plans, with the notable exception of utilities. The majority of the respondents similarly felt that no major attempts to reduce inventories had got underway as yet. At the same time, however, the comments of several respondents indicated that somewhat more cautious inventory policies might be emerging. Some observers expected the 1974 model automobiles to sell out quickly but expressed apprehensions about the outlook for demand for the 1975 models. Views were mixed regarding the prospective strength of business loan demand, but there was general agreement that bank lending policies had become tighter.

Regarding business plant and equipment outlays, the Buffalo branch directors felt that despite currently tight conditions in the financial market, most corporations were going forward with their capital spending plans, prompted by shortages in productive capacity and by the need to improve productivity. Among other respondents, a senior official of a New York City securities firm reported that except for utilities and some other scattered instances, he could not discern cutbacks in corporations' longer term capital investment plans, a view that was expressed by several other respondents. And while a New Jersey banker felt that a continued high level of interest rates might eventually lead to some retrenchment in business capital outlays, he had seen little of that so far in his area.

Similarly, most of the respondents had observed no major efforts as yet to reduce inventories. The official of the securities firm stated that notwithstanding the high level of interest rates, the current rate of inflation still made it profitable to accumulate inventories. Several respondents at-

tributed the high level of inventories to the rapid inflation and the frequently long delivery lead-times which encouraged businessmen to increase stocks on hand, both as a hedge against further price increases and as protection against shortages. On the other hand, a senior official of a nationwide department store chain attributed the recent buildup in that firm's stocks to a shortening of some suppliers' delivery lead-times. A senior economist at a large New York City bank reported that whereas until recently the bank's corporate clients had been using credit to "invest" in inventories, the rise in interest rates combined with the fact that the prices of many commodities were no longer rising as rapidly as previously had made the carrying of excessive inventories "too costly", and that this had been reflected in some slowdown in the rate of accumulation. Similarly, a senior official of a large upstate New York firm stated that in view of the rise in interest rates and the decline in price of some commodities, carrying excess inventories had become "risky".

Regarding consumer spending, the department store chain official reported that his firm's sales had been better than expected during the first half of the year. He expected a good second half, although the rate of increase would probably be slower. An upstate retailer expected an increase in dollar sales over last year's level but somewhat lower physical volume. Another director saw the retail sales picture as being fairly flat. The New Jersey banker expected that retail sales--particularly of automobiles and other big-ticket items--would be adversely affected by inflation. In this connection, an upstate banker reported a sharp reduction at his bank in consumer loans for appliance purchases, although demand for home improvement loans remains heavy. Several respondents felt the short-run outlook for automobile sales was better today than a few months ago and expected a rather quick sell-out of remaining

1974 models. They did note, however, that the long-term outlook for auto sales was clouded by concern over public acceptance of 1975 models equipped with largely unproven catalytic converters and by the uncertainties regarding the availability of the lead-free gasoline required to fuel models equipped with such anti-pollution devices.

With respect to the demand for business loans, the New Jersey banker, the securities concern official, and several other respondents saw no let-up at this time. On the other hand, several upstate bankers felt that such demand had probably peaked, at least for the balance of the year, in part, as a result of sluggish economic conditions. Similarly, a senior economist at a major New York City bank reported that business loan demand at his bank, while still high, was tapering off.

The respondents in general reported a tightening in banks' lending policies. Among others, the New Jersey banker stated that his bank had adopted a "hard nosed" lending policy. It was making no new commitments and extending only modest amounts to regular customers. Similarly, the New York bank economist reported that his firm had not taken on new corporate customers for some time and was discouraging its regular customers from borrowing for non-productive purposes such as accumulation of excess inventories and the acquisition of other firms.

THIRD DISTRICT--PHILADELPHIA

Economic activity in the Third District continues to advance at a sluggish pace. Manufacturing activity is posting little change, and manufacturers expect this trend to hold steady at least until February. Employment levels, too, remain stable. Inventory stocks are being held constant, with manufacturers reporting few plans to increase their existing levels in the next six months. Earlier optimistic plans for boosting spending on capital goods have been revised down again this month.

This slow-paced business activity is also showing up in some declines in retail sales. Both retailers' and manufacturers' expectations of higher prices in the months ahead could add fuel to the slowdown in business activity in the regional economy. Area banks experienced some disintermediation in early August, but no liquidity problems were reported. Loan levels, as well as deposit levels, are reported lower at most District banks.

Manufacturers in the Third District, responding to this month's business outlook survey, report that business activity in the Third District is continuing to move along at a slow pace. Seventy percent of the respondents report no change in new orders, shipments, and unfilled orders in August. The executives' six-month outlook reflects a continuation of this trend. Twelve percent more of the area manufacturers expect an increase in these key indicators than expect a decrease, with the remaining third anticipating no change at all by February.

