

SUMMARY OF COMMENTARY ON CURRENT ECONOMIC CONDITIONS
BY FEDERAL RESERVE DISTRICTS

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TABLE OF CONTENTS

SUMMARY.....	i
First District - Boston	I-1
Second District - New York	II-1
Third District - Philadelphia	III-1
Fourth District - Cleveland	IV-1
Fifth District - Richmond	V-1
Sixth District - Atlanta	VI-1
Seventh District - Chicago	VII-1
Eighth District - St. Louis	VIII-1
Ninth District - Minneapolis	IX-1
Tenth District - Kansas City	X-1
Eleventh District - Dallas	XI-1
Twelfth District - San Francisco	XII-1

SUMMARY*

Overview

Retailers across the country enjoyed an excellent Christmas season. Year-over-year sales increases, largely real, were well into double digits. Post-holiday sales were also relatively strong. Increases in manufacturing activity were widespread. Price hikes are becoming more frequent; delivery times are lengthening. Capital spending is picking up; the emphasis is on modernization but some capacity expansion is also planned. In the banking sector, commercial and industrial loan demand increased modestly, consumer loan demand strongly. Homebuilding and housing sales have held up well in most districts. Severe weather damaged citrus and vegetable crops in the South, but did not affect winter wheat in the Midwest.

Retail Trade

Retail sales were very strong this Christmas. Year-over-year sales gains in December were in the 10 to 25 percent range. Several districts noted that these increases were largely real. Sales of big ticket items such as appliances, consumer electronics and recreational equipment were

* Prepared at the Federal Reserve Bank of Boston

particularly strong. Apparel also fared well in some areas. Credit use was heavy, according to Chicago, Minneapolis and San Francisco. Sales volumes in early January were also good, but the year-over-year increases were not as large as in December. Inventories are generally satisfactory. Retailers are optimistic about 1984 and in the Philadelphia district they are more worried about losing sales than about accumulating excess inventories.

Automobile sales have been brisk, although low inventories have been a limiting factor in several districts.

Manufacturing

The manufacturing sector continues to recover. Increases in orders and production were widespread. Among the industries for which increases were reported were motor vehicles and automotive products, especially trucks; nonelectrical machinery; electronics; some types of steel; chemicals; semi-conductors; paper and paper board. However, an expected upturn in farm equipment did not materialize. The demand for aircraft remains depressed in the Cleveland district, but has improved in San Francisco. Boston notes that export sales remain very weak, although sales by foreign subsidiaries are improving slightly.

Capital spending is picking up. Philadelphia, commenting on its survey of manufacturers, observes that "for the first time in seven years, half of the respondents...intend to increase outlays for plant and equipment during the next six months." The emphasis is on modernization and productivity enhancement, but some expansions are planned.

Price increases are reported to be more frequent but, for the most part, still moderate. Lead times are lengthening. According to Chicago, cutbacks in domestic capacity have contributed to the scattered supply problems.

In the Atlanta and Dallas districts, higher rig counts point to a recovery in drilling activity. Minneapolis also reports an upturn in oil activity, but not in gas and coal.

Increased manufacturing activity has been reflected in more trucking and railroad business in the St. Louis district. Barge traffic has also been increasing gradually.

Banking

Commercial and industrial loan demand increased modestly in several districts, declined in St. Louis and rose sharply in Cleveland and Kansas City. Demand for consumer loans is strong in most districts. As loan demand has increased, banks have improved credit quality but become somewhat less liquid, according to Richmond.

Real Estate

Homebuilding and housing sales have held up well in most districts, although New York, Kansas City and Cleveland report a slowing in sales at year-end. Respondents in New York and Cleveland do not expect 1984 to be as strong as 1983 because most of pent-up demand has been satisfied. New York and Atlanta are also concerned about the effects of shortages and the increasing prices of housing materials. However, Chicago builders expect

1984 to be a better year and Richmond reports an upturn in speculative building, indicating that industry expectations are high. Variable rate mortgages are becoming more prevalent in the Chicago and San Francisco districts; initial rates are substantially below those on fixed rate mortgages.

Agriculture

Severe weather damaged citrus fruit crops in the Dallas and Atlanta districts. Fresh vegetables were also affected. However, San Francisco growers expect to benefit from the resulting price increases. The weather does not appear to have harmed the winter wheat crop, but cattle are not gaining weight at normal rates.

FIRST DISTRICT - BOSTON

Retailers in the First District enjoyed a very successful Christmas season. Hard goods, especially electronics, sold particularly well. Inventories are satisfactory. Plans for 1984 are optimistic. Manufacturers are also very confident that 1984 will be a good year, but they are apprehensive about 1985. Capital spending is picking up but the emphasis is on productivity enhancement rather than expansion. Exports remain very weak. Price increases seem to be more frequent, but firms are still very cautious about raising prices. Mortgage lending by thrift institutions declined in the fourth quarter. Commitment rates for fixed-rate mortgages have been edging lower.

Retail

Retailers in the First District report very strong sales gains in December. They are optimistic about 1984. Hard goods in general and electronics in particular highlighted a highly successful Christmas shopping season. Local merchants again commented on the Northeast's strength compared to associated stores in other regions.

For two of the firms contacted sales in December were more than 20 percent above sales in comparable stores in December a year ago. (Most newspaper reports of sales growth are not on a comparable stores basis.) Departments performing very well included video cassette recorders, tapes and records, computers, microwave ovens, TVs and other appliances, hardware, physical fitness products, and women's coats. A store selling

mostly apparel and other soft goods attributed "good but not outstanding" results to a lack of consumer hard goods.

All those contacted have optimistic plans for 1984, with one firm's optimism bolstered by 24 percent sales growth to date in January. Inventory levels are satisfactory. Merchants attribute consumer enthusiasm to steady prices (and even declining prices for some computer and electronics items) as well as to the general recovery.

Manufacturing

First District manufacturers are confident that 1984 will be a good year, but they are apprehensive about 1985. Everyone contacted has seen an upturn in business, with several reporting that their most recent quarter was "excellent." While order and shipment increases have been widespread, sales of automotive products - both original equipment and after-market - have been particularly robust. Demand has also improved markedly for smaller-scale, productivity-enhancing capital goods. Still languishing are very large, capacity-expanding capital goods and projects. One respondent noted that the only markets today for increased capacity in such basic industries as autos, steel and energy are overseas; and these overseas markets are drying up because of the strong dollar. Exports of all kinds are the other major area which remains very weak. In contrast to exports, sales of overseas subsidiaries seem to be picking up a little.

The capital spending plans of First District manufacturers are consistent with the pattern they observe in their own sales. A number are increasing capital spending, but the emphasis is on productivity improvement. Two respondents are adding to capacity, but most have no

plans to expand and several are consolidating their operations in fewer plants.

Employment levels are rising for most firms, although one respondent foresees a large layoff in one division. Several manufacturers noted that they are producing more output with fewer people than in the past.

