

SUMMARY OF COMMENTARY

on

CURRENT ECONOMIC CONDITIONS

BY FEDERAL RESERVE DISTRICT

August 1989

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***Summary**

Comments received by Reserve Banks from business and other contacts suggest that the nation's economy continues to grow slowly. Most Districts report slow growth in general merchandise sales, with strength in women's apparel. Auto sales are weak in a majority of Districts, although Dallas reports significantly stronger sales than a year ago. Overall manufacturing activity shows slow growth in several Districts and declining activity in some areas. Oil drilling activity has improved in recent months, although it remains at a low level. Demand for paper shows signs of weakening from high levels in some areas, while logging restrictions are limiting lumber production in several northern states. Farmers in many parts of the country expect good harvests, but weather problems are hurting production in some regions. Real estate markets and loan demand are strong or growing in some Districts, but weak in others.

Trade and Services

Most Districts report relatively slow growth in general merchandise sales. Several report that retailers are cautious and are reducing their orders for the remainder of 1989. Most report relatively weak sales of home furnishings, electronics, and appliances. Women's wear is a leading source of retail sales growth in many parts of the country. Texas retailers report "moderate to strong" growth in retail sales compared with year-earlier levels, but Philadelphia, Richmond, Chicago, and St. Louis report that sales for many retailers in their Districts were flat or down in real terms. Reports of inventories suggest that most stores have satisfactory stocks, although some unplanned increases were reported in the St. Louis District.

* Prepared at the Federal Reserve Bank of San Francisco and based on information gathered before August 1, 1989.

Auto sales are reported to be below year-ago levels in most parts of the country. Dealer inventories are accumulating to higher-than-desired levels in most parts of the country, and several Districts report that dealers' profit margins have fallen. However, car sales in Texas have increased sharply, with sales in Dallas up 13 percent from a year earlier.

Manufacturing

Reports on manufacturing industries vary considerably from one District to another. Boston, New York, and Cleveland report declining rates of growth in orders for some manufactured products, with no growth in some cases. Manufacturing conditions in the Atlanta District vary by product line, with chemical producers in Louisiana planning plant expansions. Nearly a third of manufacturers contacted by the Philadelphia bank reported declining activity, while half reported no change. Dallas and San Francisco report softening orders for electronic components. Chicago reports that orders for cutting machine tools, particularly from abroad, trail last year's levels. Richmond and St. Louis report declines in manufacturing activity. Some layoffs and plant closings associated with reduced auto production have occurred in the Chicago and St. Louis Districts, with further cutbacks anticipated. Reduced auto production, seasonal slowing, and reduced export demand have curtailed the demand for steel, according to manufacturers in the Cleveland, Chicago, and Kansas City Districts. Most Districts report that manufacturers' inventories are at satisfactory levels, although Kansas City notes efforts to trim inventories.

Agriculture and Resource-Related Industries

Conditions in the resource industries are mixed. Increased oil drilling activity has boosted demand for oil field equipment, although activity remains below last year's levels.

Strong foreign demand for lumber is buoying the lumber industries in the Richmond and Dallas Districts, but logging restrictions are hurting lumber producers in the Pacific Northwest and North Central regions. Accumulation of paper inventories were noted in Arkansas and in the Atlanta District. In contrast, orders to Dallas District paper manufacturers remain high and prices for paper products have been rising recently.

Farmers in many parts of the country expect good harvests, but weather problems are hurting production in some regions. Harvest prospects are reported to be good in the Richmond, Chicago, and San Francisco Districts, and in most of the Kansas City District. Heavy rains have hurt production throughout much of the South. Much of North Dakota is suffering from a drought which is expected to hurt wheat yields. Kansas and Nebraska wheat production is suffering from a plethora of weather and pest problems. Apple and grape producers in the West report declining sales which they attribute to concerns about food safety.

Construction and Real Estate

Construction and real estate market conditions are mixed. Strong activity is occurring in upstate New York, and in the Chicago and San Francisco Districts, with particular strength noted in Seattle. Exceptionally strong markets in California appear to have cooled off, although prices continue to rise. A slow rate of increase in activity is reported in Texas and in the Boston and New York City areas. Flat or declining activity is noted in the Richmond, Minneapolis, and Kansas City Districts. The recent decline in mortgage rates reportedly had a slight positive effect on markets in the Boston, New York, and Richmond Districts.

Financial Sector

The pace of lending activity varies considerably by region and by type of loan. Overall loan growth is reported to be strong in the St. Louis and San Francisco Districts. Demand for

FIRST DISTRICT-BOSTON

While most First District manufacturers report good year-to-year gains in sales and orders, half say that the pace of incoming business has slowed. Retail sales are generally weak and below expectation. Auto sales continue to decline and are significantly below year-ago levels. By contrast, demand for residential real estate has improved slightly since last month in response to falling interest rates and prices. Respondents agree that materials prices have peaked and that selling prices are rising modestly at most. They expect slow growth to continue and view themselves and their customers as very cautious.

Retail

A sample of First District retailers reports that recent sales are weak and below expectation. Reflecting a regional downturn in home sales, building supplies and appliances are moving especially slowly. But apparel is also soft, and consumers seem broadly cautious, spending less money per trip to the store.

Reported price changes range from no increases in building materials and electronic equipment to a 6 percent rise in hardware. One discounter lamented a lack of "bargains," as suppliers have avoided building excess inventory. Retail inventories also remain in line. Margins are under pressure, however, as overhead costs continue to rise and promotional and low-margin items make up an increasing share of sales. Retailers surveyed remain profitable, but earnings are below 1988 levels.

mortgage loans has softened in New York, while Chicago attributes its pronounced upturn in residential loan applications to lower rates and refinancing activity. Richmond reports mixed mortgage activity, with most reports of improvement attributed to refinancing. Demand for home equity credit and second mortgages is strong in the New York and Atlanta Districts, and increasing in the Kansas City District. Commercial and industrial lending activity is reported to be up in Chicago and Kansas City, growing at a slower rate in Philadelphia, and flat to down in Richmond.

Respondents were uniformly cautious about the rest of 1989, and several have lowered their expectations for sales and profits. Capital spending plans are generally modest, and staffing levels are projected to be flat to lower over the coming months.

First District auto sales are reportedly slightly lower than sales last month and significantly below year-ago levels. Although the extent of the year-to-year drop varies, some dealers report sales to be off as much as 50 percent. Layoffs have occurred, and inventories are building despite previous cutbacks in orders. While the summer is usually slow, dealers cite two reasons for the sharp year-to-year decline. First, they believe that economic uncertainty is reducing buyer confidence. In addition, the unusually long-term financing plans introduced a few years ago have extended the normal buying cycle. Consumers who usually buy a car every two to three years now find that their remaining car payments exceed their vehicle's trade-in value; thus, prospective buyers needing finance may delay new purchases. Many dealers expect the slowdown to continue until declining interest rates or "creative financing" entice buyers back to the showrooms.