Presently, the slowing in manufacturing activity is having very slight effects on employment in the District. Over 80 percent of the respondents report no change in their number of employees and the length of their average workweek.

The employment picture isn't expected to alter much in the next six months. Seven out of ten executives expect to maintain stable employment levels through February and to keep the length of the average workweek the same. Yet as the size of the work force continues to grow, we are likely to see some increase in the level of manufacturing unemployment in the region in the months ahead.

Manufacturers are showing some reluctance to increase their inventory stocks this month. Just as many decreased their stocks as increased them, and, respondents report that they expect to maintain this posture at least until February. For the second month, manufacturers indicate reluctance to boost spending plans on plant and equipment. Fifty percent of the respondents report no change in capital expenditure plans, with the remaining 50 percent split evenly between those who expect to step up their spending on plant and equipment and those who expect to cut back. Area retailers report a slight slowing in sales in July despite widespread price reductions of season-end merchandise; however, those executives surveyed report optimism for August. But uncertainty still remains regarding consumer spending later in the fall and winter. Coats and men's suits will post the largest gains on price, but executives report higher price tags on most new merchandise. The outlook for prices in manufacturing also remains pessimistic. Seventy percent of the executives polled expect to pay higher prices for raw materials in February and to receive higher prices for finished goods. Not one manufacturer reported any expectations of price declines in the manufacturing sector of the regional economy.

Loan levels at regional banks dropped off in July and early August, primarily because of restrictive loan policies. Area banks are not soliciting new business, and some report cancellations of existing credit lines. Most banks surveyed report few difficulties in the money market although, in general, area banks must pay a premium for funds over that which New York

banks pay. Disintermediation was a large problem last week for most commercial banks as well as area savings banks. Record outflows resulting from the latest Treasury issue, coupled with a drop in deposit levels, produced a substantial reduction in available funds. However, no severe liquidity problems were reported.

FOURTH DISTRICT--CLEVELAND

Reports from our directors and other business executives indicate a mixed picture of strengths and weaknesses. Inflation remains the main concern of many of our directors, and their reports indicated that prices will remain under upward pressure over the period ahead. There is little firm evidence as yet that the pace of economic activity in the District is slowing down significantly, although there are some limited indications of softening in capital spending plans among utilities. Supply conditions generally have eased, and this development coupled with higher interest cost is leading to a reappraisal of inventory situations. Demand for steel products remains intense. Industrial firms and utilities are trying desperately to stockpile coal. Conditions in the District's savings and loan industry continue to tighten.

Early returns from our monthly survey of manufacturers showed some weakening in new orders during July, following three consecutive months of recovery. Firms reported further moderate gains in shipments and inventories. Backlogs are still rising, and price increases remain pervasive.

One of our directors associated with a major retail firm emphasized that the physical volume of sales remains basically level. In addition, he was particularly pessimistic about the price outlook for the near term, noting that most of the foods in the retail pipeline carried considerably higher prices than goods currently on the shelf. Several other directors also gave pessimistic reports about the likely price structure for their products in the months ahead. A director, associated with a consumer products firm, noted specifically that the firm's price increases reflect only higher costs for raw materials and that the firm was absorbing other cost increases.

The supply situation for raw materials generally has eased in the past few months, although there are still numerous reports of shortages.

Buying lead times for production materials have improved slightly since the end of price controls. Two of our directors--one with a large industrial firm and the other with a consumer goods producer--noted that increased availability of basic materials and high interest costs are causing a significant reassessment of inventory positions. Another director mentioned that lift trucks are being delivered faster and that paper companies in Ohio are now giving quick delivery. A chemical firm reported that certain petrochemical products remain in short supply, while a chemical-rubber firm stated that petroleum derivatives are now in ample supply. The same company reported its tire inventories are on the high side, but that it does not plan to cut production. Management is relying on a pickup in new car sales, especially fleet purchases, to reduce its inventories. An executive in the machinery industry remarked that some of their inventories are growing faster than desired because shortages of component parts have held up shipments.

Industrial firms and electric utilities in the District, which depend on coal more heavily than the national average, are increasingly concerned over the possibility of a miners' strike in November. Many firms are attempting to stockpile coal. The steel industry has only a two to three-week inventory of coal. The steel industry would have to start cutting back production immediately to protect its facilities in the event of a strike.

Steel demand remains strong as customers continue to stockpile steel products. An economist with a major steel firm said that the market situation could turn around fast if customers stop hoarding. Railroad wheels, rails, and plates are in particularly short supply. Companies are paying a premium of \$100 a ton over domestic prices for imported steel.