Price increases seem to be more frequent. Most firms say they see more increases in the prices of purchased materials and components. Paper, steel and aluminum were mentioned. Several of the firms contacted have recently increased their own prices. Nevertheless, manufacturers are still very cautious about raising prices and will back off if the increase meets a lot of resistance. According to an automotive supplier, the auto companies are negotiating long-term contracts with price decreases in the first year and very modest increases thereafter. One respondent expressed concern that the wage settlement to be negotiated between GM and the UAW in 1984 will be very large and will set a pattern for other industries.

Mortgage Lending

Mortgage lending by thrift institutions declined in the fourth quarter but remained far above the level in the fourth quarter of 1982. Loan repayments appear to have exceeded loans made in the fourth quarter, but for the entire year loans were ahead of repayments. Mortgage rates have declined slightly from the highs of late summer.

SECOND DISTRICT--NEW YORK

Introduction

The improvement in the Second District's economy is continuing at a moderate pace. The Christmas season was a strong one for area retailers, with sales gains over the lackluster year-earlier period in the 10 to 20 percent range. Manufacturing activity continues to expand, led by strength in the automotive sector. Purchasing managers note a pickup in orders and an increased willingness to accumulate inventories. The nonresidential real estate market remains strong with a quickening pace of leasing activity and the announcement of new building projects. Residential construction is at a seasonal low but the outlook for the spring is favorable. On the financial side, banks report a modest increase in business borrowing and strong demand for consumer credit.

Consumer Spending

Second District retailers reported brisk sales during the Christmas season, with over-the-year increases in December generally in the 10 to 20 percent range. Business exceeded expectations at most stores and only one upstate New York chain recorded a December-to-December gain of less than 10 percent. Spending was generally heavy from the Thanksgiving weekend to Christmas, and a wide range of products was reported in demand. This contrasted with

1982 when sales were weak until late in the season and stores engaged in heavy promotional activity prior to Christmas. Sales continued strong in the final week of 1983 but in early January reports were more mixed, with growth over 1983 ranging from flat to 20 percent. Some stores report low levels of inventories and a desire to replenish stocks. Others plan to increase inventories only in line with sales. Most retailers expect demand to remain strong compared to the levels of a year ago, but with much smaller over-the-year gains than in December.

Business Activity

Business activity in the Second District continued expanding at a moderate pace in recent weeks. While the automotive industry remains the major source of strength throughout much of the District, other manufacturing industries reporting improvement were electrical and nonelectrical machinery, fabricated metals, chemicals, and food products. New orders are continuing to improve, and purchasing managers in some upstate areas noted an increased willingness to accumulate inventories.

Several companies have recently announced plans to open new facilities in the District. These include a large printing plant in Saratoga Springs, a computer operations center on Long Island, and a factory for producing computer components in the Poughkeepsie area. In addition, a number of companies will soon begin expansion and renovation of their existing operations. The largest of these projects is a \$67 million, 2-year modernization and expansion of a

paper mill in upstate New York. In most cases these new installations and expansions are expected to generate increased employment.

Unemployment has declined in the Second District in line with the national trend. The December unemployment rate in New York State was 7.4 percent, an over-the-year improvement of 1.7 percentage points, while New Jersey's 6.8 percent rate was 2.4 percentage points below its December 1982 level.

Construction and Real Estate

Residential construction activity is at a seasonal low now that cold weather has moved into the District. Traffic and sales have also slowed and are not expected to pick up before the end of January. Over the next few months though, the outlook remains bright. Homebuilders are fully booked through the spring. Nonetheless, many question the sustainability of last year's construction pace. They believe that most of the pent-up demand has already been satisfied and that lower mortgage rates and stable housing prices will be needed to generate much additional interest from potential homebuyers. Builders seem skeptical that prices will stabilize in the near-term because of ongoing labor and materials shortages. And the likelihood of continuing large Federal deficits makes them doubt that mortgage rates will decline much.

The nonresidential real estate market continues to exhibit signs of strength. Leasing of office space has progressed at a brisk pace and generally without significant rent reductions or

other landlord concessions. Although nonresidential starts have been scarce, several new plans for future projects have recently been announced. Some of these represent expansions into what are generally considered secondary locations such as the West Side and the area north of the World Trade Center in Manhattan, and north of the Route 287 corridor in Westchester County.

Financial Developments

Banks in the Second District have reported a modest increase in business borrowing during the last month. Inventories, receivables, machine tool purchases, construction, and capital expansion were cited as uses for the increased loans, although no one purpose was singled out as being particularly significant. One respondent noted an expansion of loan demand at middle-size corporations but no increase for the largest corporations.

Consumer borrowing remained strong in recent weeks. In particular, auto loan demand was cited as being robust. Some banks reported that strong consumer credit demand has continued into early January instead of the usual after-Christmas slowing.

THIRD DISTRICT - PHILADELPHIA

The Third District economy appears to be off to a good start in 1984. Significant gains are reported in the manufacturing industry since early December, and retailers, having recently enjoyed a banner holiday season, report very good January sales. The financial sector, although awaiting a long overdue pickup in commercial loan activity, continues to experience strong retail loan demand.

Third District contacts have a very positive outlook for the first half of 1984. Manufacturers' plans for increasing capital expenditures are at a seven-year high and retailers are forecasting double-digit gains in sales over the first half of 1983. Bankers expect to see a pickup in C&I loan activity and also remain very confident about retail loan demand in 1984.

MANUFACTURING

Respondents to the January Business Outlook Survey indicate significant gains in local manufacturing activity from December levels. Over 48 percent of the manufacturers surveyed report an increase in overall activity, while only 6 percent indicate a decline. New orders and shipments have posted gains comparable to their increases during most of 1983, and unfilled orders have made their strongest monthly advance since early fall. At the same time, inventory levels remain steady and marginal gains are reported in employment.

Manufacturers' outlooks for the first half of 1984 are very positive, as 3 out of 4 survey respondents are forecasting higher levels of activity by July. Highlighting the manufacturing forecast once again are planned capital expenditures; for the first time in seven years, half of the respondents to the survey intend to increase outlays for plant and equipment during the next six months. Widespread increases also are predicted in new orders, shipments, and producers' backlogs, and area businessmen are projecting gains in both inventory levels and employment.

Industrial prices are reported to have risen in January from December levels. About one-third of those polled report higher input prices while one-fourth say they have received higher prices for their finished products. Looking ahead, 82 percent of the manufacturing executives surveyed expect to face higher materials prices six months from now and 65 percent foresee higher prices for finished goods.

RETAIL

The Third District retail industry enjoyed one of its best holiday seasons in recent years in 1983 and is currently experiencing very satisfactory January activity. December sales ranged from 10 percent to 25 percent higher than those of the previous Christmas season, and several major retailers report early January volume to be 15 percent better than a year ago. The traditional January home furnishing promotions and "white sales" are in full swing in the Third District, with most contacts indicating current activity very close to expectations. Retail executives also report ideal inventory conditions over the last six weeks: very few items were in short supply during the holiday season, yet little was left unsold at the year's end. Despite the absence of widespread markdowns, characteristic of early January, the "new" merchandise on store shelves is selling very well.