Manufacturing

Most First District manufacturing contacts continue to report good year-to-year growth. Shipments and orders are 6 to 18 percent above year-ago levels at most surveyed firms. Nevertheless, half the respondents indicate that incoming orders are starting to flatten out. Contacts describe demand for products related to defense, autos, computers, and construction as relatively weak. One manufacturer said that the government is renegotiating contracts while auto makers are

cutting inventories. By contrast, respondents see demand from the commercial aircraft, paper, packaging, and food industries as more robust. Two firms mention strong export growth, but one sees weaker demand in Japan, its major market last year.

Manufacturers describe employment levels as little changed and wage increases as "noninflationary." Although several respondents report a softening in the region's labor markets, others see little change above the entry level. Inventories are closely monitored and are currently satisfactory. Contacts agree that input prices have peaked. Their own prices are reportedly stable or rising very modestly.

A majority of manufacturing contacts expect capital spending to be below last year's levels, although one-third project current outlays to be well above 1988 figures. Three optimistic firms have recently raised their investment plans. Investment programs include bricks and mortar as well as equipment.

Half the manufacturers surveyed expect business to slow somewhat further. The others see little evidence of a slowdown in their own order books. Nevertheless, they describe themselves as "watchful," lest declining confidence levels prove self-fulfilling.

Residential Real Estate

First District realtors report that residential sales have improved slightly from last month. They credit lower interest rates and prices for causing the modest improvement. Smaller homes continue to sell better than larger units, and sellers far outnumber buyers in the condominium market. Buyers appear very cautious overall, and realtors expect sales to maintain their current slow pace.

SECOND DISTRICT--NEW YORK

The pattern of developments in the Second District continued to be mixed across sectors. Some retailers reported sales well above plan, while others experienced demand that met or fell below targeted levels. Upstate New York reports on new orders, production, and general business conditions indicate some leveling off. Nevertheless, more respondents continued to report gains in these areas than reported declines. Office leasing activity in the District has maintained a moderately strong pace. The pace of homebuilding activity has been uneven across the District, and based on a survey of small- to medium-sized banks, demand for residential real estate credit has weakened.

Consumer Spending

Sales results at District department stores were mixed during June. While some retailers reported sales were well above plan, others experienced demand that just met or fell below targeted levels. Over-the-year gains in June ranged from 0.2 percent to 9.5 percent among District retail contacts. Women's and junior apparel, accessories and cosmetics continued to be in strong demand and men's departments showed some improvement from their earlier weakness. In contrast, home furnishings and appliances were generally weak. Partial results for the first half of July indicate some slowing may have occurred in recent weeks.

With the exception of one store which had stocks well above desired levels, department store contacts described their inventories as being in good shape. In one case, this was due to unusually heavy markdowns which were being continued in July.

Residential Construction and Real Estate

Homebuilding activity in the District has been mixed in recent weeks. A glut of homes in the resale market continues to be cited as a major deterrent to

homebuilding in downstate New York and northern New Jersey, but a slight pickup was noted as a result of lower mortgage rates. Many observers believe that existing home prices will need to be lowered considerably more before current owners can sell and "move up" to new homes. By way of contrast, homebuilders in several upstate New York communities are currently quite busy after an unusually rainy spring which slowed things down, and home prices continue to rise in response to strong demand. With regard to the outlook, projects have recently been proposed for 4700 new moderate income residential units in Brooklyn and 7000-10,000 units in Queens, and a survey in Monmouth County (N.J.) projects the need for some 33,000 new units to be built in that area over the next few years.

Office leasing activity has continued at a moderately strong pace since the last report as Manhattan's largest lease of the year was signed for space in a 40-story midtown building scheduled for completion in 1992. Vacancy rates declined in several parts of the District including northern New Jersey and Suffolk and Westchester counties (N.Y.). Rates moved higher in some other areas, however, including downtown Manhattan where downsizing or merging financial firms are adding to the available supply of office space.

Other Reports on Business Activity

June surveys of purchasing managers in Buffalo and Rochester suggest some tendency to a flattening out in general business conditions, orders and production with an increased majority reporting "no change" in these various categories. Nevertheless, improving conditions are still reported by substantially more firms than are reporting a deterioration. Noticeably fewer purchasing managers reported higher input prices in June. Concerning the outlook, both the monthly Rochester survey and a semi-annual survey by the Manufacturers Association of Central New York showed a large drop in the percentage of respondents expecting a further improvement in business conditions over the next three to six months.

June unemployment rates of 4.2 percent and 5.0 percent in New Jersey and New York, respectively, were again below the national average. Nonetheless, the growth in

Second District nonfarm employment has increasingly lagged the national pace since 1986. In large part this results from continued declines in manufacturing employment in the District. In addition, some nonmanufacturing industries are growing more slowly than elsewhere in the nation. As a result of this and other developments, much discussion is going on in government and private circles regarding what can be done for the region to maintain its competitive position.

Several new projects were announced or undertaken in recent weeks. In Mahwah, New Jersey, United Parcel Service broke ground for a computer and telecommunications center which will be part of a \$1.4 billion investment in its worldwide operations. In Monmouth County plans have been announced for two large mixed-use projects which it is hoped will revitalize an old resort area. Ground was also broken in northeastern New York for a \$50 million mall scheduled to open next year, and downstate plans were announced for a major expansion of the New Rochelle mall.

Financial Developments

Based on a survey of small- to medium-sized banks in the Second District, demand for residential real estate credit has softened. While interest in second mortgages remains strong, demand for primary mortgages is modest or falling. According to the bankers, adjustable rate mortgages still appear more popular than fixed-rate ones, especially those with first-year discounts. Several reasons were suggested for the softening of real estate loans. Some bankers said that the real estate market may have overexpanded and is now undergoing an adjustment period. Other reasons given were: continued uncertainty about the outlook for financial markets, relatively high interest rates, and the slowdown in the national economy. Most of the surveyed bankers characterized their local economies as strong, however, and reported that employment levels were very high. They forecast continued but slower growth in the future for their communities. In general, the respondents were not worried about inflation with many stating that its current rate is not high enough to warrant concern. Most anticipate that inflation will continue at relatively moderate rates during the next year.