Capital spending plans appear to be holding up, although there are some signs of softening. Purchasing agents in the Cleveland area continue

to maintain long lead times for capital equipment. Economists with petrochemical, machinery, and steel companies say their spending plans for the remainder of this year have not been scaled down, despite the high cost of borrowing and a squeeze on cash flow in some firms. Steel mills are increasing their capacity for making hot steel and semifinished products, where the production bottlenecks are concentrated. Nonresidential building awards in the District remain strong, but there are indications of a softening in new orders for machine tools and some other types of industrial machinery. A director in the machine tool business believes his orders backlog is about to level off and then remain on a high plateau for about a year. Other directors expressed the opinion that industrial firms must be reexamining their capital spending plans. Several utilities in the District recently announced cutbacks in planned capital spending programs.

The District's savings and loan associations lost deposits throughout the month of July and during the first week of August. An official with a Federal Home Loan Bank described the situation as poor, but not exactly a disaster. Recent deposit outflows were greater in Cleveland and Cincinnati, and were related to the Treasury note offerings. Savings and loan associations are still making mortgage loans; all are at rates of 9 percent or higher--some are charging 10 percent.

FIFTH DISTRICT - RICHMOND

The latest survey of Fifth District business conditions shows a continuation of the slowing trend noted over the past few months. The diffusion of manufacturing responses indicates a further weakening in new orders, and over one third of the survey respondents now report declines in backlogs. Some apparently involuntary inventory accumulation is continuing, and more than 40 percent of the manufacturing respondents report that inventories are excessive. Retail sales rebounded after a month of little or no change, but sales of big-ticket items remain slow. Expectations patterns among both manufacturers and retailers appear to have taken on a more pessimistic tone in recent weeks. Business loan demand remains strong, but District banks report an increasing selectivity in securing new loan applications. In the agricultural sector, recent rains have resulted in crop improvements, and current crop conditions generally range from fair to good.

As in several previous months, survey responses of manufacturers are weighted toward a reduced volume of new orders, a decline in backlogs, and further inventory accumulation. Growing dissatisfaction with high inventory levels may portend slowing production, if the orders picture does not improve significantly. For the seventh month this year, the diffusion of responses indicates some reduction in weekly hours of work. The continued slack in activity is beginning to register on current expectations patterns of District manufacturers, as increasing numbers of respondents expect business conditions to worsen over the next six months both nationally and in their respective market areas. While one third of those surveyed continue to expect their own production to increase, over one fourth now expect declines. The latter figure represents a significant increase over recent reporting periods.

The outlook for capital investment is somewhat uncertain. While almost one fourth of the manufacturing concerns surveyed consider current plant and equipment capacity inadequate, only 13 percent feel current expansion plans should be enlarged. Four respondents think such plans should be cutback, the first to express such sentiments this year. Aside from our regular survey, two more major utility firms have recently announced cutbacks or delays in expansion plans. This follows two similar actions reported last month. One utility firm announced reductions in planned investment for the next two years and had delayed for one to two years the opening of three facilities. Another major electric utility has deferred \$100 million in construction this year. In other industries, however, there were announcements of plans to build several new plants, which will involve substantial new investments over the next three years.

Of the retailers responding to our survey, two thirds reported that sales were up during the month, but an equal number indicated that sales of big-ticket items relative to total sales continued to decline. A majority of respondents indicate no change in inventories and general satisfaction with current inventory levels as well as with the number and size of outlets. Over 80 percent of the respondents in this category anticipate little or no change in the general level of business activity over the next six months.

The uneasy labor situation is currently having some impact on Fifth District business activity. By early August, strikes had closed several plants and idled thousands of workers across the District. Labor disputes are affecting such industries as primary metals, textiles, paper, chemicals, and sheet metal work. One District firm in the primary metals

category, closed since July 15, indicates that inventories are at extremely low levels, but it does not expect a rapid pickup after the strike is settled. The major uncertainty in the labor relations area is the situation in the coal industry. As of the present it appears that a major coal strike can be avoided only at the expense of outsized wage and benefit increases with corresponding increases in coal prices. Some West Virginia observers believe that, given the strong demand for coal and the large potential for profits, operators are likely to acquiesce in union demands and avoid a prolonged strike.

The monthly survey of commercial banks indicates that business loan demand continues quite strong, while demand for consumer loans remains flat. Commercial banks are adopting a position of "conscious restraint" with regard to further loan expansion. The source of demand for business loans is reported to be increasingly regional in nature, with national firms playing a diminished role. Local utilities are contributing to this condition by seeking longer term loans with fixed interest costs. Savings flows at both banks and savings and loan associations remain flat, with concern over the recent Treasury issues as a potential drain on savings deposits centered in those cities having a Federal Reserve Bank or Branch. Responding savings and loan associations in those cities report significant deposit losses.