Merchants remain confident that the recovery will continue and, consequently, are forecasting sales for the first half of 1984 to exceed those of 1983 by roughly 10 percent. One major retailer anticipates a 20 percent gain over its solid 1983 performance. Inventory plans reflect their optimistic sales forecasts. There appears to be a greater concern over preventing a loss of sales due to short supply than over holding excess merchandise.

FINANCIAL

Although Third District bankers generally agree that loan activity in the retail sector has increased consistently in recent weeks, they report varying conditions in the commercial and industrial sector. While most contacts note a 2 percent to 5 percent increase in C&I volume since early December, one banker, who deals with relatively small businesses, reports a recent surge in activity. The same executive also reports a 20 percent increase over last year in commercial loans outstanding, while year-to-year figures at other banks are mixed. Retail lending performance, on the other hand, continues to please Third District financial executives. Led by credit card lending and home improvement loans, consumer loans are growing at a 12 percent to 18 percent annual rate in January.

Although bankers have tempered their optimism over C&I activity due to its continued sluggishness, they are generally forecasting solid demand for both commercial and retail loans in 1984. Contacts maintain that a pickup in C&I demand is imminent given that the recovery continues. On the retail side, executives forecast a strong year, especially in automobile and home improvement loans.

The prime rate remains at 11 percent at area banks and most contacts believe that interest rates will remain within 25 to 50 basis points of their current levels throughout 1984. Forecasts of the direction in which rates will move differ among bank executives. Those predicting lower rates cite the fact that 1984 is an election year and also that the recovery shows signs of slowing down; others feel that private credit demands, the deficit, and increasing inflation could push rates slightly higher.

Fourth District - Cleveland

Summary. Economic activity in the District continues to improve. The employment situation is mixed, as firms have been reluctant to recall workers, and are stressing overtime and productivity increases. Retail sales were strong in the holiday and post-holiday seasons. Manufacturing activity continues its strong growth from recently depressed levels. Production of flat-rolled steel for consumer goods is strong but demand for other steel products remains weak. Capital goods production is strengthening from a low base but imports are hindering recovery for some products. Demand for automobiles is growing and some parts suppliers have reached capacity limits. Firms are cautious about increasing capacity; capital spending is emphasized for modernization rather than expansion. House construction may have topped out. Loan demand, especially for commercial and industrial loans, is strengthening.

District Labor Market Conditions. Labor market conditions in this District show mixed trends, and the unemployment rate remains well above the national average. In Ohio, the numbers of employed and unemployed workers both declined (s.a.) in December. The unemployment rate has fallen to 10.4% from 11.5% in September (s.a.) but remains 2.2 percentage points above the national rate. Unemployment (n.s.a.) rates in eleven major SMSAs in the District in November ranged from 8.5% in Columbus, Ohio to 14.1% in Youngstown.

Production workers in Ohio manufacturing firms achieved record average weekly earnings in November as overtime work continued to increase. Hourly earnings increased slightly but the average workweek increased by one-half hour to 42.5 hours.

Retail Sales. Fourth District retailers report an active holiday season, and express optimism over the first quarter sales prospects. Some report sales were unusually strong in the first two weeks after Christmas. General merchandise sales are roughly 10 to 14 percent above year-ago levels, according to three major retail chains the district. Sales gains were achieved in almost all merchandise categories, especially apparel and household furnishings. Fourth District sales of both domestic and import cars were also brisk during the holiday period. Import dealers are not currently experiencing shortages, but most expect shortages to develop again by early February. Domestic new-car dealers indicate that inventory positions are near desired levels.

Manufacturing. Manufacturing activity continues its upward trend in this District. A survey of Cleveland area purchasing managers for December indicates production was higher than in the preceding month for a larger percentage of respondents than any time since April 1977, and new orders were higher for a greater percentage of respondents than any time in over ten years. Respondents report rush orders and split shipments are becoming more common. Finished goods inventories are rising slowly. Employment is unchanged, suggesting that firms are using overtime to expand production.

A survey of purchasing managers in the Cincinnati area indicates production, new orders, and backlogs are growing, although less rapidly in December than in October. Strong price pressures are reported for commodities. Delivery time is increasing and split shipments are becoming more common. Finished goods inventories are rising.

This Bank's survey of Fourth District manufacturers indicates that firms expect moderate growth of shipments, new orders, and inventories in

January. Employment is expected to hold steady while average weekly hours worked is expected to increase.

Steel. Production of flat-rolled steel used in consumer goods is near capacity but demand for oil-country goods and construction steel remains weak. A major steel producer reports gradual improvement in demand from the capital goods sector. Another firm reports December shipments strengthened as buyers anticipated early 1984 steel price increases. Industry production is currently about 70% of capacity, adjusted for plant closings. One firm estimates the new breakeven point, given present prices, is 68%-70% of capacity, and suggests that all producers can expect to make a profit in 1984.

Capital Goods. Orders for heavy duty trucks have been strong since August because of the need to replace the existing fleet of trucks. The recent surge in demand has caused supplies of some truck components to be tight. A supplier reports being at full capacity in truck-related production, partly because his capacity was reduced in 1982 and 1983. Demand for parts for construction machinery is beginning to improve but parts demand for aircraft and agricultural equipment remains weak.

A machine tool producer reports orders have doubled from six months ago but nevertheless are still at a low level. Orders are unlikely to reach their previous peak because foreign producers now have 40% of the domestic market. Nevertheless, production of machinery to produce some electronic equipment is at capacity, and a producer expects large productivity gains from electronic equipment to dwarf interest costs as a consideration by purchasers in 1984.

Automobiles. Sales of new cars rose substantially in 1983:IVQ, following a supply-constrained third quarter. Orders are continuing their

gradual strengthening, but dealers are keeping inventories tight. A major producer reports some suppliers are at capacity, sometimes hindering automobile production. A need for additional capacity by parts suppliers is reported because many suppliers went bankrupt during the last recession. Nevertheless, suppliers are reluctant to expand capacity because of uncertainty about the duration of the current expansion.

Construction. Orders for new houses are down, and are unlikely to match last year. Builders of single-family homes report that new orders in the fourth quarter were down by 10% to 12% from a year earlier. The outlook for housing construction in 1984, according to a major Fourth District builder, is fairly good, but won't match 1983's performance because pent-up demand is not as strong as in early 1983, and interest rates are not expected to fall to the 12 1/2% levels reached in early 1983.

Commercial Banking. Loan demand appears to have strengthened at Fourth District banks in recent weeks. An increase in loan volume is evident for virtually all loan categories and especially for commercial and industrial loans and loans to financial institutions. Demand, saving and time deposit growth were not exceptionally strong. District banks apparently funded loan demand by running down their holdings of liquid assets and by issuing large denomination certificates of deposit. In particular, bank holdings of short-term Treasuries and federal fund sales both declined.