THIRD DISTRICT - PHILADELPHIA

Economic activity in the Third District is easing, according to indications from businesses surveyed in July. Manufacturers reported a drop in business for the month. Retailers said sales were flat compared to last year and auto dealers indicated sales were running below the year-ago pace. Bankers said that loan growth for the second quarter eased from the first quarter's pace and appeared to be slowing further in July. Despite the slackening pace of business, employment in most industries remains healthy. Many firms indicate they are raising wages for entry-level employees in the face of a shortage of qualified workers; however, there are not widespread plans to boost payrolls further.

Looking ahead, the consensus opinion in the Third District business community is that business will be steady to slightly slower for the rest of the year. Manufacturers expect activity to stabilize at about its current pace. Retailers expect real sales in the second half to run about even with or slightly below the rate of the same period last year. Auto dealers anticipate a further decline in sales but not a substantial drop-off. Bankers expect loan growth to slacken as the economy slows somewhat and as banks tighten credit standards for real estate lending.

MANUFACTURING

Manufacturing activity in the Third District showed signs of slowing in July, according to companies polled during the month. Nearly one-third of the manufacturers surveyed said activity was declining, while half reported steady business, and the rest indicated some improvement from June. Firms in nearly all the goods-producing industries in the region contacted in July indicated that business was off from June.

On balance, area firms were receiving fewer orders for their products in July than they did in June, and order backlogs were declining significantly as local companies stepped up shipments. Overall, area manufacturers said inventories remained level, with little change since April. Measures of employment were mixed: area firms were adding marginally to payrolls in July, but they were trimming the workweek. Industrial companies reported paying higher wages for new employees, both production workers and professional personnel. On the price front, area manufacturers continue to report more increases than decreases; however, the incidence of price hikes--for either inputs or outputs--appears to be declining.

Looking to the future, the balance of opinion among Third District manufacturers is that business will stabilize at about its current pace for the rest of the year. They expect new orders to run at a steady rate into the beginning of next year, but they anticipate further declines in order backlogs. Despite signs of slower business, area firms intend to maintain current employment levels and working hours, and they plan to boost capital spending, on balance, over the next six months.

RETAIL

Third District retailers contacted in July said sales for June and July were about even with the year-ago pace, in dollar terms. Merchants say women's apparel is selling above last year's rate, while appliances and other big-ticket items are weaker. Discount stores are achieving somewhat better results than other types of stores, and merchants describe shoppers as very price-conscious and selective with regard to the quality of merchandise they are buying. Nearly all store executives contacted in July said inventories were at planned levels. Many retailers report they are having difficulty finding entry-level employees although plans to increase staffing do not appear to be widespread.

Overall, retailers say real sales in the second half of the year will probably run about even with or slightly below the same period last year. Many merchants are trimming orders for fall merchandise although womens' apparel retailers are preparing for continued improvement in sales.

Third District domestic auto dealers contacted in July said both unit and dollar sales were running slightly below the pace of last year. Foreign auto dealers are achieving somewhat better sales (in unit and dollar terms) than they did last summer. All dealers report a continuing squeeze on profit margins due to higher car and parts prices from manufacturers and rising costs for financing inventories. Locally, domestic car dealers report inventories ranging up to twice desired levels.

FINANCE

Total loan volume outstanding at major Third District banks in early July was approximately 9 percent above the year-ago level, as the pace of growth in lending continued to ease from the rate set in the first quarter. Growth in business and consumer lending has slowed significantly in recent months. Real estate lending has remained on a strong upward trend during this same period but bankers contacted in late July said they have been booking less real estate credit in recent weeks compared to the buildup in real estate loans earlier this year.

Third District bankers generally expect loan demand to weaken in the second half in all credit categories in response to slower economic growth and tightened credit standards, especially for real estate loans.

In general, bankers indicate that deposit growth is in line with asset expansion plans, but net interest margins are under some pressure because loan rates have declined while relatively high rates are still being paid on certificates of deposit booked earlier this year.

FOURTH DISTRICT - CLEVELAND

Summary. Fourth District panelists generally do not expect a cumulative decline in economic activity this year, although a few believe real GNP could decline this quarter. Many also believe that a soft landing will not reduce the core inflation rate. They expect sluggishness in consumer spending to continue this half. Traditional capital goods producers are still operating at high levels, although softening in some industrial markets is occurring. Also, steel activity is easing. Still-lower interest rates are expected to revive overall economic activity.

Output and Inflation. The consensus view among District respondents is still that real GNP growth will average about 1% to 1.5% over the next few quarters. Nevertheless, a few believe that the odds for a recession have increased in recent weeks. They expect that real GNP will either slightly increase or decline this quarter, but do not expect a cumulative decline in overall economic activity. A few others still believe that real GNP growth will average about a 2% annual rate this half.

Most of the respondents doubt that a soft landing will succeed in reducing the inflation rate. They expect that inflation will remain sticky in a 4.5% to 5% range, even though the growth rate of real GNP is expected to be below the growth rate of potential output for the next several quarters. Most expect that inflation in the second half of 1989 will be less than in the first half because of improving supplies of farm products and energy. An

energy economist expects petroleum prices will ease in the second half, and that crude oil prices will fall to the low end of an \$18 to \$20 per barrel range. All but two respondents believe that a 4.5% inflation rate is too high and are concerned that further easing in interest rates might revive economic growth and fuel accelerating inflation.

Consumer Outlook. Producers of consumer goods and retailers generally expect continued sluggishness in consumer spending during the second half. Some expressed a view that the slowdown in consumer spending in the first half was not an aberration, and that continued slow growth in the second half will lead to extensive financing incentives by auto producers. An auto producer expects domestic new car sales to fall to about a 6.5 million annual rate this half, and a tire producer expects a relatively flat volume of sales and production of tires.

A major retailer expects real consumer spending will increase at about a 1.5% annual rate this half, and that more "specials" will be offered in order to stimulate sales.

A major appliance producer expects sluggishness in consumer spending for major household goods in the second half in response to the softening in housing. He also noted no favorable consumer response yet to the decline in mortgage rates.

Capital Goods. Traditional capital goods producers report continued high levels of production for most types of machinery and equipment, although easing in orders has occurred in some industrial markets. Demand from the electric utility industry shows no letup, lead times have not changed much,

and prices are holding firm. Demand for some types of standard industrial equipment has softened, possibly because of seasonal factors. A producer of small motors expects that second-half business will not be quite as strong as in the first half. He expects that even with a real GNP growth rate of 1% to 2% over the next few quarters, capital goods will grow at twice that rate. Bearing orders from some capital goods producers, especially machine tool builders, have slowed, and the number of bearings still on allocation has shrunk.

Steel producers foresee a larger than seasonal decline in their business during the third quarter, mostly because of production cutbacks in the auto industry. They believe that the boom in steel is over. Flat-rolled steel products remain on allocation by at least one major producer, although conditions are not as tight as they were earlier this year. Another producer removed all steel from allocation. Second-half steel shipments and production are expected to soften from the first half.