Rains have fallen over most of the District during the past two weeks, alleviating widespread drought conditions. Crops are improving as a result, with current crop conditions generally ranging from fair to good. With the sharp upward revisions in 1973 farm income figures, January-June

cash receipts from farm marketings show only a 10 percent increase over a year earlier. Low prices and poor quality offerings have marked this season's early flue-cured tobacco sales. Prices improved significantly last week, however, as growers brought better quality upstalk tobacco to market.

SIXTH DISTRICT--ATLANTA

The District's economy shows a mixed bag of pluses and minuses, according to the most recent reading. The situation for cattle producers is now considered more favorable than previous reports indicated. Bank lending remains strong in Tennessee despite the state's 10 percent usury ceiling. Residential building remains very weak. North Georgia's carpet industry is beginning to feel the effects of the decline in construction. Activity at four of the District's major ports is up over year-ago levels. Tourism continues to soar, after being depressed by gasoline shortages earlier in the year. Several large contracts have recently been awarded to District industries. Spending on pollution control in the region remains significant.

Reports from several District bankers indicate that conditions have brightened recently for the region's livestock producers. Rains have revived pastures somewhat and, for the time being, have reduced the need for purchasing high-cost supplemental feeds. Some improvement in cattle prices has brightened prospects of cattlemen, eventually succeeding in disposing of their unusually large calf inventories at favorable prices. Cattle loans continue to be renewed and extended to prevent growers from having to sell on depressed markets. Bankers are now more optimistic that these loans will be repaid from cattle receipts.

Crop reports are much improved by the recent substantial rainfall. Most District farmers stand to benefit from good yields and the high prices caused by drought damage to crops in other parts of the country.

Tennessee's 10 percent usury ceiling has apparently had little impact on reducing bank lending. Large weekly reporting banks report increases in business and consumer instalment loans as well as lending to nonbank financial

institutions. Real estate lending shows the only weakness. Apparently, Tennessee banks are able to skirt the usury ceilings in some instances by upping compensating balance requirements. Some large Tennessee bank holding companies did have a decline in second-quarter earnings, however, which may be partially related to the state's usury law. Many Tennessee banks, believing interest rates have peaked, are shortening the maturity structure of their liabilities by shifting from CDs to the Federal funds market.

Residential building remains very weak in the District. Latest information indicates increased outflows from savings and loan institutions. One bright spot is the Atlanta apartment market. Atlanta was overbuilt with apartments a year ago, but now there is a shortage partly because of the high price of single-family dwellings. This may also provide good news for the condominium market, which had come to a near standstill.

The decline in residential construction is beginning to affect north Georgia's carpet industry. According to one area banker, not only is carpet demand dropping off, but many materials are still difficult to obtain. The net result has been reductions in production and employment. This banker indicated that the demand for inventory loans by carpet manufacturers is up, with increased prices of raw materials given as the reason. There has been little, if any, demand for bank funds for capital expansion by the carpet industry.

Ports in New Orleans, Mobile, Jacksonville, and Palm Beach reported increases in tonnage shipped recently. Mobile had the third highest month in the port's history. The first Russian Merchant ship to call at the Savannah, Georgia, port has docked there to load wood pulp and cellulose for export to Europe and Russia.

Tourism has remained strong. Alabama's second largest industry is tourism, and it may receive a shot in the arm as eight welcome stations are to

be built along Alabama's borders to "sell" the state as a vacation spot. Florida is having a good summer as earlier reported. Disney World and Cypress Gardens are doing well. Two major tourist attractions in the Atlanta area have reported increases in visitors from a year ago. Atlanta's convention business is booming, with activity coming in from all over the world. At the present time, there are around 16,000 hotel and motel rooms and, in two years, the number will be increased to around 26,000.

Representatives from an Atlanta area investment house indicated that they have received feelers from Arabs about possible investment in District income-producing property; they are currently negotiating several investments in the Atlanta area.

Several new contracts have been awarded to District industries. Textron's Bell Aerospace Division of Michoud, Louisiana, has been awarded a \$36 million contract to conduct an advanced development program for the Navy's proposed 2,000 ton, high-speed surface effect ship. Rohn Industries of Winder, Georgia, received a \$30 million contract from the United States Department of Transportation to build seven high-speed turbo trains for Amtrak. Lockheed, Georgia, received a \$26 million contract for five aircraft for the Canadian Armed Forces.

Spending on environmental protection and pollution control continues to be a sizable portion of District investment spending. Miami and Tampa, Florida, received two of the largest grants made by the Environmental Protection Agency to help clean up water pollution. Miami received \$41 million; Tampa received \$34 million. The Tennessee Valley Authority will invest a record \$180 million this year on pollution-control projects at ten power plants.