COMMENTARY ON ECONOMIC CONDITIONS

FIFTH DISTRICT - RICHMOND

Overview

Fifth District business and economic activity is continuing to expand across a broad front judging from available evidence. In the manufacturing sector shipments, new orders, and order backlogs all made further gains in the latest month as did employment and the length of the average work week. Inventories were down sharply. Among retailers, department stores and other general merchandise dealers still contend that the holiday season provided a spectacular conclusion to a very good year. Most have reported double digit gains, December to December, with little of those gains absorbed by price increases. Housing and construction, also, are holding the gains of spring and summer. The residential sector is seeing more speculative building of late in anticipation of a spring resurgence of sales. Financial institutions have recently experienced moderate growth in loan demand, largely on the consumer side. With little deposit growth, however, liquidity is down from the unusually high levels reached in the fall.

Manufacturing

The recent advance in manufacturing activity apparently continued through the latest month. Shipments, new orders, and order backlogs all showed further increases from the previous month. The rate of increase in new orders seems to have fallen off somewhat, but seasonal factors in a few industries are largely responsible. Across the sector employment was up moderately and the average work week increased slightly. Nonetheless, there was a significant inventory runoff, particularly of finished goods, but

materials were also down. Most District manufacturers are comfortable with current inventory levels.

For the most part these developments have occurred consistently across industries, and there are few notable exceptions. Particular strength has recently appeared in primary metals and machinery and equipment, however, and seasonal weakness is most apparent among furniture manufacturers.

Consumer Spending

Reports from District retailers continue to suggest very strong activity through the end of the year. Many department stores around the District have reported sales gains of 12 percent to 26 percent, December 1983 over December 1982. A nationwide chain specializing in home appliances and consumer electronics and entertainment equipment reported a year over year gain of 43 percent for the month. One major exception to this pattern is a large catalog showroom retailer, which showed a year over year gain of less than 2 percent.

In addition, there are indications that at least some dealers were able to trim promotional activities at year end while holding sales levels and preserving margins. Despite some concern just prior to the holiday selling season, there are few indications that stock outages or inventory shortages presented any generalized problems. With the exceptions of a few lines and an occasional sale item, dealers were apparently able to meet customer demands.

Automobile sales are also reported to have held up surprisingly well over the month. Some import dealers continue to encounter supply problems, selling, as they say, everything they can get their hands on.

Otherwise, activity is characterized as robust, but stable, despite a continuing shortage of low mileage used cars.

Housing and Construction

The construction sector also remains quite lively. The commercial and industrial side continues to make steady month by month gains, and the level of activity is now significantly improved from earlier in the year. The principal strength in the industry, however, is still originating in the residential sector. By nearly all accounts sales of residential property continue apace, and builders are trying to get ahead in anticipation of spring sales. For the first time in a good while there is talk of speculative building going on. Clearly, industry expectations are for another good year in the District's housing sector.

Banking and Finance

Loan demand at District financial institutions is still growing moderately, and growth remains largely on the consumer side. Nonetheless, as deposit growth has slowed and loan demand has picked up, however moderately, institutions have moved to restore credit quality and have become somewhat less liquid. Most institutions seem to be comfortable with current credit quality and loan to deposit ratios.

The Outlook

Business people in the District remain, on balance, strongly optimistic. Retailers seem to think they can hold the gains of 1983 and have another very good year. Manufacturers are looking for further improvement and most expect progress over at least the next six months. The reemergence of

speculative house building attests to the positive outlook in that sector.

One of the few negative notes comes from the textile industry where there is still much concern over import competition.

SIXTH DISTRICT - ATLANTA

Construction and consumer spending continue to sustain economic recovery in the Southeast, and contacts are optimistic about 1984. Retailers enjoyed the best holiday sales in the last four years. Housing purchases remained strong through December despite rising mortgage rates and adverse weather. Strength in these sectors has prompted recalls of laid-off manufacturing workers and sharp increases in orders in construction-related industries. Lending activity slowed in December, but bank deposits advanced sharply. Unusually cold weather adversely affected tourism and agriculture. Losses of vegetable and citrus crops have pushed up prices.

Employment and Industry. Industry contacts believe that labor market conditions continued to improve through December and gains will persist at least through the first quarter. In November, unemployment fell in four of the six District states. Manufacturing employment grew by over 85,000 from November 1982 after falling by 161,000 in the previous 12-month period. Vigorous auto sales led to the recall of 1,600 workers for a second shift at a large auto assembly plant near Atlanta. The scheduled mid-February reopening of a large Alabama sheet steel mill and the attendant recall of 2,500-3,000 workers bodes ongoing improvements in manufacturing employment. Contacts expect 1984 to be a good year for the timber industry as well. Boosted by renewed vigor in the housing industry, southeastern construction employment rose 38 percent in November above year-earlier levels. The American Plywood Association indicates that 1983 plywood production, nearly 25 percent over 1982 levels, attained record highs, largely as a result of increased demand in the "do-it-yourself" market. A rig count increase from 282 in November to 321 during December betokens recovery in Louisiana's oil and gas exploration industry. Many chemical plants in Louisiana found themselves ill-equipped to cope with the unusual Christmas cold spell, but an industry

spokesman believes the short-lived production halts may have helped stabilize falling prices.

Consumer Spending. District retailers surveyed about December sales regard 1983 as the best year since 1979. New car sales sustained the momentum of recent months despite unusually cold weather. Department store merchants report double-digit increases over the previous year. Retailers cite apparel, big-ticket items, and jewelry as leading holiday sellers. These reports suggest a continuation of the healthy growth shown in November's state sales tax receipts. Merchants perceive widespread consumer optimism about employment prospects. If this optimism is well-founded, retail spending should remain strong in 1984.

Construction. December's housing sales were slightly above normal despite unusually severe weather and rising conventional interest rates early in the month. Realtors report increases in the share of used homes sold and in the proportion of buyers "trading up." Improved employment opportunities and transfers account for much of the real estate activity in Nashville, Mobile, and Jacksonville. The sale of houses to retirees in Florida is strengthening as national economic improvements enable homeowners to sell their residences elsewhere. Builders who have moved from Houston's saturated market are stimulating residential construction in Orlando, and realtors expect this trend to continue. Area lenders say that the deregulation of the FHA mortgage rate has resulted in higher rates and lower discount points. Confusion over post-deregulation requirements for FHA loans made some lenders less willing to make FHA loans. In the opinion of those surveyed, FHA activity should increase as lenders become more familiar with the loans' new terms. However, some builders fear recent price increases in supplies will dampen the pace of residential building. In the last two months, the number of single-family building permits declined on a seasonally adjusted basis.

Office space absorption and construction in Atlanta and Nashville continues at a brisk pace. Shopping center development is reviving throughout the Southeast. However, commercial construction in Orlando has slowed from its previously booming pace. Realtors fear that Orlando and several other cities may have excessive inventories of office and hotel accommodations on the market or under construction.

Financial Services. After maintaining strong growth for six months, loans at large banks advanced only slightly on a seasonally adjusted basis from November to December. The slow growth is attributable to a decline in real estate lending, flat demand for consumer loans, and a moderation in the recent strong growth of commercial loans. Bank contacts report that loan demand through early January increased over late last year, although the improvement in Mississippi has been modest. Respondents most often cite commercial lending as the fastest growing segment, but Florida and Atlanta contacts report that consumer lending is strong. S&L spokesmen indicate that loan applications are at least maintaining, if not surpassing, the rate of late last year.