Financial Conditions. Bank and financial economists expect further declines in interest rates this summer. Lower rates so far have not had an effect on loan demand, although most lending rates have not fallen much. However, a bank economist expects that lower mortgage rates, now common at about 9.5% for a 30-year fixed-rate mortgage, will soon begin to stimulate demand for mortgages. Lower interest rates later this summer are expected by some of the economists to revive economic growth in a 2% to 3% range. The recent surge in demand deposits was described by one bank economist as due largely to rebuilding of compensating balances by their business accounts.

FIFTH DISTRICT-RICHMOND

Overview

After moderating for several months, growth in the District economy softened further in July. Activity was flat in some sectors and actually declined in others. Retail sales were weak on balance, and manufacturing activity decreased. Home sales were below their earlier level, and tourism and port activity were mixed. On the financial front, loan demand was generally weak. Despite the current sluggishness in their sectors, manufacturers, retailers, homebuilders and bankers are optimistic that their own business activity will increase in the next six months. Agriculture and forestry offer the brightest prospects for growth, as a good season will likely boost farm receipts, and strong foreign demand is supporting lumber sales and prices.

Consumer Spending

About half of the retailers responding to our regular mail survey reported lower sales in July while only a few reported increases. Most retailers, however, expect their sales to rise over the next six months.

Retailer responses to our July survey were generally unchanged from May. Most car dealers again indicated slower sales, while department store volume increased slightly, as sales of big ticket items apparently improved.

Manufacturing

District manufacturing activity, which has been weakening in recent months, fell in July according to our regular mail survey. Reports of

declines outnumbered reports of increases in shipments, new orders, and unfilled orders. Export orders, employment, and the length of the workweek were largely unchanged. Inventories of materials evidently declined, while inventories of finished goods were unchanged. Prices for both finished products and raw materials apparently continued to rise, but at a slightly slower rate than was reported in May.

District manufacturers continue to be more optimistic about prospects for their own businesses than for general business activity in the nation. Respondents who expect increases in sales and unfilled orders in the next six months slightly outnumbered those who expect declines. The majority look for employment and the workweek at their respective plants to remain at current levels. Only one District producer in five, however, expects the general economy to improve over the next six months, while two in five expect it to decline.

Expectations of Inflation and Foreign Trade

In their responses to our July mail surveys, District manufacturers and retailers also indicated their expectations about U.S. prices, wages, exports, and imports. As in our previous survey, most respondents expect the rate of increase in prices and wages to stabilize or slow in the next six months. Slightly more July than May respondents look for the trade deficit to widen. The July survey results are summarized below.

	<u>Expecting Rate of Increase to:</u>			<u>Expecting a Decline</u>
	<u>Rise</u>	<u>Slow</u>	<u>Not Change</u>	
Prices	9%	31%	53%	7%
Wages	10%	19%	71%	0%
Exports	14%	22%	49%	14%
Imports	18%	29%	46%	7%

Ports

Reports received from the three major District ports--Hampton Roads (Norfolk), Charleston, and Baltimore--show that import volume was unchanged in July from June. The export picture was mixed, with shipments higher at Charleston and Hampton Roads but about the same at Baltimore. Compared to a year ago, increases in export activity exceeded increases in import activity, and representatives expect this trend to continue during the next six months. At Hampton Roads, the largest coal port in the nation, coal exports have reportedly been at normal levels in recent weeks.

Financial

According to our telephone survey of financial institutions, commercial and industrial loan demand was generally flat to lower in July. Mortgage demand was mixed with half of those surveyed reporting higher demand and the other half lower demand. Of those reporting higher mortgage demand, most attributed the strength to refinancing activity. Auto loan demand was sluggish at banking institutions, and respondents felt that more dealer financing was the cause. Many bankers expect loan demand to firm once borrowers perceive that interest rates have bottomed out.

Housing

Housing activity in the District was reported as mixed overall, but still well behind last year's levels according to our telephone survey of builders and realtors. The suburban Washington, D.C., market has been especially slow recently, primarily because of large inventories of higher-priced homes. Most respondents noted that lower mortgage rates had begun to have a small positive effect. Several respondents said reduced

mortgage rates had not resulted in heavier customer traffic but had allowed buyers to purchase more expensive homes.

Tourism

District hotel and motel representatives contacted by telephone indicated that tourist activity was mixed compared to last summer. About half reported that bookings were higher than last year at this time, which they attributed to more repeat customers, better convention business, and better weather. About one-third reported lower bookings. Our contacts gave mixed views on prospects for tourism for the rest of the summer, 40 percent expect increases, and 33 percent expect decreases from last year.

Agriculture

Abundant rainfall and moderate temperatures throughout much of the District during July have raised optimism that fall yields will be strong. The apple crop is in generally good condition. The harvest of early peaches has begun, with that crop also rated as good.

The District's lumber industry has apparently benefited from strong foreign demand that has largely offset the weakness in domestic demand due to softness in construction. Foreign buyers of lumber were said to have bought all grades and to have paid top prices.

SIXTH DISTRICT - ATLANTA

Overview: A number of contacts at businesses headquartered in the Southeast have revised their expectations of business activity downward in light of either reports of a general economic slowdown or an actual slowdown in their sales. Few have indicated that they were going to change their capital investment plans as a result. Businesses related to the housing and construction industries have reported significant slowing, and the trucking industry also reports that business is down. Recently, oil and gas exploration has been showing some strength, and this has in turn been helping suppliers to this industry. There are a few reports of localized pressure on wages, particularly for unskilled workers. Input prices are being reported as stable, and in a few cases, falling slightly.

Reports of Business Activity: Although economic activity continues to expand in the Southeast, several areas of softness have become apparent. The slowdown in residential, office, and retail construction continues, and the effects are now being felt in several related industries. A furniture retailer notes that sales have slowed recently and that he expects some further slowing. A supplier of building materials reports that sales in Florida are down and that his firm is introducing lower-priced materials for cost-conscious contractors. Some slowing in the paper and pulp industry is also apparent. Several contacts report that order backlogs have decreased recently. A warehouse operator reports that most goods continue to move through normally but certain items, especially paper goods, are said to be accumulating. The transportation and freight industry is reporting a general slowdown in business. Several large trucking firms report that their volume of shipments has decreased, in some instances dramatically. Two operators, one in Florida and the other in New Orleans, note that shipments of building materials have been off substantially. Although rail sources have not revised their business expectations downward any further, truck operators report that in general their outlooks have been revised down recently.