SEVENTH DISTRICT--CHICAGO

The economic situation in the Seventh District continues to show marked contrasts. Most capital goods producers report further increases in backlogs. Problems of shortages have eased somewhat, partly as a result of rationing by higher prices. Consumer demand for some appliances and furniture has softened. Residential construction is at a very low ebb, with no prospects of a revival this year. Strikes are hampering output in a variety of activities. Price and wage inflation appears to be accelerating. The most significant adverse development of the past month has been the substantial deterioration in the outlook for the corn and soybean crops.

Electric utilities and auto companies are slowing their capital expenditure programs, mainly because demand for their products has fallen below expectations. Such decisions do not seem to have moderated the extremely strong demand for virtually all types of machinery and equipment. Some machine-tool producers are not taking additional orders for lead-time items because of pricing uncertainties. Perhaps demand is most intense for railroad equipment and mining machinery. Some freight car producers are booked through 1975. A major producer of mining machinery has embarked on a three-year program designed to more than double its capacity.

Reduced activity in some sectors and the rapid rise in prices since decontrol have eased supplies of some items. Fuel supplies are ample at current prices, and "absolutely no" shortages of any major petroleum product are expected to develop through the remainder of 1974. Paper also is more available at prices 20 to 25 percent higher. Electrical components for consumer goods may be in excess supply. On the other hand, there has been no letup in demand for steel or aluminum and many other materials. Complaints about slow deliveries of axles, transmissions, brakes, bearings, diesel engines,

castings, and forgings continue. Because of **failures** of suppliers to meet delivery schedules, some companies are pushing programs to become more self sufficient.

We have not found evidence of a general buildup of excessive inventories (although there are many imbalances), but a significant decline in total business activity would soon cause such a development. For the present, most firms appear to be increasing inventories according to plan or the degree of availability of the items they purchase. High interest rates and limited availability of credit have caused some firms, especially smaller ones, to limit inventory investments and capital outlays.

Strikes have been significant in holding down construction activity and output of motor vehicles and various types of equipment. By far, the most serious strikes in the District was settled on July 22 when cement truck drivers in the Chicago area resumed work after a nine-week strike that had halted a large part of all construction activity in seven countries. First-year wage increases of 10 to 12 percent or more are common, with or without strikes. The main factor delaying conclusions of some labor negotiations has been a failure to agree on cost-of-living adjustments clauses for future years.

The residential construction situation is miserable, In June, building permits for new dwelling units were off 70 percent from last year and the six months' total was off over 50 percent. Permits for homes in the Chicago area were lowest for any June since World War II, and permits for apartments were the lowest since 1956. (Permits in the Milwaukee area were off over 40 percent for six months.) The Illinois usury rate was belatedly raised from 8 percent to 9.5 percent in July, but this is not expected to help much because of the impact of high money market rates on the availability of mortgages.

Proposed new developments of both residential and commercial projects are said to have "dried up". Financial stringencies reflect the problems of real estate subsidiaries of insurance companies, banks, and manufacturers in obtaining funds, as well as the plight of the savings and loan associations. Large Chicago savings and loan associations reported a net outflow of savings in July for the fourth straight month and a record outflow for any month. Demand for housing continues strong, with vacancy rates reduced, rents rising sharply and prices of existing homes holding steady or rising further.

Heavy rains earlier in the year, followed by drought, have drastically altered the prospects for the corn and soybean crops in the Corn Belt. The corn crop is almost certain to be substantially lower than in 1973, instead of the large increase anticipated early in the year. The soybean crop will benefit from high prices, but incomes of farmers who lose a major share of their crops will be reduced sharply. Reduced availability of feed grains and forage may cause farmers to liquidate inventories of meat animals, leading to lower meat prices temporarily but followed by higher prices in 1975.

EIGHTH DISTRICT - ST. LOUIS

The pace of economic activity in the Eighth Federal Reserve District has continued up in recent weeks. Retail sales at major department stores have slowed, but most of the decline has been offset by rising automobile sales. Manufacturing continues at a high level, and employment remains about unchanged. Loan demand remains at a relatively high plateau, following a sharp increase in the first half of the year. Agricultural conditions have improved in recent weeks as a result of rainfall over most of the District. Corn yields will be below average for recent years because of lack of moisture in July.

Consumer spending at major department stores has declined in recent weeks. Big-ticket items, especially those related to housing, are being hit the hardest, although clothing and shoe sales were also reported to be sluggish. Most of the decline has been offset, however, by a sharp recovery in automobile sales. One major St. Louis dealer reported that automobile sales were at record levels in July and that he cannot obtain a sufficient number of large cars to meet demand at current prices.

In general, manufacturing activity has continued at the high levels of recent months, but most firms report some increase in inventories. The steel industry and other capital goods industries not related to construction are still continuing to expand operations. A steel industry representative reported no letup in their orders backlogs, and firms which use steel noted the long delivery time. Aluminum is reported to remain in very "tight" supply. Delivery of some other metal products, such as brass, however, was reported to be substantially improved.