Deposits at large banks ended 1983 with the strongest monthly showing since June. The strength is attributable to faster expansion of both demand and time deposit accounts and the continued strength of savings. Jumbo CDs contributed significantly to the spurt of deposits in December. Savings at thrifts grew slowly in December and early January, according to those surveyed. Contacts do not expect the January 1 elimination of the quarter point advantage formerly held by S&Ls on regular savings accounts to trigger the sort of competitive struggle in the Southeast that attended the introduction of MMDAs a year ago; competition is concentrated in higher rate accounts.

Tourism. Cold weather weakened the performance of the tourism industry in December. Visitor center registrations declined relative to year-ago levels in three states, and attendance at most southeastern attractions fell. Hotel occupancy is still soft in most cities. Even in Orlando, occupancy fell 7 percent in November after 14

months of increases. Air travel continues to improve because of rising passenger volume and expanded carrier service at southeastern airports. The relatively small (1-2 percent) increases in revenue-passenger miles reported in December by the major southeastern-based carriers are probably attributable to unusually high year-earlier volumes. Discounts triggered much of the year-ago increase. Since the proportion of passengers flying on discount has declined, present levels indicate healthy conditions despite the modest nominal growth. Renewed auto-train service from Virginia to Florida has generated strong demand. Most southbound routes are sold out, and advance bookings are reportedly heavy.

Agriculture. The unexpected freeze at Christmas inflicted substantial injury on Florida agriculture. Grower losses may exceed \$500 million. Approximately 85 percent of the state's orange crop had not been harvested when the cold struck. The most recent USDA estimate projects a 23 percent loss in the orange crop with a concomitant 13 percent decline in juice yield per box. By early January the wholesale price of orange juice had climbed 15 percent above its pre-Christmas level. Imports of Brazilian orange juice should temper the impact on consumers somewhat, but Brazilians have increased prices 18 percent from last season in anticipation of strong demand.

Consumers will face much sharper price increases for fresh vegetables until new crops reach harvest. The wholesale price of lettuce has more than doubled since the freeze. Tomatoes, pepper, and squash also incurred extensive injury. Higher prices will partially offset citrus crop losses, but revenues for many growers will be below earlier expectations. Vegetable growers' annual revenue should decline because they have lost their most advantageous marketing period. The freeze has reduced employment except in south Florida, where many growers have undamaged fruit suitable for sales as fresh produce, and in portions of central Florida, where growers are rushing oranges to juice processors.

SEVENTH DISTRICT--CHICAGO

Summary. In early 1984 business activity in the Seventh District is on the uptrend over a broadening spectrum of sectors. Evidence available in the District does not indicate the "slowing" suggested by some national data. The general view here is that the improvement will continue through 1984, but with a possible dampening effect from higher interest rates in the second half of the year. Employment in manufacturing is rising, but gains in nonmanufacturing are modest at best. Reports on retail sales were strong for December. Inventories are generally low. Demand for some types of mechanical capital goods, e.g. construction equipment, is strengthening. Wholesale prices are firming, but many remain below 1979 levels. Residential construction is expected to increase again in 1984, but remain far below peak years of the 1970s. Severe cold adversely affected some sectors in late December, but stimulated outlays on batteries and plumbers' bills. Rising demand is causing shortages of some materials such as gypsum board and has boosted backlogs for heavy trucks and trailers and large autos.

Shortages and Leadtimes. Reports indicating pressure on capacity are becoming more frequent. For December, 38 percent of the purchasing managers in Chicago and 48 percent in Milwaukee reported longer delivery leadtimes, while only a few reported shorter leads. In late 1982, delivery times were shortening. The stretchout has been particularly marked for truck trailers and custom-built heavy trucks. Large cars also are back ordered. Gypsum board producers say that shortages in the South are attracting high-cost shipments from Canada. The piggy-back rail car fleet is fully utilized. There are also some reports of tight supplies of steel sheets, computer chips, refrigerators, and car batteries. Problems of supply partly reflect cutbacks in domestic capacity. Most industries still have ample capacity, and steps are being taken to eliminate bottlenecks.

Prices. Some 45 percent of District purchasing managers reported paying higher prices in December, while only a few paid lower prices. A year earlier companies paying lower prices still outnumbered those paying higher prices. Prices have not risen sharply except for a few cases such as aluminum and airline fares. More moderate increases are also reported for castings, forgings, paper and paperboard, gypsum board, and some types of steel. In most industries where prices have increased, analysts insist that substantial further increases must occur if profit margins are to return to a prosperous level. Further increases in utilization rates are necessary, however, before the competitive situation will permit such increases in these industries.

Consumer Purchases. General merchandise retailers were very pleased with sales in the Christmas season. Sales of recreational equipment, appliances, computers, telephones, and auto accessories were especially strong. Auto sales were held back by availability of large domestic cars and Japanese cars. Credit use has been heavy, and delinquencies have been low--probably as a result of careful screening in response to more lenient bankruptcy laws. Airline traffic in December only about equalled year-ago, partly because of weather, but also because most bargain fares have been withdrawn.

Employment. Improved job markets in the District are still largely a result of callbacks in manufacturing. Rehires by motor vehicle and parts plants are by far the most important, but there have also been gains in appliances, mobile homes, and recreational vehicles. Residential construction is also up. In November, all District states, with Michigan far in the lead, reported good gains in factory employment from late 1982, but the shortfall from late 1978 still ranged from 15 percent in Wisconsin to 20 percent in Iowa, and 24 percent in Illinois, Indiana, and Michigan. Total non-manufacturing employment data show no improvement through November. State

and local governments, public utilities, and financial institutions are generally hiring only to fill essential vacancies, and many are reducing staff.

Steel. Raw steel facilities are expected to operate at 65 percent of capacity in the first quarter versus 60 percent in the fourth quarter. Rates will be higher at the most modern Chicago-area mills. Demand for all types of steel is stronger, but the concentration is in cold-rolled steel, mainly for auto and truck bodies, and hot-rolled sheet for frames for trucks and large cars. Tubular "oil country" products are picking up from a low level. (Quality of some pipe on hand had deteriorated.) Demand for plates, for producer goods, and heavy structurals, also has improved, but very slightly. Steel mill operations were handicapped by a variety of problems during the severe cold of late December.

Capital Goods. Mechanical-type capital goods (non-electronic) are showing signs of life. Orders for large and double trailers, authorized last year, are three times current capacity, and quoted delivery times are for September. Producers of heavy-duty trucks to haul trailers are quoting April deliveries. Capacity to produce heavy trucks has been reduced and may be under strain if demand continues to rise. But the capital goods picture in the District is still far from satisfactory. Relatively few laid-off workers have been called back. Orders for freight cars increased in December, but from a very low level. In farm equipment, the anticipated spurt in sales before the turn of the year to gain tax advantages did not materialize.