Several industries, however, have stated that their business is starting to improve. Oil and gas drilling is up. The increase has been strongest in natural gas exploration in the Gulf, but one contact says that the recent stability in oil prices has begun to restore some confidence among oil drillers. This is showing up in increases in orders for drilling equipment from Louisiana suppliers. A manufacturer of air conditioning equipment reported that his firm has been running close to capacity recently with no sign of slowdown anticipated. He attributed the strength in orders to remodeling and replacement rather than to new building construction. Producers of communications and electronic equipment in Georgia state that business is still strong and that they do not expect much, if any, slowing in their industry. The one weak spot in communication and electronic equipment sales has been in federal government orders.

Several financial institutions pointed out that because of growth in home equity lines of credit, consumer loans have increased recently. Two lenders noted that there has been some increase in ARM mortgage lending, although they remain somewhat cautious in their outlook. A few other bankers noted, however, that borrowers seem to have become more hesitant to take out new loans in light of general reports of a slowing economy. Auto loans are widely reported being down.

Wages and Prices: Reports of tight labor supplies and greater than expected wage pressures are rare in the Southeast. Five percent seems to be the upper limit to reported wage increases, although the cost of benefits, particularly medical care, is still increasing more rapidly than wages. A hotel chain operator reports that it is still difficult to get workers at or slightly above minimum wage and sees few signs of slowing business activity. A spokesman for a ship repair yard in Louisiana said that pressures on crew wages and charges for repair work have been building with the increased demand for offshore drilling. Several manufacturers said that materials prices have been essentially steady. Rolled steel and copper prices have remained constant for the past few months, and prices for some grades of paper have actually come down recently.

Feed costs have remained stable owing to recent rains in the Midwest, although District fertilizer demand and costs have fallen because heavy rains in the Southeast have reduced planting substantially.

Inventories and Investments: Even though several businesses reported that they had revised their economic outlook down, few have reported any changes in planned inventories or investment plans. A furniture distributor intends to reduce already low inventories because of expectations of further slowdowns in sales. On the other hand, several chemical producers in Louisiana announced plant expansions recently. A number of automobile parts producers in Tennessee have recently announced large expansions or plans to construct new plants altogether. The firms produce parts for domestic auto makers. A paper and lumber producer noted that several new plants currently under construction will bring substantial capacity on line in the next two years during a period in which he is now expecting slowing sales. An assembler of offshore drilling equipment and rigs has opened a previously idle factory.

SEVENTH DISTRICT--CHICAGO

Summary. Several reports suggest slower growth, overall, in economic activity in the District, with declines in some sectors. Chicago purchasing managers indicating rising production continued in June to outnumber those noting declines, though by a smaller margin than in earlier months over the past two years. Orders are showing no growth, however, and backlogs are falling. Milwaukee purchasers say production and orders were about unchanged in June and backlogs were beginning to soften. Manufacturing employment in District states, seasonally adjusted, peaked in January. A number of manufacturers in the region note a slowing in activity or orders at their firms--slower growth for some, declines at others. Real estate markets, both nonresidential and residential, appear to be picking up in response to lower interest rates. Consumer spending continues sluggish. Favorable weather has enhanced crop prospects.

Motor Vehicles. Though auto production cuts through the third quarter have been limited, preliminary indications are that automakers will reduce output more substantially in the fourth quarter. Sales incentives have been enhanced further in an effort to sell excess inventories. Expectations for 1990 sales have been revised downward. A Big Three automaker announced a major cost-cutting program, involving substantial reductions in white-collar staffing. Sales of larger trucks are showing varying degrees of softness, with deliveries of medium-duty trucks below last year and orders for heavy trucks easing though deliveries are higher. An Indiana truck trailer manufacturer recently halted second-shift production and laid off 350 workers.

Machinery. Markets for a variety of types of equipment continue to expand, but there appear to be an increasing number showing indications of weakness. Although shipments of metal-cutting machine tools this year have been sharply higher than in

1988, orders have trailed last year, particularly from abroad, and backlogs have fallen since February. Smaller pieces of earthmoving equipment used in residential construction continue weaker, as has been the case for many months. Softening has been noted recently in marine and recreational vehicle markets. A maker of industrial machinery has seen weakening in orders. On the other hand, a producer of electrical controls and power supplies used in a wide range of types of industrial equipment expects continued strength in these markets through year-end. Markets for mining equipment are strong, including robust demand from abroad. Road maintenance equipment buying is also strong. Demand for agricultural equipment continues to improve.

Construction. Lower mortgage interest rates reportedly are generating a pronounced upturn in inquiries and loan applications, both commercial and residential. Part of this increased activity reflects refinancing by current property owners, including shifts from adjustable-rate to fixed-rate loans. Part is expected to give rise to added construction. Thirty-year fixed-rate residential loans are being offered in the Chicago area generally in a 9.5-9.75 percent range, down from 10.75-11 percent common in March. Measures of construction activity continue stronger in this part of the country than nationwide. Year-to-date shipments of portland cement, for 5 months, were 5 percent higher in the East North Central states and 1 percent lower in the nation. Year-to-date gypsum board shipments were 8 percent higher than a year earlier in District states, against only a 4 percent rise nationwide. Nonresidential and residential construction contracts are above a year ago in District states and lower nationwide, suggesting relative strength in future construction activity in this region.

Steel. Demand for steel has slowed, but perhaps mainly seasonally. There appears to be an unusual concentration of shutdowns among the steel industry's customers in July. Unwinding of inventories accumulated earlier, to guard against

the risk that negotiations over expiring labor agreements at steel mills might have been unsuccessful and led to strikes, is also thought to have contributed to slackened demand for steel. Planned auto production and related demand for sheet steel is strong again in August, following July shutdowns, but production cutbacks expected at automakers later this year would curtail this market for steel. Construction markets for steel were strong in the first half, and additional projects are coming up for bidding, but some other projects have been delayed for various reasons. Machinery markets for steel, as noted above, are turning increasingly mixed. Steel exports in 1989 have been up sharply, from a very low level, while imports have declined.

General Merchandise. A large retailer noted weakness in sales of durables, particularly furniture and draperies. Appliance sales are holding up a little better. Sales growth in nondurables, mainly apparel, has increased after weakness last year. A June survey of a large number of small Michigan retail stores indicated that year-to-year sales increases were only about keeping pace with the rise in prices.

Agriculture. Widespread rains and cooler-than-normal temperatures since mid-July led to enhanced harvest prospects and lower crop prices. Since the favorable weather occurred during the critical pollination period, corn yields this year are now expected to equal, or exceed, the average for non-drought years. Prospective soybean yields, while benefiting from rapid plant growth recently, still hinge heavily on weather patterns during the pod-filling stage in August.