In general, the firms contacted reported that employment has been steady in recent weeks. Eighth District unemployment continued at a lower rate than the national average. However, a few manufacturers with rising inventories noted that operations may have to be curtailed and employment cut back.

Business loan demand continued up but apparently at a slower rate in recent weeks than heretofore. Total business and consumer loans for the District have continued to increase somewhat. Low yielding savings-type deposits at banks and savings and loan associations have remained virtually unchanged since last spring, but time certificates have increased, especially those denominations over \$100,000.

The damage from the drought in the Eighth District is "spotty", and its impact on crop production is difficult to determine. Early corn yields have been severely damaged in some localities, but recent rains and cooler temperatures have increased prospects for soybean and late corn. Cotton and rice crops have not been significantly damaged by the dry weather.

NINTH DISTRICT - MINNEAPOLIS

The prospects for the District economy are not as promising as earlier in the year. A price-cost squeeze is still hurting the District livestock industry, and dry weather is expected to reduce crop yields markedly. District consumer spending has softened recently, and no substantial sales pickup is foreseen. Tourist business is good in the eastern part of the District, but is sluggish in the western states. Savings inflows to District financial institutions have slowed as large investors have sought higher yielding investment opportunities. District loan demand is expected to remain strong at both rural and urban banks.

District livestock producers have sustained substantial losses and are expected to do so until the price-cost situation improves. Bankers report much refinancing of feeder-cattle loans. However, District livestock producers appear to be getting the credit they need, and the Bank is not aware of any bankruptcies in this industry in the District. The pricing problem in the cattle industry is rapidly reverberating from the feedlot owner to cow-calf operators, many of whom are still holding their 1973 calves. For the cow-calf rancher, the full impact of the high grain prices will probably be felt later this fall. A Montana director indicated that there are currently no buyers for feeder cattle in his area because buyers are holding back, given current uncertainties about feed and cattle prices.

Although the situation was undoubtedly improved by recent rains, dry weather is expected to lessen District crop yields noticeably. Within the District, South Dakota is experiencing the most severe drought conditions, and a lack of moisture is also a serious problem in North Dakota and Montana. With the exception of the southwestern corner, crop yields in Minnesota, on the other hand, should be quite good.

savers have withdrawn funds from their area's financial institutions and invested these funds in higher yielding alternatives.

Respondents to our latest agricultural credit conditions survey reported that no letup is expected in the strong loan demand experienced by District agricultural banks in the second quarter. Eighteen percent of the respondents reduced or refused a loan in the second quarter, and 20 percent expect to have problems meeting loan requests in the next three months. Factors contributing to this continued strong loan demand are a reduction in the availability of merchant credit, increased prices of farm inputs, the continued need to refinance feeder-cattle loans, and the expected need to finance wheat inventories. Also, the absence of Government payments this summer has increased loan demand: previously Government funds were used to cover mid-year operating expenses and pay off bank loans. Loan demand is also very strong at urban banks, and a twin cities banker reported that his bank is allocating loan funds among customers and has a flat prohibition against commitments to other than traditional customers. This bank looks for its loan demand to continue very high in the months ahead.

TENTH DISTRICT--KANSAS CITY

In light of the recent sharp rise in farm prices at wholesale levels, inquiries were made in several Tenth District states to assess the agricultural situation. Despite recent rains and cooler temperatures in the District, damage to crops, particularly corn, has been serious although grain sorghum and soybean prospects have improved somewhat. Some District bankers have indicated that they expect spillover effects from the drought conditions to show up soon in increased loan demands by farmers. Consumer interest in the recent 9 percent Treasury note issue has prompted substantial deposit withdrawals. Several District bankers have expressed concern over the longer run impact of similar Treasury financing operations in the future.

Recent and cooler temperatures over much of the District have eased the stress on growing crops, but additional precipitation will be required before any significant benefits are realized. A grain spokesman mentioned that by no means has the drought been broken, but "now that we've had rain, there is hope it can rain again". The general consensus on crop conditions is that the corn has been badly damaged and the rains will be of little benefit. Except for irrigated corn, which accounts for nearly one half of total acreage, the Nebraska crop will be "nearly zero" this year and only a small portion is suitable for chopping into silage because of its low nutritive value and the buildup of nitrates in the stalk. The Kansas and Missouri corn prospects are not so grave as Nebraska's, but again the recent rains came too late to be of much help. However, with additional rainfall, the yield prospects for soybeans and grain sorghum could be substantially improved as these crops are now in the critical development stage.

In light of recent developments, corn production in the nation will likely fall moderately below 1973 levels. One month ago, the crop was

expected to be about 8 percent larger than last year's. The soybean crop will also probably fall below earlier expectations. With grain supplies already very tight, the shortfall in 1974 production levels will likely buoy prices over the next year. Furthermore, the hoped-for reductions in feed costs for livestock producers and some abatement in food prices have been blunted by this new outlook on the grain situation.