Parts Versus Finished Goods. The capital equipment improvement is still characterized as a repair, replacement and modernization market, rather than an expansion market. Modest increases in demand for forgings, castings, components, steel bars, drill bits, and fasteners are in line with this assessment.

Electric Power. Electricity usage has increased in the past month or two reflecting both higher industrial demand and cold weather. This rise was welcomed by District utilities, some of which are under unprecedented financial strain. The power industry, once a rock of stability, faces perilous times because of an adverse regulatory atmosphere (both on rates and environmental considerations), and questions concerning costly facilities under construction that are not needed to accommodate prospective demand.

Housing. Sales of new and used houses, which slipped from the rates reached last spring, have held up better than many observers had thought possible. Assuming no significant rise in interest rates, builders expect a further increase in starts in 1984. However, the District total would still be about 50 percent short of the best years in the 1970s. An important reason for optimism in the Chicago area is the sharp rise in use of variable rate mortgages from about 25 percent last spring to 50 percent in October--even higher in new homes. First year mortgages rates of 10 percent or less are available, usually with 3 or 4 percent fees. A wide array of terms are offered, so "shopping around" on the part of home buyers is advisable.

EIGHTH DISTRICT - ST. LOUIS

The upward momentum of the economic expansion in the Eighth District continued in December and early January. The Christmas season surpassed retailers' optimistic expectations despite severe cold weather in the last two weeks, and after-Christmas sales have been satisfactory. Manufacturing has been improving almost across the board, most transportation companies are moving more goods, and employment has risen markedly since early fall. Real estate sales and construction activity have remained strong despite a seasonal slowing.

Outlook

Employers in the St. Louis and Memphis areas, according to recent surveys, anticipate slower growth in total employment over the next three months. Less than 20 percent of the employers polled plan to hire additional workers in that period, a similar proportion expect some staff reductions, while over 60 percent plan virtually no net changes. Three months earlier, 27 percent of the St. Louis employers planned staff additions and only 7 percent expected reductions.

Consumer Spending

District retailers use words like "tremendous" and "fantastic" to describe their Christmas sales. One large chain reported December sales 38 percent above the previous December, and most stores reported gains in double digits. Most merchandise sold well, but the willingness of shoppers to invest in "big ticket" and high-quality items was particularly impressive. There was no need for panic price markdowns to move merchandise as in the previous year, and hence retail profits jumped more than

sales. After-Christmas sales were generally described as satisfactory, but year-over-year comparisons were lower than in December.

Manufacturing and Employment

Manufacturing activity continued to expand in the District during December and early January. Orders are up, backlogs are increasing, and some firms are implementing capital spending plans. Most capital spending continues to be directed toward productivity improvements, but some is for capacity expansion.

With greater production, employment has continued to rise. An automobile company increased its employment by 1,500 in early January, both to staff an additional shift and to reduce overtime payments. However, unemployment rates have shown only a slight decline in recent months as the labor force has also continued to expand.

Real Estate and Construction

Real estate sales and construction (adjusted for seasonal influences) have remained at high levels since November. One builder sold 15 relatively high-priced homes in the first week of January, which was beyond his expectations. Six other homebuilders reported heavy shopper traffic through display homes, and a major realtor said sales of older homes were strong for December and the first half of January.

Transportation

Several truck lines in the District reported improved business in December and early January; for one line, December was the best month in four years. Two railroads reported business up nearly 25 percent in December from the same month a year earlier, with gains in most general business lines. Barge traffic at the Memphis port has been gradually

increasing. On the other hand, one company owning 150 barges recently filed for bankruptcy. Barge traffic in the St. Louis area was adversely affected in late December and early January by the unexpected quick freezing of the Mississippi River further north, locking in many barges.

Agriculture

A large number of acres were planted in winter wheat despite the PIK program, and the crop appears to be surviving the cold weather. Early indications are that plantings of corn and soybeans this spring are likely to match those of the large 1982 plantings. As a result, sales of seed, fertilizer and herbicides are improving.

Finance

Commercial and industrial loans at large District banks declined on a seasonally adjusted basis during December and early January. Savings and loan associations have been making few loans to businesses, even though they have had authority to do so for more than a year. Two St. Louis area associations, however, have recently added additional lending officers and are aggressively seeking business loans. Most District associations have less than 1 percent of their assets in commercial loans, and even the aggressive associations are nowhere near the Federal limit of 10 percent in 1984. Nonetheless, these percentages have been rising and are expected to continue to rise as associations gain experience.

In general, the financial health of the savings and loan associations in the District has continued to improve. Several Louisville and St. Louis savings and loan associations, however, reported an increase in delinquencies on mortgage loans in December.

NINTH DISTRICT - MINNEAPOLIS

Strong holiday retail sales, which occurred despite the unusually frigid district weather, indicate continued growth in both consumer confidence and the economy. These sales have been accompanied by heavy consumer borrowing. Also despite the cold weather, the agricultural outlook, particularly in the livestock sector, has improved a little. Activity in the district's resource-related industries has improved as well.

Consumer Spending

All reports indicate consumer spending this holiday season was very strong and would have been even stronger if temperatures had not hit record lows. One large district retail chain reports that its stores experienced their best December nominal sales increase in ten years. Further, this nominal increase was mainly real, coming as it did at a time when inflation fell to a twenty-year low. A Minneapolis retailer reports similar increases, noting that winter apparel sold quite well. Our Bank directors report good sales throughout the rest of the district, too. Several retailers say sales dropped somewhat when temperatures dropped below zero. But some of them were surprised by a vigorous post-holiday demand, which came when customers--and their wallets--thawed out. Business at ski resorts has also been hurt by the intense cold, but it also improved when the weather did.

Motor vehicle sales continue to show the soundness evident in previous reports. Domestic car sales managers say that inventories of both cars and trucks were barely adequate at year's end. Sales were up last quarter,

especially sales of trucks. One firm's truck sales were reportedly 41 percent higher this December than last. Recreational vehicles are also said to be in great demand. Big cars and pickups are selling very well in South Dakota. Moderate to good sales are reported in southern Minnesota, Montana, and most of South Dakota. Furthermore, special promotions have not been fueling these sales; they instead reflect the favorable economic climate.

To finance this spending, consumer borrowing has been increasing at a good clip in nearly all of the district. A Bank director in rural Minnesota reports that consumer lending has been strong there lately, while another in South Dakota says that it has been fairly good at many banks. One large district retailer says that its credit sales have been rising, both absolutely and as a percentage of its increasing total sales. Another local retailer reports no problems with its credit accounts. However, consumer lending is still weak in the economically troubled Upper Peninsula of Michigan.