Preliminary results from our latest survey of District bankers suggest that farmland values continued to edge up in the second quarter, but at a slower pace than in earlier periods. The second quarter rise of 1 percent compares to gains of about 3 percent in each of the previous three quarters. The slowing was particularly evident in Illinois and Iowa where lingering drought concerns prevailed throughout the second quarter.

EIGHTH DISTRICT - ST. LOUIS

Summary

A gradual reduction in the growth rates of employment and consumer spending has continued in recent months and led to layoffs in several durables manufacturing industries. Nonresidential construction contracts rebounded in the second quarter, but residential contracts were flat. Although recent rains have helped to ease drought conditions in northern Missouri, excessive rainfall has caused production losses in other parts of the District.

Employment

Average District payroll employment in the three months through May was virtually unchanged from the previous three-month average, following moderate growth earlier in the year. Employment growth slowed in services and wholesale/retail trades in recent months while employment declined in construction and manufacturing. Compared with a year earlier, May payroll employment was up 1.4 percent in the District while rising 3.1 percent in the nation. There has been little evidence of excessive wage pressures. In Arkansas, for instance, nominal hourly wages for manufacturing workers were only 0.7 percent higher in May than a year earlier.

Manufacturing

District manufacturing employment in the March-May period fell at a 0.6 percent rate compared with the previous three months, with employment declines in most industrial sectors. Sluggish sales of light trucks prompted a one-week closure of a Louisville assembly plant, the first such

shutdown in six years. Weak sales of refrigerators and computer peripherals led two Arkansas producers to announce major layoffs. Rising worldwide inventories of coated paper, used in magazines, caused a major layoff of Arkansas paper mill workers. In a June survey of Missouri purchasing managers, 48 percent of respondents reported increases in new orders in the second quarter, a response slightly below that of a year earlier. Delivery lead times increased in the second quarter for 28 percent of respondents compared with 38 percent in the first quarter and 68 percent a year earlier.

Construction

Although construction employment continued to fall, the value of construction contracts rebounded in the second quarter, suggesting future strengthening. The value of District nonresidential construction contracts rose 23.2 percent in the second quarter, after falling at a similar rate in the first quarter. District residential contracts rose marginally in the second quarter (0.8 percent), returning to the level of a year earlier. Contacts suggest that recent mortgage rate declines have not caused substantial increases in homebuilding as consumers expect further rate declines.

Consumer Spending

Retail sales growth has weakened in recent months. Non-auto sales since May were 2-5 percent higher than a year earlier compared with 4-7 percent gains earlier in the year. Women's apparel and accessories are reported to be selling moderately well, but sales of men and boy's goods, and in most cases, of home furnishings and appliances, are weakening. While inventories are near desired levels at most outlets, some retailers in Arkansas report unplanned increases. Car sales generally have been

slow, with inventories remaining at high levels. Tennessee contacts report new car sales are slow, while used cars sales are moderate to strong.

Agriculture and Mining

Most District crops are in fair to good condition. Rains helped ease drought conditions in northern Missouri, although subsoil moisture and livestock water supplies remain deficient. Cotton, soybean, and tobacco growth is being hampered by excessive rains in the District's southern states. By limiting access to cutting sites, the rains have also reduced the supply of logs to some District paper mills. Compared with the same period last year, coal production fell 8.5 percent in the District and 3.4 percent in the nation in the six-week period through July 15. Sympathy strikes, industry-wide vacations and stockpile drawdowns affected the coal production figures during this period.

Banking

Total loans at the District's weekly-reporting banks grew at an 11 percent annual rate for the second quarter, somewhat higher than the 7.7 percent rate reported for the same period in 1988. Most of the overall growth can be traced to real estate loans (primarily nonresidential), which increased at a 24.7 percent annual rate, more than twice that for the same period in 1988. Consumer loans continue to be weak, growing at a 1.6 percent rate. Total deposits at these same institutions declined considerably during the second quarter, falling at a 2.5 percent annual rate compared with a 3.0 percent rate of increase for the same period last year. Weakness in business demand deposits and unusually large tax payments by households are cited as possible explanations for this overall decline.

NINTH DISTRICT--MINNEAPOLIS

Ninth District economic conditions have been mixed. While the Minnesota labor markets have shown signs of weakening, those in other states have not. Consumer spending has been fairly strong, but housing activity has been weak and automobiles sales have been flat. Conditions in resource-related industries have been mixed.

Employment

The district employment situation has been mixed, with some signs of increased unemployment in Minnesota. The unemployment rate in Minnesota in May was 4.9 percent, 0.6 percentage points higher than in April and 0.8 percentage points higher than in May 1988. The unemployment rate in the Minneapolis-St. Paul metropolitan area was 3.8 percent in May, unchanged from April and 0.6 percentage points higher than in May 1988. A director reports that turnover among employees was lower than earlier in the year and that it had become easier to hire employees in the last two months. A major manufacturer of electronics, control systems, and defense items headquartered in Minneapolis announced a restructuring which would eliminate about 4,000 jobs worldwide out of its current total of 78,000 employees. The 4,000 jobs include 300 that were already cut earlier this year from its corporate headquarters.

The unemployment rate in North Dakota fell to 3.7 percent in May from 4.5 percent in April and 4.6 percent in May 1988. The unemployment rate in South Dakota in May was 3.7 percent, a slight increase from the 3.5 percent rate in April and unchanged from the 3.7 percent rate in May 1988. The unemployment rate in Montana dropped sharply in May to 5.5 percent from 7.2 percent in May 1988, and in the Upper Peninsula of Michigan the unemployment rate

in April was 9.3 percent compared to 10.3 percent in April 1988. A director reports tight labor markets in Western Wisconsin.

Consumer Spending

Consumer spending on general merchandise has continued to be fairly strong. One retailer reports that sales in June were 14.2 percent higher than in June 1988. Some of the increase was due to opening of new stores; stores which were in operation last year had 6.1 percent higher sales in June than a year ago. Inventories remained at acceptable levels. A retailer reports that it reduced the number of sales promotions and sold more items at full price, thereby helping profit margins.

Automobile sales have recovered from low levels in the first quarter but have been generally lower than a year ago. A domestic manufacturer closed its truck-building facility in St. Paul for two weeks because of slack demand for pickup trucks. Dealers report sharply lower profit margins from a year ago. A director remarked that sales of recreational vehicles, boats, and campers, which are usually strong at this time of the year, "have completely dried up."