The drought has greatly reduced the carrying capacities of pastures throughout the District, forcing producers either to use supplemental feed ahead of schedule or to move animals to other points, including slaughter. The recent rains will help alleviate this problem, but more rain will be needed before the pastures begin to rejuvenate. If dry conditions persist, especially into and through 1975, heavy liquidation of animals will likely occur. While this will temporarily boost meat supplies in the short run, supplies in the longer run will be smaller and prices correspondingly should move higher.

In July total loans at Tenth District weekly reporting banks continued to rise at well above normal seasonal rates, with commercial and industrial loans accounting for most of the increase. Farm loans at these banks fell more than seasonally, but several banks anticipated that the demand for such loans would soon be stimulated by the drought and the increasing cost of feed grains. District reporters experienced a decline in demand deposits, mostly United States Government, and substantial gains in other types of deposits, with the result that total deposits grew at well above average seasonal rates. No larger banks indicated special problems in meeting targets for CD funds.

The situation at smaller District banks may be somewhat different. The tendency for farmers to withhold crops from market and the special problems

of cattle feeders appear to have caused deposits in smaller banks to grow less than seasonally and loan payoffs to be less than anticipated. Consequently, the normal seasonal easing of liquidity pressures may be delayed this year.

The overriding concern among bankers contacted was the \$2.25 billion issue of 9 percent Treasury notes being completed at the time of the survey. Consumer interest in these securities was resulting in substantial withdrawals of deposits from both banks and savings and loan associations. Although only one bank explicitly voiced concern about the cost of processing small individual orders., several of the banks noted a substantial concern over the longer run impact on deposits if such issues were to become more common.

ELEVENTH DISTRICT--DALLAS

Many of the labor contracts settled in the Eleventh District, since the end of the wage-price controls on April 30, are reported to have granted the biggest wage hikes in the history of collective bargaining in the Southwest. A survey of new multiyear contracts indicates that the first-year increases in wages and fringe benefits range from 7 to 12 percent, with most averaging about 10 percent. Increases during the remaining years of the contracts run about a third less. In addition, the typical contract includes cost-of-living adjustments that provide a one percent increase in the hourly wage rate for each 0.3 point rise in the consumer price index (CPI)--with adjustments made quarterly. For example, the 4-point rise in the CPI during the second quarter of 1974 would have boosted hourly wage rates under these contracts by 13 cents. The settlements apparently reflect organized labor's insistent demand that real wages be protected during periods when prices are subject to sharp and persistent advances. A key point in the negotiation of these agreements is reported to be labor's position that wages not be subject to downward adjustment in the event that living costs should decline.

In contrast to the new union contracts, salary increases for white-collar workers typically include a one-time cost-of-living adjustment of 5 to 7 percent and merit raises averaging 6 percent. Most respondents doubt that the income of salaried workers will keep pace with the rise in wages of their blue-collar counterparts--especially if the CPI continues to climb at a rate in excess of 10 percent.

Despite the record wage settlements, there have been some favorable contractual developments for Southwestern businesses. For example,

it has not been necessary to renegotiate any existing contracts containing emergency reopening provisions. And a new wage settlement was signed by a Texas steel manufacturer three months before the existing contract was due to expire. An executive of the firm attributed the prompt settlement in part to be the "Experimental Negotiating Agreement" signed last year, which contains provisions promising to pay workers a \$150 cash bonus if they do not strike.

Commercial loan officers at large banks in the District report that they are discouraging borrowing that "is not absolutely necessary" in response to the reduced availability of funds. In general, only loans to regular customers are being considered, and even these are kept to short term. High interest rates are driving many businesses to seek interim-term bank loans rather than financing through long-term debt or equity issues. Businessmen anticipate that these bank loans will be refunded in debt and equity markets when interest rates fall. However, one Dallas banker is concerned that these customers will not be able to roll over their loans for some time. Therefore, his bank is not making these loans.

Borrowing at banks to finance inventories remains strong, but most respondents expect the volume of these loans will level off as the rise in materials and other prices slows. In addition, bankers are encouraging customers to hold borrowing to the lowest level practical. Moreover, businessmen are reported to be returning to more prudent buying practices in accumulating their materials inventories, instead of engaging in "panic buying" and in stockpiling materials that are in short supply.

There have been reports in the financial media that many "country" banks are growing more reluctant to supply reserves to the Federal funds market. There is, however, no evidence that this practice is occurring to any significant extent in the Eleventh District. Sales of Federal funds to large District banks by correspondents and small country banks remain very high. Apparently, however, banks have become a little more selective and cautious with regard to whom they sell Federal funds. Interviews at several large banks in the District indicate that efforts are being undertaken to spread sales among more banks in order to reduce potential risk. While this cautious sentiment might result in a slight redistribution of funds, there has been no appreciable decrease in the District in the total volume of funds supplied to the Federal funds market.