Agriculture

Overall, the agricultural picture has improved slightly in the last few months. Most of the heavy winter wheat plantings in North Dakota and Montana have adequate snow cover, although some fields have been whipped bare by high winds. If wheat production is as high as expected, though, the resulting low prices will depress farmers' profits. An agricultural implement dealer in Montana reports good sales and low inventories. Recent estimates show that the newly enacted Federal Dairy Diversion Payments Program will offer farmers between \$5,000 and \$15,000 each. But district Bank directors in dairy-intensive areas find it hard to accurately estimate the likely degree of

farmer participation in this program. Lending to dairy farmers has been relatively strong in some parts of the district. While a recent survey of agricultural lenders shows that farmers have been paying off their debts more quickly, a Bank director in South Dakota says that farmers' financial statements have not been as good as expected. Finally, while cattle prices have increased, extremely cold weather and high hay prices have made it difficult and expensive to keep cattle from losing weight. On balance, one Bank director is guardedly optimistic about livestock profitability.

Resource-Related Industries

Resource-related business activity has perked up recently. Renewed interest in lumber operations in western Montana is reported. While sales have fallen from their high point in 1983, stud prices rose 23 percent last year, and slow but steady improvement is foreseen this year. The pulp and paper industry is still performing well throughout the district. Due to favorable drilling costs, oil activity in North Dakota is trending upward. However, gas activity and coal production are not expected to pick up. Iron ore production is starting to pick up, though. A local taconite official thinks that production this year will exceed 1983 levels.

TENTH DISTRICT--KANSAS CITY

Overview. Economic activity in the Tenth District continues to show moderate improvement following a strong Christmas sales season. New car sales have increased somewhat in early January. Both retail inventories and materials inventories are being closely controlled. Lead times for materials inputs are beginning to increase. Housing sales slowed late in 1983, and the demand for mortgage funds at savings and loan associations is weak. Commercial and industrial loan demand has been increasing at commercial banks, and deposit growth is strong. Tenth District agriculture has apparently not suffered greatly from the severe winter weather.

Retail Trade. Most retailers report current dollar sales in 1983 from 13 to 20 percent higher than in 1982. Christmas sales were unexpectedly higher than in previous years for most retailers, although some stores were hurt by December's bad weather. Sales are expected to continue their growth in 1984. More than half of the respondents began clearance sales earlier than in the past in order to reduce inventories and remain competitive. Prices have been stable and are expected to remain so in early 1984.

Automobile Sales. Most auto dealers surveyed report significant sales increases in the first weeks of January compared to December's somewhat disappointing performance, which some attribute to harsh weather. No problems in obtaining financing for floor planning were reported. Loans are available for potential buyers although some dealers have suffered from reductions in low-cost captive financing. Inventories range from constant to slightly expanded. All dealers surveyed were optimistic about sales in 1984.

Purchasing Agents. Most purchasing agents contacted report steady to slightly increasing input prices through 1983. Agents are expecting increases

in major input prices in the range of 3 to 9 percent in 1984. Although few difficulties are being experienced in getting materials, lead times have increased and are expected to increase further. All respondents report inventory levels to be relatively lean but satisfactory. Stocks are expected to remain at or slightly above their current levels during 1984.

Housing Activity and Finance. Home builders report that housing starts in 1983 were way ahead of the previous year, while sales of new houses were moderately higher. A slight slowdown in sales was experienced in the last few weeks of 1983. Prices of new houses increased 3 to 5 percent in 1983. Virtually all home builders surveyed report fairly tight inventories of unsold houses.

Savings inflows at savings and loan associations are slightly higher than a year ago, but virtually all respondents report a weak demand for mortgage funds. Nearly all institutions surveyed indicate that mortgage interest rates are holding steady and will continue to do so for the next few months.

Banking. Loan demand at Tenth District banks increased in December, with the strongest growth in commercial and industrial loans. No declines were reported in consumer, agricultural, or commercial real estate loans, but a couple of institutions experienced declines in residential real estate loans. Total deposits were up in almost all surveyed banks. Virtually all categories of deposits increased or remained the same, with demand deposit growth the strongest. The prime rate ranged between 11 and 13.5 percent, with over 80 percent of the banks charging 11 to 11.75 percent. None of the respondents changed their prime rate last month and over 70 percent do not expect a change to occur this month. Consumer lending rates were also unchanged, and no change is expected this month.

Agriculture. Severe winter weather conditions in the Tenth District brought minimal livestock death losses, but there has been an absence of weight gains by feeder cattle in recent weeks. Although District bankers expect the extreme cold to have little impact on marketing of cattle, they are concerned about depleted stocks of hay in the event of more severe weather. The winter wheat crop in the Tenth District is in good condition with adequate snow cover apparently protecting the wheat from freeze damage. Wind erosion, normally a problem in parts of the District at this time of year, is virtually nonexistent despite adverse weather conditions. Anticipated end-of-year loan paydowns by farmers did not materialize, with little if any improvement expected in the near future. Bankers report some refinancing of troubled loans while a few large farm bankruptcies have occurred across the District. There has been some increase in Farmers Home Administration emergency loan applications by banks' farm customers, but processing delays prevent the assistance from being readily available. Many farmers appear to be carrying large stocks of corn in anticipation of price improvement. Sales of farm machinery and equipment across the District have been flat with no yearend upturn. Equipment manufacturers are not optimistic about increased sales of farm machinery and equipment in 1984.

ECONOMIC COMMENTARY

ELEVENTH DISTRICT—DALLAS

Economic recovery in the Eleventh District is continuing at a moderate pace, as strong performance in construction and several manufacturing industries more than offsets problems in agriculture and portions of the energy industry. Total manufacturing production is growing, with orders for nonelectrical machinery proving particularly vigorous. Commercial construction is relatively high for this time of the year, while the majority of residential construction remains in apartments and condominiums. Retail and auto sales continue to climb. A cautiously optimistic outlook for the oil field equipment industry exists. The recent wave of freezing weather resulted in large losses for Texas citrus farmers.

Recent District manufacturing experience varies greatly among industries but, overall, moderate growth has been occurring. The District is sharing in the increase in capital goods demand that has taken place across the country. Orders for nonelectrical machinery used in manufacturing continue a surge that prevailed throughout the fourth quarter of 1983. Heavy steel fabrication output is also rising. Raw steel manufacturers indicated a slight increase in orders over the last two months. A shakeout of inefficient producers, however, is likely because of heavy foreign competition and low profits. Aluminum production is running at nearly 100 percent of capacity, in response to strong demand from the auto, housing and appliance industries. Demand for chemicals and plastics

continues to grow only moderately, but producers are very optimistic about sales for the first half of 1984. Orders for semi-conductors continue strong with future increases in employment and investment for plant and equipment expected. Despite losses in 1983, some apparel manufacturers along the Mexican border are optimistic about 1984.

Drilling activity in Texas continues to respond positively to stable oil prices, but signs of weakness still exist in some portions of the District energy industry. On a seasonally-adjusted basis, the Texas rig count posted a fourth quarter gain of 19 percent over the third quarter. The rig count declined significantly during the early weeks of January, but much (and perhaps all) of the decline is seasonal. Given stable oil prices, industry analysts see gradual improvement in the demand for many types of oil field equipment. In Dallas, the office of a large oil exploration company just announced extensive layoffs of white collar workers. One respondent expects a significant decline this year in District oil field services employment.