Housing activity has been sharply lower than a year ago. The number of new housing permits issued in Minnesota in May was 27 percent lower than in May 1988. The number of new housing permits issued in the Minneapolis-St. Paul metropolitan area in May was 32 percent lower than a year ago. June home sales in the Minneapolis-St. Paul area were 7.6 percent higher than in June 1988 but 7.3 percent lower on a year-to-date basis. The decline in residential construction was offset to some extent by an increase in nonresidential construction. The dollar value of contracts for future residential and non-residential construction in the Minneapolis-St. Paul area was unchanged in May from a year ago.

Tourist spending has been fairly strong. Contacts in Western Wisconsin report that the bed-and-breakfast business is booming and that many resorts are booked into the fall. The number of tourists visiting the Upper Peninsula of Michigan was reported to be 5 percent higher on a year-to-date basis than a year ago. A director reported that the number of tourists in Montana was 12 percent higher this year than the same period last year.

Resource-Related Industries

Conditions have been mixed in resource-related industries. North Dakota, which earlier was expected to have a record grain crop, has now declared a large part of the state as a drought area. However, the barley and sugar beet crops in North Dakota were reported to have been doing well. In western Minnesota, millions of honeybees were killed by spraying intended for grasshoppers, creating potential losses not only of honey but also of crops that bees pollinate. The mining industry was reported to be doing well throughout the district. A Colorado company plans to buy a bankrupt Minnesota mining firm and reopen an iron mine and a taconite processing facility in Minnesota by early 1990. Reports from the lumber industry were somewhat mixed with some signs of slackening demand and continued raw material shortages attributed to environmental problems.

TENTH DISTRICT - KANSAS CITY

Overview. The Tenth District economy continues to grow moderately. Overall retail sales continue to increase, although new car sales are weak. Increases in manufacturers' input prices are moderating and most materials are readily available. Retailers and manufacturers are both trimming inventories. Drilling activity, while variable from month to month, is below its year-ago level. Housing activity remains weak, with the effect of slightly lower mortgage rates not yet evident. Loan demand at commercial banks is flat to somewhat stronger for most loan categories. Lower yields likely held winter wheat production below average despite acreage increases.

Retail Sales. Most Tenth District retailers report sales increases over last year and over the last three months. However, merchandise sales are expected to be flat over the rest of this year and most respondents are reducing their inventories. Prices have been steady and are expected to remain so in the near future. Tenth District automobile dealers report weak new car sales over the last month. Dealers expect 1989 sales at or below 1988 levels and are trying to trim inventories.

Manufacturing. Most respondents report that input prices rose moderately over the last year. However, input prices changed little over the last three months, and only small increases are expected over the next three months. Although some lead times have lengthened, most materials are readily available. Nearly all respondents are trimming their inventories and plan to trim further in coming months. The inventory reductions reflect a recent build-up of excess inventories at some firms as well as long-term efforts to reduce normal inventory levels. Most Tenth District manufacturing plants are operating near full capacity. However, one steel manufacturer reports that

the recent strength of the dollar has hurt sales of U.S. produced pipe and rails. Several firms report problems in finding skilled labor.

Energy. Volatility in oil prices appears to be contributing to month-to-month variability in district drilling activity. Drilling activity also remains below year-ago levels. After falling in June to 225, the average number of active drilling rigs in the district increased sharply to 246 in July. Exploration and development activity, therefore, stands about 8 percent below the level of one year ago.

Housing Activity and Finance. District housing activity is down from a year ago, and most homebuilders report a slight decline in starts from a month earlier. New single-family home sales and prices have been steady and multifamily construction is virtually at a standstill. Most respondents expect little change in housing activity for the rest of the year.

Deposit inflows at district savings and loan institutions are slightly higher than a month ago but lower than a year ago. However, deposit inflows vary substantially from one institution to another. Some respondents attribute the recent behavior of deposit flows to uncertainty about the new savings and loan legislation. Although mortgage demand has been mixed, modest growth is expected in the near future. Nearly all respondents report slightly lower mortgage rates, but most expect stable rates in coming months.

Banking. District commercial bank respondents report more increases in loan demand than decreases. Increased demand is reported to be most apparent for commercial and industrial loans, home equity loans, and agricultural loans. Decreased demand is evident for home construction and commercial real estate loans. Demand for other types of loans is said to be generally unchanged. Among responding banks, loan-to-deposit ratios are about the same

as a month ago but somewhat higher than a year ago. At most banks, lending rates both to businesses and consumers have either fallen in the last month or are expected to decline in the near future. Deposit levels are generally the same or somewhat higher than a month ago. Demand deposits and small time and savings deposits have shown the greatest strength.

Agriculture. Winter wheat yields and quality vary widely across the district as the harvest nears completion. Some fields in Kansas and Nebraska were not harvested due to crop damage from cold weather, drought, insects, or hail. Wheat quality in Kansas was reduced by harvest delays due to late season rainfall. In other parts of the district, however, wheat yields and quality were average or above average. Overall, yields likely held winter wheat production below average despite acreage increases.

The district corn, soybean, and milo crops are generally in good condition. Across most of the district, recent rainfall has improved crop growing conditions, and good yields are likely if further timely rainfall is received. But in some areas, where planting was delayed last spring, crops could be threatened by an early frost.

Little expansion in district cattle and hog numbers is expected this year. District fed cattle prices remain strong, but cattle feeding margins are being squeezed by the high price of feeder cattle. High feeder cattle prices, in turn, are contributing to large profit margins for cattle ranchers. Although such profits would typically result in an expansion of cattle herds, drought-diminished feed supplies are likely to restrict herd expansion this year. Slaughter hog prices are higher, but little expansion in hog-feeding activity is likely because feeding margins remain near break-even levels.

ELEVENTH DISTRICT--DALLAS

The District economy is expanding at a modest pace. Manufacturing growth is slow. Retail sales continue to increase at a moderate to strong rate. Buyer incentive programs have helped to push up auto sales. Construction activity shows signs of a modest recovery. The oil and gas drilling upturn, which began in the first quarter, is still on track. Prices paid to District farmers in June were up slightly on a year-over-year basis, but down a little from May.

Manufacturing is growing slowly, but the recent performance of individual industries varies widely. Following declines that carried into the first quarter of 1989, demand for oilfield equipment has expanded lately, but sales have not pushed above year-earlier levels. Orders to District lumber producers are up and selling prices are said to be the highest in eight years. The increased demand is coming from areas outside the District. Part of the expansion in sales is said to stem from environmentally-related production problems elsewhere in the nation. Demand for stone, clay and glass remains sluggish. The major geographic exception is the Houston area, where increases in construction activity have stimulated purchases of building-related concrete and glass products. Orders to fabricated metals producers generally are rising, but firms that serve the construction industry say their sales are weak. Demand for primary metals varies widely among products but overall sales have shown little change recently. Electric and electronic equipment orders are softening. Semiconductor sales are down. Demand for lower-end computers is also weakening, but demand for upper-end products remains strong.