New factory orders received by District manufacturers are generally running ahead of year-ago levels. Heavy demand is reported by producers of primary and fabricated metals, oil field drilling equipment, plastic products, and agricultural equipment. However, manufacturers of residential construction materials continued to experience sharply reduced sales, and petrochemical producers report a slight softening in new orders in the last month.

Most manufacturers are experiencing some relief from soaring prices of raw materials. A majority of the producers surveyed report the rise in materials prices has slowed in recent weeks. Moreover, prices of some items--including cotton, polyester, plywood, and carbon scrap--have actually declined. However, manufacturers of wood and plastic products have not experienced any letup in the skyrocketing costs of these materials.

TWELFTH DISTRICT--SAN FRANCISCO

Little change in the overall level of economic activity is expected by our directors. In their view, inflation will remain the number one policy problem. Manufacturing is generally at capacity levels, but shortages continue to hamper output. Consumer spending is described as steady to cautious. Residential housing activity is very weak, and this weakness is contributing to a slowdown in the lumber industry. The agricultural outlook is good. Banks face heavy loan demand, and some classes of borrowers are experiencing difficulties in raising funds. Our directors do not expect that there will be much real growth in GNP during the second half of the year. They are very concerned with inflation, and some think cost-push pressures are increasing. Business investment expenditures are heavy. Consumer spending is variously described as cautious or stable. Department store sales appear to be good, and automobile sales continue to show a recovery although considerable inventories of small cars have accumulated. Except for housing, no major weaknesses are apparent.

Manufacturing activity is very strong in most District states. Shortages and slow deliveries, especially of steel and chemicals, are causing production difficulties. Heavy equipment producers report large order backlogs, and Boeing's activity is helping to strengthen the Seattle economy. Strikes which had been causing disruption have been settled in many areas, for example, Portland and Salt Lake City, but they continue in some industries in Idaho, Washington and Southern California.

Nonresidential construction is maintaining its recent pace despite some strikes and shortages of structural steel. Some construction wage settlements were very high, and the resulting wage costs are expected to

weaken construction activity in the future. Residential housing is still weak with little sign of recovery, and multiple construction is even weaker. In the Portland metropolitan area, multiple units in the first half of the year were down 63.2 percent over the same period a year ago, and single-family houses were down 33.5 percent. Lack of housing activity has in turn contributed to falling lumber demand. Lumber production has declined in the Pacific Northwest, and some mill closings are expected. In contrast, pulp and paper and packaging materials are continuing to keep that part of the forest products industry at or near capacity production.

The Seattle-Tocoma-area economy is sustained by aerospace, agriculture, and pulp and paper industries. The Alaska pipeline development is also stimulating port activity. In western Washington, the Spokane world's fair has stimulated local construction and tourism, and the region's agricultural crop prospects are excellent. Except for lumber, the Oregon economy is experiencing a good year, particularly in agriculture and manufacturing. Agriculture shows some weakness in Idaho and Utah, where cattle production is more relatively important, but producers of potatoes and other crops in irrigated areas expect large crops. Agricultural processors are expanding capacity, and mining activity also contributes to the strength of the local economy. California's overall level of growth is expected to be somewhat above the national average. Like most other District states, its agricultural outlook, except for cattle, is good. Business activity, although hampered somewhat by strikes, should remain high. Tourism in the state appears to be recovering.

Banks report that commercial loan demand remains strong, and consumer and real estate loans have been growing modestly. The real

estate demand at banks reflects the reduced lending capacity of savings and loan associations. Consumer-type savings deposits are not showing much growth, and the larger banks have had to bid for C-Ds in the money market.

High interest rates had some impact on credit demands. Some projects have been postponed, but many firms have turned to bank lines in order to avoid long-term market issues at this time. Issues are being postponed because long-term rates are expected to be somewhat lower next year. Capacity expansion is being financed in many cases by internal funds and in a few instances from either foreign customers or through Euro-dollar loans. High rates have hurt those industries which ordinarily rely upon the money market or other short-term sources for a large proportion of their funds, for example, finance companies, leasing companies, and auto dealers.

Public utilities are experiencing particular difficulties. A Washington power company held back from marketing a new long-term issue and has been relying upon bank debit, but Pacific Northwest Bell went to the market and received a 8.90 percent rate. Consolidated Edison's problems, in the view of some utilities' management, have made all utilities' issues more difficult to float. One utility applied to the SEC for an exemption to sell an issue to underwriters on a negotiated basis rather than to use competitive bidding.