Auto sales throughout the District remain strong. December's unusually cold weather may have prevented Dallas from posting its best year ever. Houston and San Antonio dealers indicated that low availability of cars hampered sales.

Retail sales in December proved above expectations in all major District cities but Houston. Most major cities reported double-digit increases in department store sales in December, compared with a year earlier, although Houston was up only 5 percent. A number of respondents said that demand for apparel and appliances has been particularly strong. Optimism concerning the first half of 1984 was widely expressed.

Commercial construction continues at a high level for this time of year. The paucity of office building construction in Houston is largely being offset by retail and light industrial construction elsewhere in Texas. Dallas' value of nonresidential permits for 1983 rose above the previous year's, but Houston's fell. Respondents expect Dallas' strength and Houston's weakness in nonresidential construction to continue in 1984.

The pace of residential construction is generally stable at an historically high rate, but significant declines in the overbuilt multifamily sector are widely anticipated. Although apartments and condominiums currently account for the majority of permits issued, single-family home construction appears to be on the increase.

Loan growth at District member banks on a year-over-year basis has been rising steadily since September 1983. That follows a period of deceleration which began in the first quarter of last year. Even so, the year-over-year rate of growth in loans remains well below the average for the first quarter of 1983 and for the second half of 1982. At large banks, growth in real estate loans is continuing at a very high rate, while business loan growth remains sluggish. Deposit growth at member banks slowed in every quarter of last year compared to year-earlier levels. Deposit data for December indicated that this trend of deceleration continued through year-end.

Total Texas agricultural cash receipts for 1983 through September were 5.5 percent higher than those for 1982, owing to higher crop prices. Prices paid by Texas farmers increased 3.2 percent. A spate of freezing weather resulted in a \$200 million loss to Texas citrus growers.

TWELFTH DISTRICT

In the Twelfth District the expansion is continuing at a rapid pace. Consumer spending during the Christmas and post-holiday season has been exceptionally strong, both at retail stores and automobile dealerships. Western homebuilding activity in November regained 1983's August peak and nonresidential construction spending has been rising as well. In the manufacturing sector, employment gains have been widespread and especially strong in such defense and capital goods industries as electronic equipment and missiles and space vehicles. Agricultural prospects are improving. Adjustable rate mortgages are gaining increased borrower acceptance and helping to sustain housing. Consumer loans are growing rapidly due to consumers' increased creditworthiness and optimism.

Consumer Spending

Consumer spending was extremely strong throughout the district during the Christmas holiday season, and buying apparently has remained strong in the post-holiday period, after allowance for the normal seasonal slowdown. The strength has been apparent both at retail stores and automobile dealerships. Major department stores in Southern California, for example, experienced an average 16 percent gain in sales in December over a year earlier. In Arizona, sales were up by a similar percentage. Even in Oregon, where the overall economic recovery has been lagging and weather was particularly severe, major retailers experienced year-to-year sales gains in December ranging from 12 to 18 percent. Stores have been discounting merchandise heavily and thus have been moving a large volume to attain these sales increases. In fact, due to their depleted inventories and optimism with regard to future sales, retailers are revising their inventory plans upward for the first half of 1984 -- although their attitude with regard to inventory building still has to be described as cautious. To finance their heavy expenditures, consumers have been

sharply increasing their installment debt. Nevertheless, financial institutions consider consumers' increased willingness to borrow as a positive factor affecting spending, since consumers do not appear to be overextended and delinquency rates actually are declining.

Manufacturing and Mining

Manufacturing employment has been rising rapidly throughout most of the district states, except in Oregon where the lumber industry has been cutting payrolls since August. Gains have been especially strong in the electronic equipment industry -- which has been experiencing rising defense, consumer and business demand -- and in the missiles and space vehicle category. California has been the location for most of this increased high-technology employment, but Arizona and Utah also have been experiencing rapid gains. The West's other capital goods industries -- including those that manufacture non-electrical machinery, trucks and aircraft -- also are experiencing a pickup in orders. In Washington, orders for commercial transport planes have risen so sharply since mid-1983 that aircraft employment is expected to stabilize or perhaps rise moderately in 1984 after falling by about 9,000 during each of the two preceding years. With the notable exception of the Pacific Northwest aluminum industry, employment in the West's energy and metal mining and processing industries has stabilized but not yet begun to rise significantly. The copper, coal and oil industries continue to suffer from weak prices and excess worldwide supplies. Overall, respondents report that manufacturers intend to add workers to their payrolls very cautiously in 1984 so as to realize continued rapid productivity growth and hold down the increase in unit labor costs.

Construction and Real Estate

Homebuilding activity has rebounded more strongly in the West than it has nationally. For example, Western housing starts in November regained the 1983-peak reached in August. Permits issued for new dwelling units in the region also rose more than nationally, suggesting that Western homebuilding activity in coming months will remain relatively strong. Sales also are reported to be holding up well, although housing prices are rising. Respondents attribute this strong housing market to buyers' increased acceptance of the newer adjustable rate mortgage packages which offer initial rates substantially below those of the current fixed-rate mortgages. Nonresidential construction spending also is picking up. The upsurge in retail sales is encouraging modernization and construction of retail stores. The high-tech firms, especially electronic manufacturers, are building new plants. The decline in office vacancy rates, and the availability of pension fund and insurance company financing, are encouraging developers to plan and start construction of new office buildings.

Agriculture

The agricultural sector is currently in the midst of its normal seasonal slowdown. Crop farmers throughout the district are optimistic about prospects for 1984, however. Grain farmers expect to benefit from the higher prices for wheat and cotton resulting from the Midwestern drought. California and Pacific Northwest farmers also expect higher prices and stronger demand for their citrus and other produce because of the freeze in Florida and Texas. They also are encouraged by the possibility that energy, interest and other production costs may only increase moderately. Farmers are concerned, however, that agricultural exports could fall again in 1984 due to the high foreign exchange value of the dollar and foreign imposition of trade barriers. Livestock producers experienced a decline in net income last year and current conditions are not favorable. The drought-induced

higher feed costs are forcing ranchers to slaughter their herds earlier than usual, increasing the availability of meat and reducing prices below year-ago levels.

Financial Institutions

The past few months have seen a significant increase in adjustable rate mortgages (ARMs) in most parts of the Twelfth District. Financial institutions have overcome borrower hesitancy with aggressive pricing and the inclusion of limits on potential increases in interest costs. Some are offering ARMs at differentials of up to 200 basis points under fixed rate mortgages, along with a below market rate of less than 10 percent for the first six months. Such pricing has opened up the market to those unable to qualify at the higher rates on fixed rate mortgages. The inclusion of caps on any future upward movement in rates also has contributed to buyer acceptance of ARMs, providing buyers at least a partial reduction in risk. The consumer meanwhile is showing signs of continued financial health, as evidenced by a sharp increase in consumer loans. In December, the amount of consumer loans outstanding (n.s.a.) at Twelfth District banks rose at an annual rate of 37 percent. The sharp increase in December boosted the annual increase in banks' consumer loans outstanding to 8 percent.