Apparel orders are growing from first-quarter levels. The demand for casual clothes is showing a particularly strong expansion. Food processing firms cite unexpectedly slow increases in sales. Some meat processors say they are hedging against expectations of higher input prices. Orders to District paper manufactures remain high and prices for paper products have been rising recently. Nevertheless, some paper firms are concerned about the rising value of the dollar. Chemical producers report that demand is declining slightly and productive capacity is increasing, while sales by petroleum refiners are up.

District retailers continue to show moderate to strong growth year-over-year. The expansion appears to be focused in department store sales. Apparel marketings are said to be strong and some firms also report increases in demand for consumer durables. Growth rates in retail sales are particularly high in south Texas. Although expansion also has been strong in Houston for much of this year, severe weather is said to have discouraged purchases during June.

Auto sales have been strong, but a significant portion of recent growth is said to be linked to temporary incentive programs. In June, auto sales in Dallas were up 13 percent from a year earlier. Expansion was also strong in Houston -- despite some declines in import sales. In San Antonio, growth has been somewhat weaker than in the District's two major cities.

District construction activity is beginning to show signs of a recovery, albeit a weak one. For the first time in almost two years, the value of total construction contracts has risen above a year earlier. Nonresidential building is the strongest component of construction growth, but

residential contract values are also increasing. Single-family homebuilding is expanding, but multifamily building remains at very low levels. Although office vacancy rates remain high, they have been declining in several of the District's largest cities.

Oil and gas drilling continues to recover. Although the District's rotary rig count remains below mid-1988 levels, it is nearly 30 percent above the January 1989 count. Respondents note that they are expanding drilling cautiously. Although they are pleased with reports showing strong worldwide petroleum consumption, they fear that Kuwait and debt-burdened Iran and Iraq could increase production significantly, causing prices to fall. Some producers say they are using revenues from higher oil prices to improve their balance sheets rather than to increase exploration.

Weather and prices are the chief concerns in agriculture. Increased soil moisture has raised crop and forage potentials in much of the District, but drought remains a concern in south Texas, the Panhandle, and New Mexico. Furthermore, rain has been accompanied by hail and flood damage in some areas. Excess moisture has become a problem in Louisiana and eastern Texas. In June, prices paid to Texas farmers averaged 2 percent above a year earlier, chiefly as a result of a 6 percent increase in livestock prices. Crop prices are 7 percent below a year earlier. Lower prices for corn, oats and grain sorghum more than offset higher prices for cotton, hay, potatoes and wheat. Both crop and livestock prices were slightly lower in June than in May.

TWELFTH DISTRICT -- SAN FRANCISCO

Summary

Overall economic conditions in the Twelfth Federal Reserve District continue healthy, although the pace of growth appears to have slowed from that seen earlier this year. Retail sales growth is satisfactory but not robust, with weakness in "big-ticket" items including automobiles. Manufacturing activity continues healthy, with strength in commercial aircraft and relatively slow growth in electronics. Most western fruit and vegetable producers are having a good year, although concerns about food safety have hurt sales of apples and table grapes. Log shortages in the Pacific Northwest have resulted in higher prices for lumber and wood chips. Construction and real estate activity continue healthy in most parts of the District, with some cooling noted in California, while the market is heating up in the Seattle area. Western bankers report strong loan demand, but slow deposit growth and stiff competition for deposits.

Business Sentiment

Twelfth District business leaders polled during July expect the economy's growth rate to slow during the next year. Almost three quarters of those questioned expect GNP to grow more slowly during the next year than its 2 1/2 to 3 percent historical rate. A majority of respondents foresee weakness during the next four quarters in consumer spending, business investment, and housing starts. Over half expect the inflation rate to fall during the next year.

Trade and Services

Sales at most department stores are reported to be satisfactory, not especially strong but strong enough that retailers are not particularly concerned. However, uncertainty about the future of southern Oregon's lumber industry has caused a slump in retail sales there. In recent months, District sales of women's apparel have improved, but the men's clothing market has

weakened. Weak sales continue for "big-ticket" items, such as electronics, furniture, and appliances.

Auto sales continue weak in most parts of the District, as rebate programs have not yet reduced excessive inventories to acceptable levels. One banker notes that many customers attracted by the discount programs cannot obtain financing due to their poor credit histories.

Wage trends in the trade and service industries are mixed. Retailers report some wage pressures, particularly at the low end, although one notes that these pressures are "manageable." A transportation services firm recently negotiated a new four-year contract that includes annual wage hikes of only 3 percent. However, wage pressures are intense in the health services. Nurses in several parts of the District are seeking double-digit wage increases in their new contracts, and strikes have begun at some hospitals.

Manufacturing

Bottlenecks in the commercial aircraft industry seem to have stabilized, as gradual progress is being made on increased output. A Seattle-area avionics subcontractor reports "extensive" pressure on wages, while in southern California, the downturn in defense spending is releasing workers and making them available to support commercial production.

Some softness in orders for electronic components is reported. One manufacturer reports that his sales grew by 15 to 25 percent in each of the past three years, but growth currently is running at only a 3 percent pace.

Agriculture and Resource-Related Industries

Most western fruit and vegetable producers are having profitable years. Pacific Northwest food processors report that they have already booked 1989 orders that exceed 1988 totals. Most frozen fruits and vegetables are now in short supply, with inventories of frozen

peas, green beans, and sweet corn the lowest in ten years. Prices of most processed vegetables have jumped 15 percent or more in the past year. Wet weather on the East Coast has hurt tomato production there, which has boosted California sales. However, grape and apple producers report declining sales which they attribute to concerns about safety. The inventory of unsold apples currently stands at a record 6.7 million boxes, double the amount a year ago.

Limited log supplies have boosted the prices of Northwest lumber products dramatically in recent months, despite reduced lumber demand. The price of a Northwest two-by-four rose 14 percent between the second quarter of 1988 and the second quarter of 1989. The reduced supply of timber also has doubled the price of wood chips, a key input to pulp and paper manufacturing.

Construction and Real Estate

Construction and real estate activity continue strong in most parts of the Twelfth District. In California, the frenetic pace of the past year appears to have cooled somewhat, as fewer sales involve bidding wars. As a result, homes are staying on the market longer and prices are rising more slowly.

At the same time, Seattle's real estate market has taken off, with reports of double-digit annual price increases. Construction activity also is booming, and some contractors are so busy that they are declining opportunities to bid for new work.

Financial Sector

Most western bankers report strong loan demand and slow deposit growth. Many institutions report that their profits have risen in recent months. However, several bankers note that stiff competition for deposits is forcing them to raise deposit rates, so they expect profit margins to fall.